FSM Development Bank

2016 Annual Report

Your Partner In Business

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LETTER TO THE SHAREHOLDERS:

Dear Shareholders:

On behalf of the Board of Directors, we are pleased to present the Annual Report for the year ended December 31, 2016 and the Audited Financial Statements for the FSM Development Bank for the years ended December 31, 2016 and 2015.

The year 2016 began with somewhat of a scare what with the El Nino drought, though moderate, affecting many of the FSM islands, especially the remote outer islands. The States and the National Government confronted the challenges brought on by El Nino by collaborating with each other and through assistance from disaster management agencies, donor partners, and others who could help, including FSM Development Bank.

The year 2016 was also quite an important year for the FSM, with many opportunities to progress the priorities decided by the Leaders of the ***Pacific Islands Forum*** when they met here in Pohnpei in September of 2016. The priorities discussed included climate change and resilient development, management of our fisheries and ocean, international and intra-regional trade and investment, disability, and gender equality. In connection with these priorities, FSMDB in 2016 began the Green Climate Fund (GCF) pre-accreditation process to hopefully access grants that will address many of these economic as well as social challenges in the region, including the ones discussed at the Pacific Islands Forum.

In terms of statistics, FSMDB in 2016 approved $22.8 MM for 463 loans. Business loans represented 87%, consumer loans at 11% and the remaining 2% for residential loans. The loan portfolio at year end stood at $28.4 MM; loans to the Tourism Sector constituted 23% followed by Wholesale/Retail at 17%, Real Estate development at 12% and Agriculture/Fisheries at 5%. A total of $16 MM was disbursed during the year. No government contribution or subsidies were received in 2016.

Despite what we view as challenges, especially given FSM's stagnate economy, FSMDB ended the year with a change in net position of $3.3 MM. The bank was able to generate enough in revenues from its core operations to cover its expenses. Furthermore, as in prior years, the bank again achieved an unqualified opinion from external auditors for the period under review.

There is much being done and much still to do. We are committed in fulfilling our mandate, which is to contribute to the development of our islands. We believe it is important that FSMDB continues to strengthen its balance sheet, improve earnings, and expand its financial, human, and technical resources and capabilities – all the while driving FSM's economic growth. As a commitment to the FSM people, we stand ready to collaborate with our stakeholders to advocate for and achieve our mission, our vision, and our goals.

Our achievements in 2016 could not have been done without our supporters. As we move forward, we want to thank our shareholders for their continued support and to the Board of Directors for their tireless efforts. We also want to acknowledge the dedication of FSMDB's management team and hardworking staff, who ensure that our Bank is operating and managed prudently. But most especially, we take this opportunity to thank our customers for allowing us to serve you as "Your Partner in Business."

Sincerely,

Anna Mendiola, President/CEO

John Sohl, Chairman of the Board

ABOUT THE BANK

Establishment:

The Federated States of Micronesia Development Bank (FSMDB) is a component unit of the National Government of the Federated States of Micronesia. It was established in 1979 by Public Law 1-37. The Bank opened operation in 1980 but lending did not start until 1982. In 1994, the enabling law that created the Bank was amended to reorganize the structure of the Bank into a corporation.

The primary function of the Bank initially was to provide financing to commercial businesses mainly in the FSM. Over the years, the Bank has added more programs to meet its strategic objectives and customer needs. In 2008, the Bank created its residential home loan program to help locals build their homes. In 2011, the Bank added a consumer lending revolving fund mainly to help generate revenue.

The FSM Development Bank is a key player in the development of the private sector in the Federated States of Micronesia that enjoys the confidence of the national and state leaders, its customers, regulators and stakeholders. FSMDB services and performance are comparable to the best-managed development financial institutions in the Pacific region.

The bank's headquarters is located in the State of Pohnpei, the capital of the FSM. The Bank also has branch offices in the other three FSM states of Chuuk, Kosrae and Yap and an online presence at www.fsmdb.fm.

Vision:

To be Micronesia's Premiere Development Finance Partner and Leading Catalyst for Transforming FSM Sustainable Development.

Mission:

To assist new and existing businesses to grow prosperously, creating jobs and producing economic vitality throughout our Nation**.**

Core Values:

- ***Customer satisfaction*** – through the provision of professional customer service;
- ***Teamwork*** – through mutual respect, cooperation, loyalty, commitment, collaboration and dedication;
- ***Integrity***– through observing the highest standards of ethics, accountability, transparency and to treat all stakeholders equitably;
- ***Inclusiveness*** – through undertaking economic development that enhances the life of all the people of FSM whilst sensitive to the protection of the environment and respectful of our culture and heritage; AND
- ***Excellence*** – through achieving the highest level of performance by continuously improving our skills and business practices.

SHAREHOLDERS:

The FSM National Government is the principal shareholder of the bank. It owns 98.8% of the outstanding shares. The States of Chuuk and Kosrae each own 0.9% and 0.3% of the bank's outstanding shares respectively. The States of Pohnpei and Yap are not shareholders but they are given representation on the Bank's Board of Directors to ensure that all the FSM States are represented.

Shareholders	No. of Shares	Amount
FSM National Government	3,197,883	$31,978,830
State of Kosrae	9,000	$90,000
State of Chuuk	30,000	$300,000
Total Shares	3,236,883	$32,368,830

BOARD OF DIRECTORS:

The Board of Directors is comprised of seven members. Six of them are elected by the shareholders. The seventh member is the President and Chief Executive Officer (CEO), who serves as the Ex-Officio to the board. Aside from the Ex-Officio, all board members serve a term of 3 years on a staggering basis. The composition and representation of the Board for the period under review were as follows:

*John Sohl – Pohnpei State Government – Chairman
*Peter Aten – Chuuk State Government – Vice Chairman
*Senny Phillip – FSM National Government – Member
*Florian Yatilman – FSM National Government – Member
*Alik Isaac – Kosrae State Government – Member
*Maria Laaw – Yap State Government - Member
*Anna Mendiola – CEO & Ex-Officio

FSMDB Governance and Management Training

MANAGEMENT:

FSMDB is managed by a senior management team comprised of a President/Chief Executive Officer (CEO), Senior Vice President/Chief Operating Officer (COO), Senior Vice President/Business Development Officer (BDO) and Chief Financial Officer (CFO). Assisting the senior management team is a Legal Counsel and Internal Auditor/Compliance Officer. For the period under review, the Bank's management team comprised of the following individuals:

President/CEO:	Anna Mendiola
Senior Vice President/COO:	Alik J. Alik
Senior Vice President/BDO:	Fabian Nimea
Chief Financial Officer:	Brandon J. Tara

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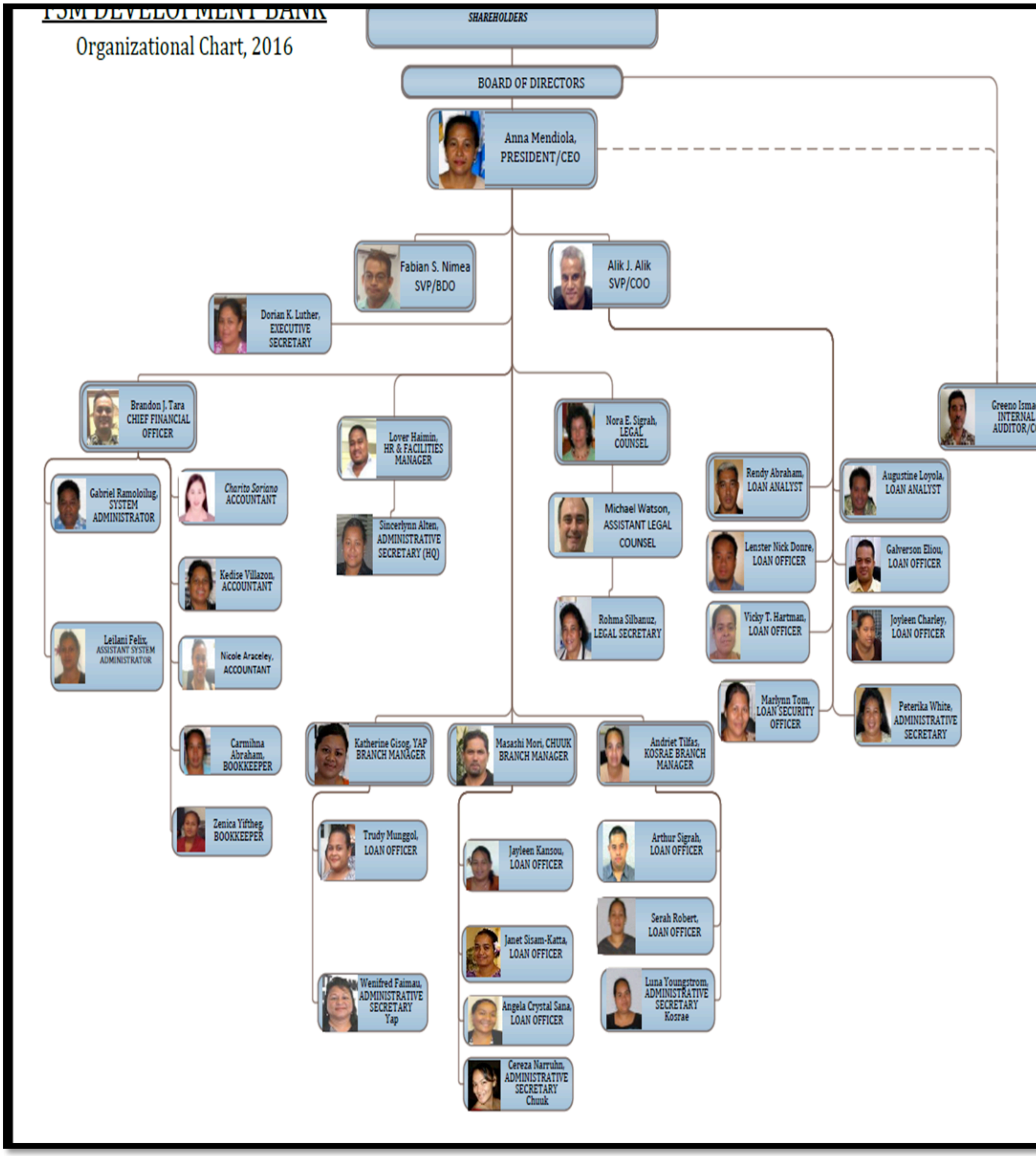
Legal Counsel:	Nora Sigrah
Internal Auditor/Compliance Officer:	Greeno Ismael

Appreciation to former staff and Board of Directors:

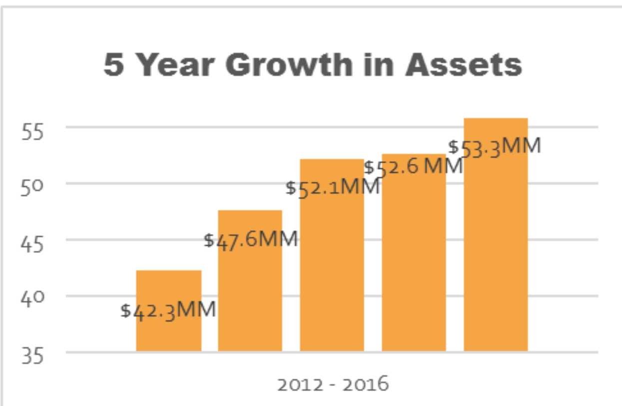
Heaps of thanks & gratitude go to members of our Board and employees who left the bank during 2016 for other endeavors. We wish them well.

FSMDB Organizational Chart:

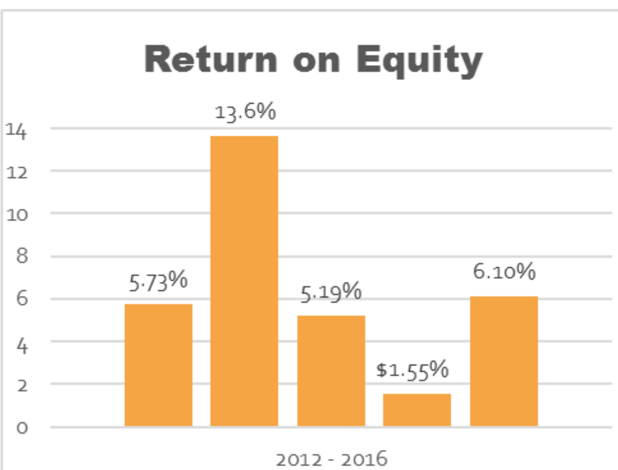


MANAGEMENT REPORT:

FSMDB continues to grow its assets by strategically ensuring that more than enough revenues are generated to cover operating expenses and surplus earnings are retained to increase assets. To ensure future growth and sustainability, within the last five years, the bank has grown its assets from $42 MM to $53 MM as illustrated below. Our loans receivable have also grown within the last five years. The bank in recent years has reduced its interest rates on its business loans from between 6% - 9% down to a range of $3% - 7%. In 2016, earnings from operations was positive and the return on equity improved compared to the prior year. Though our net income has fluctuated, FSMDB has for the past 5 years ended the year with a positive net position. The bank has also managed to improve collections and streamline expenses to maintain financial stability within the last five years.



The Bank's assets have steadily grown in the last five years.



The Bank's return on equity has remained positive the last five years.

BUSINESS DEVELOPMENT

2016 has been a great year for the Bank's operation as it strives to realign its purpose and strategies with its surrounding environment at all levels. As we have learned during the Pacific Islands Forum, risks and vulnerabilities have become more pronounced. Environmental degradation, climate change, sea-level rise, natural disasters, and other threats pose additional challenges to the ability of this nation to achieve sustainable development. The uncertainty regarding US Compact Economic Assistance post 2023 also reveals risks within the FSM economy and financial system, as well as the vulnerability of FSM to exogenous shocks.

The Bank established a Business Development arm of its operation with the objective of aligning the strategic elements of the Bank's business in such a way as to best support the fulfillment of its long-term purpose. To ensure strategic alignment, the Bank's people, culture, structure and processes have striven to adapt as the Bank's strategy itself shifts. Over the years, the Bank has made many exciting improvements in delivering its programs.

Hotel Operations in Chuuk & Yap

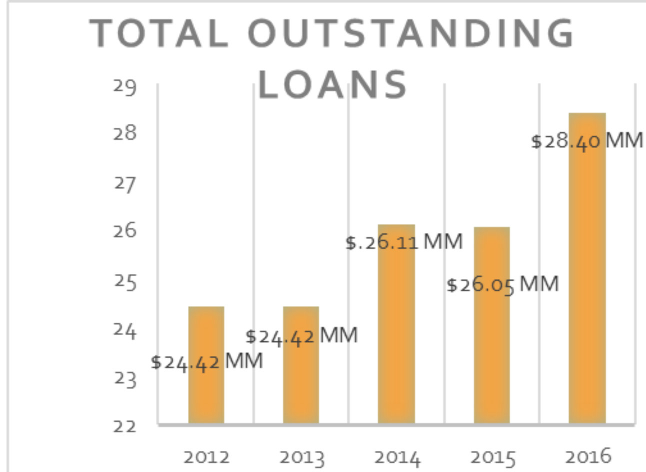
Lending Updates:

FSMDB's total loan portfolio or outstanding loans at the end of this reporting period totaled a little over $28 million. FSMDB has continued to grow its loan portfolio based on its approved strategic plan. More specifically, between 2012 and 2016, the bank grew its total loan portfolio by 17% from $24.0 MM in 2012 compared to $28.4 in 2016. For the period between January 1, 2016 and ending December 31, 2016, FSMDB approved 463 loans totaling $22.8 million.

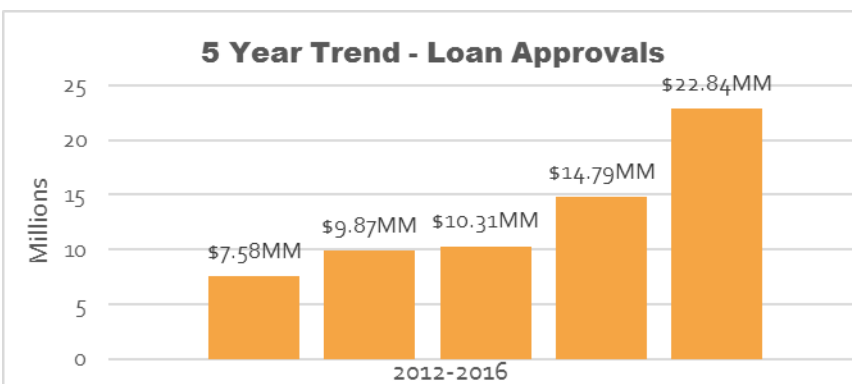
Business loans represented 87%, consumer loans at 11% and the remaining 2% for residential loans. The loan portfolio at year end stood at $28.4 MM; loans to the Tourism Sector constituted 23% followed by Wholesale/Retail at 17%, Real Estate Development at 12% and Agriculture/Fisheries at 5%. A total of $16 MM was disbursed at year end. No government contribution or subsidies were received in 2016.

Business and Housing Projects

2016 Approvals by Sector	Amount	Percent
Agriculture/Forestry	$ 5,577,163.00	24%
Services	739,828.00	3%
Manufacturing	8,952.00	0%
Real Estate	1,812,990.00	8%
Wholesale/Retail	387,735.00	2%
Tourism	3,106,785.00	14%
Transportation	1,149,477.00	5%
Consumer	2,520,187.00	11%
Line of Credit	7,186,200.00	31%
Residential	347,586.00	2%
Total	$ 22,836,903.00	100%



Apartment Complex, Chuuk



FSMDB's Development & Finance Training Institute (DFI):

Human resources development has always been an important component of the bank's strategic goals. As part of the bank's reform efforts, the Board of Directors approved in 2014 the establishment of a Development & Finance Training Institute (DFI). Since its establishment, the DFI has conducted several trainings for our borrowers, Board members and staff, employees from our local partners including the governments and component units, commercial banks and lending institutions, members from the private sector, and community members. In 2016, two trainings were held at the institute, namely, Professional Development Trainer's Training and Good Corporate Governance. We wish to thank our supporters and graduates for your continued confidence and support of FSMDB's DFI.

Certificates & Awards

Corporate Social Responsibility:

In addition to supporting FSM's nation building efforts through our many projects, our Home Energy Loan Program (HELP) for energy efficient homes, and our in-house Development Finance & Training Institute, FSMDB also believes in supporting the nation in civic and socially responsible activities that contribute to the development of the FSM. At FSMDB, we value people. We respect our environment. We promote sustainable economic development. As your partners in business, for many years now, we have been contributing and will continue to contribute to disaster mitigation efforts, local conferences and training/workshops, sporting events, cultural activities, and educational endeavors of many individual students through our scholarship program, to local schools, and other worthy programs.

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FEDERATED STATES OF MICRONESIA
DEVELOPMENT BANK

(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

FINANCIAL STATEMENTS AND
INDEPENDENT AUDITORS' REPORT

YEARS ENDED DECEMBER 31, 2016 AND 2015
(AS RESTATED)

FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

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INDEPENDENT AUDITORS' REPORT

Board of Directors
Federated States of Micronesia Development Bank:

Report on the Financial Statements

We have audited the accompanying financial statements of the Federated States of Micronesia Development Bank (the Bank), which comprise the statements of net position as of December 31, 2016 and 2015, and the related statements of revenues, expenses and changes in net position and of cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Deloitte.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Federated States of Micronesia Development Bank as of December 31, 2016 and 2015, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As described in note 1 to the financial statements, the Bank adopted GASB Statement No. 72, *Fair Value Measurement and Application*. As a result, the Bank has elected to restate its 2015 financial statements to reflect the adoption of this standard. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 4 to 6 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Financial Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The Schedule of European Investment Bank August 2010 Finance Contract Ratios on page 26 is presented for purposes of additional analysis and is not a required part of the financial statements. The Schedule of European Investment Bank August 2010 Finance Contract Ratios is the responsibility of 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 the 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, the Schedule of European Investment Bank August 2010 Finance Contract Ratios is fairly stated, in all material respects, in relation to the financial statements as a whole.

Deloitte.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated April 17, 2017, on our consideration of the Bank's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Bank's internal control over financial reporting and compliance.

Deloitte & Touche LLP

April 17, 2017

The following is a discussion and analysis of the Federated States of Micronesia Development Bank's (the Bank) financial performance for the fiscal year ended December 31, 2016.

Though the Federated States of Micronesia (FSM) economy remained stagnant in 2015, the year 2016 saw some improvement in the economy with some infrastructure projects and tourism activity due to high-level meetings such as the Pacific Islands Forum. The Bank in 2016 approved $22.8 million for 463 loans. Business loans represented 87%, consumer loans at 11% and the remaining 2% for residential loans. The loan portfolio at year end stood at $28.4 million; loans to the *tourism sector* constituted 23% followed by *wholesale/retail sector* at 17%, *real estate development sector* at 12% and *agriculture/fisheries sector* at 5%. In terms of loan approvals for 2016, over 70% was approved for loans in the commercial, tourism, and agriculture/fisheries sectors. A total of $13.5 million was undisbursed at year end. No contributions or subsidies from the government were received in 2016.

The tables below highlight the financial comparison from fiscal year 2014 through 2016. In 2016, the Bank implemented GASB Statement No. 72, *Fair Value Measurement and Application*. This Statement requires a new measurement approach to recording the Bank's equity investment in Bank of the Federated States of Micronesia. The implementation had a material effect on the assets and on the Bank's net position resulting in the restatement of fiscal years 2015 and 2014 (see Note 1 to the financial statements).

Summary Statements of Net Position

	2016	2015 (As Restated)	2014 (As Restated)
Assets:			
Current assets	$ 15,373,227	$ 15,822,373	$ 13,887,315
Noncurrent assets	40,547,568	36,791,039	38,307,488
Total assets	$ 55,920,795	$ 52,613,412	$ 52,194,803
Liabilities:			
Liabilities	$ 1,615,233	$ 1,627,103	$ 1,981,559
Net position:			
Net investment in capital assets	1,624,211	1,633,285	1,657,506
Unrestricted	52,681,351	49,353,024	48,555,738
Total net position	54,305,562	50,986,309	50,213,244
Total liabilities and net position	$ 55,920,795	$ 52,613,412	$ 52,194,803

At the end of 2016, the Bank had $1.6 million invested in capital assets. Please refer to note 5 to the financial statements for additional information concerning the Bank's capital assets.

In 2016, the lone long-term liability the Bank has with the European Investment Bank (EIB) was reduced to $1.2 million compared to $1.3 million in 2015. Borrowed funds represents only 2.0% of total assets. Leverage is very low providing ample room for the bank to borrow funds for its lending activities should the need arise. For additional information concerning the Bank's debt, please refer to note 8 to the financial statements.

From operations, the Bank earned $2,126,856, which represents a 537% increase comparing to last year's results of $333,852. The Bank's return on equity remained positive and increased from 1.4% in 2015 to 6.1% in 2016. Moreover, the ratio of total net position to assets was at 97%. The bank was able to generate more than enough revenues to cover expenses, all from internal sources.

In 2016, the Bank's investments in the financial markets earned a significant turn-around of 63% growth compared to 2015. The total ratio of non-performing loans to total assets at the end of 2016 approximated 6%. As of December 31, 2016, total loan loss provision for total non-performing loans (those defined as aggregate principal and interest are past due 90 days and above) was at 101%. Based on the loan classification policy and review of individual loans, the Bank is adequately reserved for loan losses.

Summary Statements of Revenues, Expenses and Changes in Net Position

	2016	2015 (As Restated)	2014 (As Restated)
Operating revenues	$ 2,736,600	$ 2,460,513	$ 2,545,945
Reversal of (provision for) loan losses	1,179,871	(286,209)	(72,962)
Operating expenses	(1,789,615)	(1,840,452)	(1,792,313)
Earnings from operations	2,126,856	333,852	680,670
Non-operating revenues, net	1,192,397	439,213	998,783
Change in net position	3,319,253	773,065	1,679,453
Net position at beginning of year	50,986,309	50,213,244	48,533,791
Net position at end of year	$ 54,305,562	$ 50,986,309	$ 50,213,244

The Bank manages two trust funds, namely, the Investment Development Fund (IDF) and the Yap Development Loan Fund (YDLF). The total assets for each of these funds at the end of 2016 were $1,815,618 and $268,686, respectively. Assets under IDF continues to decrease as all the States have withdrawn their funds from the State sub-accounts. The Bank stopped drawing management fees from the IDF in 2016. YDLF earned $371 in 2016. Management had resubmitted a request to the FSM National Government to repeal the IDF law as only three loans remain active in the Private Sector sub-account and all loans in the State sub-accounts have defaulted and the projects are defunct.

Economic Outlook

Management anticipates the year 2017 to be better than 2016 in terms of economic activities. The Bank continues to seek out projects that are export oriented or import substituting. The Bank is also looking into helping the construction sector by providing real estate development loans and Surety bonds. The Bank was able to start some Home Energy Loan Program (HELP) projects in 2016 to help promote energy efficient homes for lower recurring electricity costs and hopes that this program grows going forward.

In line with the Bank's strategic plans and goals, the Bank's Business Development Office along with our FSMDB Development Finance Training Institute, the Bank anticipates to be more proactive in developing ideas into viable business proposals and providing entrepreneurial training to help improve the management of successful businesses in the FSM. The Bank is also working on its accreditation to access the Green Climate Fund (GCF) to provide projects to help climate change adaptation and mitigation.

Contacting Financial Management

The Management's Discussion and Analysis report is intended to provide information concerning known facts and conditions affecting the Bank's operations. This financial report is designed to provide a general overview of the Bank's finances and to demonstrate the Bank's accountability for the funds it receives and expends.

Management's Discussion and Analysis for the year ended December 31, 2015 is set forth in the Bank's report on the audit of financial statements, which is dated April 7, 2016. That Discussion and Analysis explains the major factors impacting the 2015 financial statements and can be viewed at the Bank's website at www.fsmdb.fm or Office of the Public Auditor's website at www.fsmopa.fm.

For additional information about this report, please contact Anna Mendiola, President/Chief Executive Officer, P.O. Box M, Kolonia, Pohnpei 96941or visit the website at www.fsmdb.fm.

FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Statements of Net Position
December 31, 2016 and 2015

	2016	2015 (As Restated)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 7,903,776	$ 8,627,124
Time certificates of deposit	937,542	936,381
Accounts receivable	4,655	8,146
Receivable from trust funds	-	197,448
Prepaid expenses	1,317	90,703
Interest and other receivables	109,937	122,571
Current portion of loans receivable	6,416,000	5,840,000
Total current assets	15,373,227	15,822,373
Noncurrent assets:		
Depreciable assets, net	1,624,211	1,633,285
Investments	15,066,298	14,291,833
Equity investment	5,100,240	4,825,200
Loans receivable, net of current portion and allowance for loan losses	18,756,819	16,040,721
Total noncurrent assets	40,547,568	36,791,039
Total assets	$ 55,920,795	$ 52,613,412
LIABILITIES AND NET POSITION		
Current liabilities:		
Current portion of long-term debt	$ 133,961	$ 128,449
Accounts payable	111,581	128,021
Payable to trust funds	129,273	-
Unearned grant revenues	105,816	124,010
Accrued interest payable	13,325	13,325
Credit life payable	100,357	78,401
Total current liabilities	594,313	472,206
Noncurrent liabilities:		
Long-term debt, net of current portion	1,020,920	1,154,897
Total liabilities	1,615,233	1,627,103
Commitments and contingencies		
Net position:		
Net investment in capital assets	1,624,211	1,633,285
Unrestricted	52,681,351	49,353,024
Total net position	54,305,562	50,986,309
Total liabilities and net position	$ 55,920,795	$ 52,613,412

See accompanying notes to financial statements.

FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Statements of Revenues, Expenses and Changes in Net Position
Years Ended December 31, 2016 and 2015

	2016	2015 (As Restated)
Operating revenues:		
Interest income on loans	$ 2,423,610	$ 2,198,035
Loan fees	196,457	127,820
Rental	26,931	37,735
Interest income on time certificates of deposit	11,193	11,788
Miscellaneous	78,409	85,135
Total operating revenues	2,736,600	2,460,513
Recoveries of (provision for) loan losses	1,179,871	(286,209)
Net operating revenues	3,916,471	2,174,304
Operating expenses:		
Interest expense	52,030	90,061
General and administrative expenses:		
Personnel services	991,136	965,145
Depreciation	146,069	118,162
Travel	98,481	103,326
Contractual services	92,922	98,747
Rent	87,549	102,900
Retirement plan contributions	55,467	49,434
Utilities	42,071	44,887
Communication	40,286	42,939
Branch automation	28,319	18,373
Training	22,316	59,399
Supplies	20,373	31,332
Community development	14,745	8,586
Equipment	13,936	14,417
Staff relations	12,936	8,625
Fuel, oil and petroleum	9,555	11,583
Repair and maintenance	8,076	9,329
Insurance	5,978	6,925
Printing	2,210	1,934
Miscellaneous	45,160	54,348
Total general and administrative expenses	1,737,585	1,750,391
Earnings from operations	2,126,856	333,852
Nonoperating revenues (expenses), net:		
IDF reimbursement	-	250,000
Investment earnings, net	1,192,397	190,603
Loss on sale of assets	-	(1,390)
Total nonoperating revenues, net	1,192,397	439,213
Change in net position	3,319,253	773,065
Net position at beginning of year, as restated	50,986,309	50,213,244
Net position at end of year, as restated	$ 54,305,562	$ 50,986,309

See accompanying notes to financial statements.

FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Statements of Cash Flows
Years Ended December 31, 2016 and 2015

	2016	2015
Cash flows from operating activities:		
Cash received from customers	$ 2,741,532	$ 2,561,262
Cash received from grantor	-	124,970
Cash paid to suppliers for goods and services	(523,672)	(689,760)
Cash paid to employees for services	(991,136)	(965,145)
Interest received on time certificates of deposit	11,193	11,788
Interest paid	(52,030)	(90,061)
Net cash provided by operating activities	1,185,887	953,054
Cash flows from noncapital financing activities:		
Principal repayment of long-term debt	(128,465)	(538,134)
Net transfers in from trust funds	326,721	132,440
Net cash provided by (used for) noncapital financing activities	198,256	(405,694)
Cash flows from capital and related financing activities:		
Acquisition of fixed assets	(136,995)	(95,331)
Net cash used for capital and related financing activities	(136,995)	(95,331)
Cash flows from investing activities:		
Loan origination and principal collections (disbursements), net	(2,112,227)	128,310
(Increase) decrease in time certificates of deposit	(1,161)	1,056,945
(Increase) decrease in investments	(14,608)	1,353,197
Interest income on savings accounts	-	615
Dividends received	157,500	157,500
Net cash (used for) provided by investing activities	(1,970,496)	2,696,567
Net change in cash and cash equivalents	(723,348)	3,148,596
Cash and cash equivalents at beginning of year	8,627,124	5,478,528
Cash and cash equivalents at end of year	$ 7,903,776	$ 8,627,124

See accompanying notes to financial statements.

FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Statements of Cash Flows, Continued
Years Ended December 31, 2016 and 2015

	2016	2015
Reconciliation of earnings from operations to net cash provided by operating activities:		
Earnings from operations	$ 2,126,856	$ 333,852
Adjustment to reconcile earnings from operations to net cash provided by operating activities:		
(Recoveries from) provision for loan losses	(1,179,871)	286,209
Depreciation	146,069	118,162
(Increase) decrease in assets:		
Accounts receivable	3,491	28,945
Interest and other receivables	12,634	83,592
Prepaid expenses	89,386	(81,384)
Increase (decrease) in liabilities:		
Accounts payable	(16,440)	43,164
Unearned grant revenues	(18,194)	124,010
Credit life payable	21,956	16,504
Net cash provided by operating activities	$ 1,185,887	$ 953,054

See accompanying notes to financial statements.

(1) Summary of Significant Accounting Policies

Reporting Entities

The Federated States of Micronesia (FSM) Development Bank (the Bank) was created in 1979 by Public Law 1-37 of the First Congress of the Federated States of Micronesia. The Bank began its operations on October 1, 1980. The Bank was reorganized in January 1994 by Public Law 8-47 of the Eighth Congress of the Federated States of Micronesia. The purpose of the Bank is to provide loans for economic development of the FSM. Such loans may otherwise be too risky for commercial banks to underwrite. Additionally, the Bank's repayment terms tend to be longer than those offered by commercial banks. As of December 31, 2016, the Bank has issued 3,236,883 shares to the FSM National Government (98.8%), Chuuk State (0.92%) and Kosrae State (0.28%). These shares do not convey ownership and have been made in accordance with the aforementioned law but these shares have no financial impact on the accompanying financial statements.

The Investment Development Fund (IDF) was established by Public Law 5-122 in January 1989. The purpose of the IDF is to finance projects which will (1) have their operations primarily located within the FSM; (2) improve the balance of payments position of the FSM; (3) increase the value of visible and invisible exports or result in import substitutions; (4) demonstrate positive economic returns; and (5) contribute to the furtherance of close economic relations with the United States.

The Yap Development Loan Fund (YDLF) is administered by the Bank in a Trust capacity. All loan decisions are made by executives of the respective state governments.

The Bank is a component unit (a discretely presented proprietary fund type) of the FSM National Government. The financial statements in this report do not represent the financial position, results of operations or cash flows of the FSM National Government as a whole. The financial statements of the Bank are not obligations of the FSM National Government unless specifically authorized by the FSM National Government. To date, no such authorizations have been made.

Fund Structure and Basis of Accounting

The accounts of the Bank are organized as a discretely presented component unit - proprietary fund of the FSM National Government. Proprietary funds are used by governmental units to account for operations that are financed and operated in a manner similar to a private business. This accounting is appropriate when costs of providing goods or services to the general public are to be financed primarily through user charges or where the periodic determination of net income is appropriate for accountability purposes. The accrual basis of accounting is utilized by proprietary funds. Under the accrual basis, revenues are recorded when earned, and expenses are recorded at the time the liabilities are incurred.

The accounts of the IDF and YDLF are accounted for as fiduciary fund types as the amounts are to be reported on the respective entities' financial statements (the FSM National Government and Yap State, respectively).

(1) Summary of Significant Accounting Policies, Continued

Fund Structure and Basis of Accounting, Continued

The Bank utilizes the flow of economic resources measurement focus. Its financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) as applied to governmental units using the accrual basis of accounting. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

The Statement of Net Position presents all of the Bank's non-fiduciary assets, deferred outflows of resources, liabilities and deferred inflows of resources, with the difference reported as net position. Net position is classified for accounting and reporting purposes into the following three net position categories:

- Net investment in capital assets - capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets as well as deferred outflows of resources and deferred inflows of resources that are attributable to those assets or related debt.

- Restricted - restricted assets reduced by liabilities and deferred inflows of resources related to those assets that are subject to externally imposed stipulations.

- Unrestricted - the net amount of the assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. All other revenues are reported as nonoperating. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Cash and Cash Equivalents

For the purposes of the statements of net position and the statements of cash flows, cash and cash equivalents are defined as cash in bank checking and savings accounts, money market funds, and commercial paper with original maturities of three months or less from the date of acquisition.

Time certificates of deposit with original maturities of greater than three months are separately classified.

Investments

Investments and related investment earnings are reported at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability (i.e., the exit price) in an orderly transaction between market participants at the date as of which the fair value of an asset or liability is determined.

An equity investment in the common stock of Bank of the FSM (investee) is stated at the net asset value (NAV). The NAV is used as a practical expedient to estimate fair value. The NAV is determined based on the total shareholders' equities reported by the investee. Refer to *New Accounting Standards* section below for the changes reflected in the accompanying financial statements.

(1) Summary of Significant Accounting Policies, Continued

Loans and Allowance for Loan Losses

Loans receivable are stated at unpaid principal balance less the allowance for loan losses.

Management maintains the allowance for loan losses at a level adequate to absorb probable losses. Management determines the adequacy of the allowance based upon reviews of individual loans, recent loss experience, current economic conditions, the risk characteristics of the various categories of loans and other pertinent factors. Loans deemed uncollectible are charged to the allowance. Provisions for losses and recoveries on loans previously charged off are added to the allowance.

Interest on loans is accrued and credited to income based on the principal amount outstanding. The accrual of interest on loans is discontinued when, in the opinion of management, there is an indication that the borrower may be unable to meet payments as they become due. Upon such discontinuance, all unpaid accrued interest is reversed.

Fixed Assets

Fixed assets are stated at cost, less accumulated depreciation. Depreciation is based on the straight-line method over the estimated useful lives of the respective assets. All assets have estimated useful lives of three to five years.

The Bank's policy on fixed assets requires that assets with a purchase value of $5,000 and over are capitalized and depreciated based on their useful lives. Assets with a purchase value less than $5,000 are expensed fully in the year of purchase.

Unearned Grant Revenues

Unearned grant revenues represents amounts received from grant and contract sponsors that have not yet been earned.

Compensated Absences

Earned but unused annual leave is paid to employees upon termination of their employment. Accordingly, vested or accumulated vacation leave is recorded as an expense and liability as the benefits accrue to employees. It is the policy of the Bank to record the cost of sick leave when leave is actually taken and an expense is actually incurred. Accordingly, no liability is recorded for non-vesting accumulating rights to receive sick pay benefits, which approximated $169,000 and $147,000 at December 31, 2016 and 2015, respectively.

Off-Balance Sheet Financial Instruments

In the ordinary course of business, the Bank enters into off-balance sheet financial instruments consisting of commitments to extend credit and loan guarantees. Such financial instruments are recorded in the financial statements when they become payable.

Estimates

The preparation of financial statements in conformity with GAAP requires 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. A material estimate that is particularly susceptible to significant change in the near term relates to the determination of the allowance for loan losses.

(1) Summary of Significant Accounting Policies, Continued

New Accounting Standards

During the year ended December 31, 2016, the Bank implemented the following pronouncements:

- GASB Statement No. 72, *Fair Value Measurement and Application*, which addresses accounting and financial reporting issues related to fair value measurements and requires entities to expand their fair value disclosures by determining major categories of debt and equity securities within the fair value hierarchy on the basis of the nature and risk of the investment. The implementation of this statement resulted in additional disclosures about fair value measurements, the level of fair value hierarchy, and valuation techniques. Additionally, the implementation resulted in the re-measurement of equity investment from cost-basis to NAV, as cost-basis measurement is no longer an allowable measureable method for equity investment. Such implementation had a material effect on the accompanying financial statements resulting in the restatement of the Bank's 2015 financial statements to reflect the required adjustments as follows:

	As Previously Reported	Adjustment	As Restated
As of December 31, 2014:			
Net position	$ 47,466,312	$ 2,746,932	$ 50,213,244
For the year ended December 31, 2015:			
Investment earnings, net	$ 24,523	$ 166,080	$ 190,603
Change in net position	$ 606,985	$ 166,080	$ 773,065
As of December 31, 2015:			
Equity investment	$ 1,912,188	$ 2,913,012	$ 4,825,200
Total assets	$ 49,700,400	$ 2,913,012	$ 52,613,412
Total net position	$ 48,073,297	$ 2,913,012	$ 50,986,309

- GASB Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, which eliminates two of the four categories of authoritative GAAP that exist under the existing hierarchy prescribed by Statement No. 55. The two categories that will remain under the new standard are (1) GASB Statements and (2) GASB technical bulletins and implementation guides in addition to AICPA guidance that the GASB clears. The implementation of this statement did not have a material effect on the accompanying financial statements.

- GASB Statement No. 77, *Tax Abatement Disclosures*, which requires governments that enter into tax abatement agreements to disclose certain information about the agreements. The implementation of this statement did not have a material effect on the accompanying financial statements.

- GASB Statement No. 78, *Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans*, which addresses a practice issue regarding the scope and applicability of Statement No. 68, *Accounting and Financial Reporting for Pensions*. The implementation of this statement did not have a material effect on the accompanying financial statements.

(1) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

- GASB Statement No. 79, *Certain External Investment Pools and Pool Participants*, which addresses for certain external investment pools and their participants the accounting and financial reporting implications that result from changes in the regulatory provisions referenced by previous accounting and financial reporting standards. Those provisions were based on the Investment Company Act of 1940, Rule 2a7. Rule 2a7 contains the Securities and Exchange Commission's regulations that apply to money market funds and were significantly amended in 2014. The implementation of this statement did not have a material effect on the accompanying financial statements.

In June 2015, GASB issued Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not Within the Scope of GASB Statement No. 68, and Amendments to Certain Provisions of GASB Statements No. 67 and No. 68*, which aligns the reporting requirements for pensions and pension plans not covered in GASB Statements No. 67 and No. 68 with the reporting requirements in Statement No. 68. The provisions in Statement No. 73 are effective for fiscal years beginning after June 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In June 2015, GASB issued Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which replaces Statements No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans,* as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, and addresses financial reporting requirements for governments whose employees are provided with postemployment benefits other than pensions (other postemployment benefits or OPEB). The provisions in Statement No. 74 are effective for fiscal years beginning after June 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In June 2015, GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which replaces the requirements of Statements No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions,* as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, and provides guidance on reporting by governments that provide OPEB to their employees and for governments that finance OPEB for employees of other governments. The provisions in Statement No. 75 are effective for fiscal years beginning after June 15, 2017. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In January 2016, GASB issued Statement No. 80, *Blending Requirements for Certain Component Units - an amendment of GASB Statement No. 14*, which improves financial reporting by clarifying the financial statement presentation requirements for certain component units. The provisions in Statement No. 80 are effective for fiscal years beginning after June 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In March 2016, GASB issued Statement No. 81, *Irrevocable Split-Interest Agreements*, which improves accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement. The provisions in Statement No. 81 are effective for fiscal years beginning after December 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

(1) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In March 2016, GASB issued Statement No. 82, *Pension Issues - an amendment of GASB Statements No. 67, No. 68, and No. 73*, which addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements. The provisions in Statement No. 82 are effective for fiscal years beginning after June 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In November 2016, GASB issued Statement No. 83, *Certain Asset Retirement Obligations*, which establishes criteria for determining the timing and pattern of recognition of a liability and a corresponding deferred outflow of resources for Asset Retirement Obligations (ARO). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. The provisions in Statement No. 82 are effective for fiscal years beginning after June 15, 2018. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

(2) Deposits and Investments

The deposit and investment policies of the Bank 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 Bank's investments. Legally authorized investments are as follows:

(i) Government obligations - Obligations issued or guaranteed as to principal and interest by the 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 other mortgage-backed securities provided that the obligation is an agency of the United States Government, the National Government of the Federated States of Micronesia, 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 investment 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 Bank's investment advisor at the time of purchase, that not more than five percent of the market value of its investments shall be invested in the stock of any one corporation, and that not more than ten percent of the market value of its investments shall be invested in any one industry group.

(2) Deposits and Investments, Continued

(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.

A. Deposits

Custodial credit risk is the risk that in the event of a bank failure, the Bank'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 Bank does not have a deposit policy for custodial credit risk.

As of December 31, 2016 and 2015, the carrying amount of the Bank's total cash and cash equivalents and time certificates of deposit was $8,841,318 and $9,563,505, respectively, and the corresponding bank balances were $8,904,033 and $9,662,223, respectively, which were all maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. As of December 31, 2016 and 2015, bank deposits in the amounts of $1,520,366 and $1,521,581, respectively, were FDIC insured. The Bank 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. Management's confidence in the financial strength of their banking institutions was the basis of the decision to not require collateralization. No losses as a result of this practice were incurred for the years ended December 31, 2016 and 2015.

B. Investments

As of December 31, 2016 and 2015, investments at fair value are as follows:

	2016	2015
Fixed income securities:		
Domestic fixed income	$ 5,121,414	$ 5,008,967
Other investments:		
Domestic equities	8,895,921	8,298,900
Shares in a mutual fund (Templeton Global BD FD ADV TGBAX)	1,048,963	983,966
	$ 15,066,298	$ 14,291,833

(2) Deposits and Investments, Continued

B. Investments, Continued

As of December 31, 2016, investments in domestic fixed income are as follows:

	Moody's Credit Rating	Investment maturities (in Years) Less Than 1	1 to 5	6 to 10	Greater Than 10	Fair Value
U.S. Government securities:						
U.S. Treasury Notes	Aaa	$ -	$ -	$ 1,827,784	$ -	$ 1,827,784
U.S. Government agencies:						
Federal Home Loan Bank	Aaa	210,199	-	-	-	210,199
Federal Farm Credit Bank	Aaa	320,176	580,003	-	-	900,179
Federal National Mortgage Association	Not rated	-	295,620	97,234	402,970	795,824
Federal Home Loan Mortgage Corp.	Not rated	-	-	-	243,677	243,677
Corporate bonds	A3	-	87,617	714,338	-	801,955
Corporate bonds	A2	-	147,416	-	-	147,416
Corporate bonds	Baa3	-	-	194,380	-	194,380
		$ 530,375	$ 1,110,656	$ 2,833,736	$ 646,647	$ 5,121,414

As of December 31, 2015, investments in domestic fixed income are as follows:

	Moody's Credit Rating	Investment maturities (in Years) Less Than 1	1 to 5	6 to 10	Greater Than 10	Fair Value
U.S. Government securities:						
U.S. Treasury Note	Aaa	$ -	$ -	$ 1,886,177	$ -	$ 1,886,177
U.S. Treasury Bond	Aaa	-	-	1,071,281	-	1,071,281
U.S. Government agencies:						
Federal Home Loan Bank	Aaa	-	339,820	-	-	339,820
Federal Home Loan Mortgage Corp.	Not rated	-	-	84,106	212,931	297,037
Federal National Mortgage Association	Aaa	-	366,292	-	189,344	555,636
Federal National Mortgage Association	AA+ S&P	-	125,663	-	-	125,663
Federal Farm Credit Bank	Aaa	-	179,348	-	-	179,348
Corporate bonds	A3	-	-	197,869	53,685	251,554
Corporate bonds	A1	-	-	92,635	-	92,635
Corporate bonds	Aa3	-	-	51,471	-	51,471
Corporate bonds	Aa2	-	-	45,947	-	45,947
Corporate bonds	Aa1	-	-	51,797	-	51,797
Corporate bonds	Baa1	-	-	60,601	-	60,601
		$ -	$ 1,011,123	$ 3,541,884	$ 455,960	$ 5,008,967

(2) Deposits and Investments, Continued

B. Investments, Continued

The Bank categorizes its fair value measurements within the fair value hierarchy established by GASB Statement No. 72. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. The Bank has the following recurring fair value measurements as of December 31, 2016 and 2015:

		Fair Value Measurements Using		
	December 31, 2016	Level 1	Level 2	Level 3
Fixed income:				
U.S. Treasury obligations	$ 1,827,784	$ -	$ 1,827,784	$ -
U.S. Government Agencies	2,149,879	-	2,149,879	-
Corporate notes	1,143,751	-	1,143,751	-
Total fixed income	5,121,414	-	5,121,414	-
Equity securities:				
U.S. equities	8,895,921	8,895,921	-	-
Mutual fund shares	1,048,963	1,048,963	-	-
Total investments at fair value	$ 15,066,298	$ 9,944,884	$ 5,121,414	$ -

		Fair Value Measurements Using		
	December 31, 2015	Level 1	Level 2	Level 3
Fixed income:				
U.S. Treasury obligations	$ 2,957,458	$ -	$ 2,957,458	$ -
U.S. Government Agencies	1,497,504	-	1,497,504	-
Corporate notes	554,005	-	554,005	-
Total fixed income	5,008,967	-	5,008,967	-
Equity securities:				
U.S. equities	8,298,900	8,298,900	-	-
Mutual fund shares	983,966	983,966	-	-
Total investments at fair value	$ 14,291,833	$ 9,282,866	$ 5,008,967	$ -

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

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to the transaction, the Bank will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The Bank's investments are held and administered by trustees. Accordingly, these investments are exposed to custodial credit risk. Based on negotiated trust and custody contracts, all of these investments were held in the Bank's name by the Bank's custodial financial institution at December 31, 2016 and 2015.

(2) Deposits and Investments, Continued

B. Investments, Continued

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 Bank. As of December 31, 2016, the Bank's investment in U.S. Treasury securities and agency obligations of the Federal Farm Credit Bank constituted 12% and 6%, respectively, of its total investments. As of December 31, 2015, the Bank's investment in U.S. Treasury securities constituted 21% of its total investments.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of debt instruments. The Bank has a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

(3) Equity Investment

At December 31, 2016 and 2015, the equity investment in Bank of the FSM represents 225,000 common shares and approximately 24.1% ownership interest. Total shareholders' equity reported by Bank of the FSM approximated $21,251,000 and $20,105,000 at December 31, 2016 and 2015, respectively.

(4) Loans Receivable

A summary of loans receivable at December 31, 2016 and 2015 follows:

	2016	2015
Unpaid principal balance	$ 28,392,819	$ 25,832,979
Allowance for loan losses	(3,220,000)	(3,952,258)
	$ 25,172,819	$ 21,880,721

Movements in the allowance for loan losses during the years ended December 31, 2016 and 2015, are as follows:

	2016	2015
Balance at beginning of year	$ 3,952,258	$ 3,828,893
(Recoveries of) provision for loan losses	(1,179,871)	286,209
Loans charged off	(436,642)	(1,374,436)
Loan recoveries from previously charged off loans	884,255	1,211,592
Balance at end of year	$ 3,220,000	$ 3,952,258

(5) Fixed Assets

A summary of fixed assets as of December 31, 2016 and 2015, is as follows:

	Beginning January 1, 2016	Additions/ Transfers	Deletions/ Transfers	Ending December 31, 2016
Building	$ 1,674,348	$ -	$ -	$ 1,674,348
Computers and software	652,912	109,561	-	762,473
Vehicles	144,572	27,434	-	172,006
Office furniture, fixtures and equipment	39,733	-	-	39,733
	2,511,565	136,995	-	2,648,560
Less accumulated depreciation	(878,280)	(146,069)	-	(1,024,349)
Fixed assets, net	$ 1,633,285	$ (9,074)	$ -	$ 1,624,211

	Beginning January 1, 2015	Additions/ Transfers	Deletions/ Transfers	Ending December 31, 2015
Building	$ 1,674,348	$ -	$ -	$ 1,674,348
Computers and software	485,103	171,088	(3,279)	652,912
Vehicles	144,572	-	-	144,572
Office furniture, fixtures and equipment	39,733	-	-	39,733
	2,343,756	171,088	(3,279)	2,511,565
Less accumulated depreciation	(762,007)	(118,162)	1,889	(878,280)
	1,581,749	52,926	(1,390)	1,633,285
Fixed assets in progress	75,757	-	(75,757)	-
Fixed assets, net	$ 1,657,506	$ 52,926	$ (77,147)	$ 1,633,285

(6) Related Party Transactions

As of December 31, 2016 and 2015, the Bank has direct loans with outstanding balances of $428,438 and $336,606, respectively, to employees of the Bank and project loans extended to businesses owned by or affiliated with employees of $2,019,105 and $581,483, respectively. These loans were made under similar terms and conditions as exist with other borrowers. Officers and Board members are not eligible to borrow from the Bank.

(7) Staff Loan Revolving Fund

In July 2007, the Bank's Board of Directors approved the establishment of a Staff Loan Revolving Fund. In September 2007, a savings account was established for this purpose. As of December 31, 2016 and 2015, the account has a balance of $104,723 and $260,530, respectively.

(8) Long-Term Debt

Long-term debt consists of the following at December 31, 2016 and 2015:

	2016	2015
Unsecured loans payable to European Investment Bank under a August 2010 master finance contract of EUR 4 million:		
Drawn on August 20, 2014; original amount of $275,000 (equivalent EUR 205,500), bearing interest fixed at 3.705%, and payable through semi-annual principal and interest installments of $24,778 on January 15, 2015 and equal installments of $25,772 beginning on July 15, 2015 through maturity on July 15, 2020.	$ 189,975	$ 233,268
Drawn on August 20, 2014; original amount of $334,550 (equivalent EUR 250,000), bearing interest fixed at 4.520%, and payable through semi-annual principal and interest installments of $17,997 on January 15, 2015 and equal installments of $19,467 beginning on July 15, 2015 through maturity on July 15, 2025.	285,287	310,469
Drawn on August 20, 2014; original amount of $796,976 (equivalent EUR 595,558), bearing interest fixed at 4.520%, and payable through semi-annual principal and interest installments of $42,873 on January 15, 2015 and equal installments of $46,375 beginning on July 15, 2015 through maturity on July 15, 2025.	679,619	739,609
Total long-term debt	1,154,881	1,283,346
Less current portion	(133,961)	(128,449)
Long-term debt, net of current portion	$ 1,020,920	$ 1,154,897

Annual debt service requirements to maturity for principal and interest are as follows:

Year Ending December 31,	Principal	Interest	Total
2017	$ 133,961	$ 49,267	$ 183,228
2018	139,710	43,518	183,228
2019	145,709	37,519	183,228
2020	151,968	31,260	183,228
2021	106,476	25,207	131,683
2022-2025	477,057	49,883	526,940
	$ 1,154,881	$ 236,654	$ 1,391,535

(8) Long-Term Debt, Continued

Long-term debt changes during the years ended December 31, 2016 and 2015 are as follows:

	Balance January 1,	Additions	Reductions	Balance December 31,	Due Within One Year
2016:					
Loan payable	$ 1,283,346	$ -	$ (128,465)	$ 1,154,881	$ 133,961

	Balance January 1,	Additions	Reductions	Balance December 31,	Due Within One Year
2015:					
Loan payable	$ 1,821,480	$ -	$ (538,134)	$ 1,283,346	$ 128,449

(9) Unearned Grant Revenues

During the year ended December 31, 2015, the Bank was awarded a $250,000 Home Energy Loan Program grant from the International Union for Conservation of Nature Resources (IUCN). $232,000 of the grant will be awarded to the qualified borrowers for new loans to construct homes that will demonstrate features and measures designed to conserve energy, reduce consumption of fossil fuels and enhance energy efficiency as principle reduction of loans, while the remaining $18,000 will be used by the Bank for renovations to improve energy efficiency. As of December 31, 2016 and 2015, $124,970 has been received and $19,154 and $960, respectively, expended by the Bank.

(10) Nonoperating Revenue

The Bank was reimbursed for expenses incurred in administering the Investment Development Fund (IDF) program from the IDF Private Sub Account for $250,000 for the year ended December 31, 2015.

(11) Retirement Plan

The Bank's retirement plan (the Plan) is a self-administered program established to pay retirement, disability and survivor income to employees and their survivors to supplement similar benefits that employees receive from the FSM Social Security System. The Plan is a contributory plan in which the Bank matches 100% of the participants' contributions up to a maximum of 10 percent of the participant's annual salary, if the participant contributes 3 or more percent from his or her annual salary. Employee participation is optional. The Bank's Chief Financial Officer is the designated Plan Administrator. Matching contributions to the Plan during the years ended December 31, 2016 and 2015 were $55,467 and $49,434, respectively. Total Plan assets as of December 31, 2016 and 2015 were $845,119 and $706,804, respectively. Management is of the opinion that the Plan does not represent an asset or a liability of the Bank.

(12) Commitments and Contingencies

Guaranty

The Bank, from time-to-time, is contingently liable on loan guarantees ranging from 50% to 90% of the outstanding loan balances for commercial projects within the FSM. There were no outstanding guaranteed loan balances as of December 31, 2016 and 2015.

(12) Commitments and Contingencies, Continued

Loan Commitments

Undrawn balances on lines of credit and loan commitments for loans approved but undisbursed approximated $13,475,000 at December 31, 2016, of which $11,410,000 represent approved loans to three borrowers.

Litigation

The Bank is a party to various legal proceedings, the ultimate impact of which is not currently predictable. Therefore, no liability has been recorded in the accompanying financial statements due to management's inability to predict the ultimate outcome of these proceedings.

Insurance

The Bank carries insurance to cover its potential risks from vehicle usage. The Bank is substantially self-insured for all other risks. Management is of the opinion that no material losses have been sustained as a result of this practice during the past three years.

Lease Commitments

The Bank has three operating leases for its State operating locations. These leases expire in varying dates through December 2021. Several of these leases provide options to renew upon expiration, based on renegotiated rates. Future minimum annual lease payments payable under the noncancellable lease agreements are as follows:

Year ending December 31,	
2017	$ 38,600
2018	14,500
2019	13,200
2020	13,200
2021	13,200
	$ 92,700

The Bank leases portions of its headquarters building under three separate agreements expiring from September 2017 to September 2025. Future minimum annual lease income receivable under the noncancellable lease agreements are as follows:

Year ending December 31,	
2017	$ 28,200
2018	20,700
2019	20,700
2020	18,500
2021	11,700
Thereafter	43,900
	$ 143,700

Additionally, the Bank provides housing benefits for certain contract employees with payment included as part of rent expense. The lease agreements are between the respective landlords and the employees.

(12) Commitments and Contingencies, Continued

Lease Commitments, Continued

Total recorded lease expense and income under the aforementioned agreements amounted to $87,549 and $26,931, respectively, for the year ended December 31, 2016 and $102,900 and $37,735, respectively, for the year ended December 31, 2015.

(13) Subsequent Events

Management has evaluated subsequent events through April 17, 2017, which is the date that the financial statements are available to be issued. There were no material subsequent events that would require recognition or disclosure in the financial statements for the year ended December 31, 2016.

FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Schedule of European Investment Bank
August 2010 Finance Contract Ratios
December 31, 2016

1.) Ratio of Capital (paid in capital plus reserves) to total assets should be above 20%:

Total net position	$	54,305,562
Total assets	$	55,920,795
		97%

2.) Ratio of non-performing loans (defined as aggregate principal and interest due over 90 days and above) to total loans should not exceed 15%:

Total non-performing loans	$	3,201,976
Total assets	$	55,920,795
		6%

3.) Ratio of provision for loan losses to non performing loans shall not be less than 100%:

Allowance for loan losses	$	3,220,000
Total non-performing loans	$	3,201,976
		101%

See accompanying independent auditors' report.

TRUST FUNDS ADMINISTERED BY THE
FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

FINANCIAL STATEMENTS AND
INDEPENDENT AUDITORS' REPORT

YEAR ENDED DECEMBER 31, 2016

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INDEPENDENT AUDITORS' REPORT

Board of Directors
Federated States of Micronesia Development Bank:

Report on the Financial Statements

We have audited the accompanying financial statements of the Investment Development Fund and the Yap Development Loan Fund (the Funds), administered by the Federated States of Micronesia Development Bank (the Bank), which comprise the respective statement of fiduciary net position as of December 31, 2016, and the related statement of changes in fiduciary net position for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Deloitte.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Investment Development Fund and the Yap Development Loan Fund as of December 31, 2016, and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

As discussed in Note 1 to the financial statements, the financial statements referred to above present only the respective financial position of the Investment Development Fund and the Yap Development Loan Fund and are not intended to present fairly the financial position and results of operations of the Federated States of Micronesia Development Bank in conformity with accounting principles generally accepted in the United States of America.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated April 17, 2017, on our consideration of the Bank's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Bank's internal control over financial reporting and compliance.

Deloitte & Touche LLP

April 17, 2017

TRUST FUNDS ADMINISTERED BY THE
FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Trust Funds
Statement of Fiduciary Net Position
December 31, 2016

	IDF	YDLF	Total
ASSETS			
Current assets:			
Cash and cash equivalents	$ -	$ 119,479	$ 119,479
Receivable from FSMDB	142,607	-	142,607
Total current assets	142,607	119,479	262,086
Noncurrent assets:			
Time certificates of deposit	-	148,574	148,574
Interest and other receivables	9,716	633	10,349
Loans receivable, net of an allowance of $16,801	1,663,295	-	1,663,295
Total noncurrent assets	1,673,011	149,207	1,822,218
	$ 1,815,618	$ 268,686	$ 2,084,304
LIABILITIES AND NET POSITION			
Liabilities:			
Payable to FSMDB	$ -	$ 13,334	$ 13,334
Commitments			
Net position:			
Restricted	1,663,295	-	1,663,295
Unrestricted	152,323	255,352	407,675
Total net position	1,815,618	255,352	2,070,970
	$ 1,815,618	$ 268,686	$ 2,084,304

See accompanying notes to financial statements.

TRUST FUNDS ADMINISTERED BY THE
FEDERATED STATES OF MICRONESIA DEVELOPMENT BANK
(A COMPONENT UNIT OF THE FSM NATIONAL GOVERNMENT)

Trust Funds
Statement of Changes in Fiduciary Net Position
Year Ended December 31, 2016

	IDF	YDLF	Total
Additions:			
Recovery of loan losses	$ 136,545	$ -	$ 136,545
Loan interest	78,446	-	78,446
Investment interest	384	371	755
Total additions	215,375	371	215,746
Deductions:			
Miscellaneous	40	-	40
Total deductions	40	-	40
Change in net position	215,335	371	215,706
Net position at beginning of year	1,600,283	254,981	1,855,264
Net position at end of year	$ 1,815,618	$ 255,352	$ 2,070,970

See accompanying notes to financial statements.

(1) Purpose and Summary of Significant Accounting Policies

Purpose

The Investment Development Fund (IDF) and the Yap Development Loan Fund (YDLF) are administered by the Federated States of Micronesia Development Bank (the Bank). The Bank utilizes the Funds to carry out its stated purpose of providing loans for the economic development of the FSM. The specific purpose of each fund is as follows:

IDF was created to finance projects which will (1) have their operations primarily located within the FSM; (2) improve the balance of payments position of the FSM; (3) increase the value of visible and invisible exports or result in import substitutions; (4) demonstrate positive economic returns; and (5) contribute to the furtherance of close economic relations with the United States. The IDF is administered by the Bank in a Trust capacity on behalf of the FSM National Government and its four States.

YDLF is administered by the Bank in a Trust capacity. All loan decisions are made by executives of the respective state governments as these funds represent local appropriations designated to be loaned for development purposes.

Fund Structure and Basis of Accounting

The accounts of the IDF and YDLF are accounted for as fiduciary fund types as the amounts are to be reported on the respective entities' financial statements (the FSM National Government and Yap State, respectively).

Cash and Time Certificates of Deposit

For the purposes of the statement of fiduciary net position, cash is defined as cash in bank checking and savings accounts, and time certificates of deposit with original maturities of three months or less. Deposits maintained in time certificates of deposit with original maturity dates greater than three months are separately classified.

Loans and Allowance for Loan Losses

Loans receivable are stated at unpaid principal balance less the allowance for loan losses and are reserved in net position as restricted net position.

Management maintains the allowance for loan losses at a level adequate to absorb probable losses. Management determines the adequacy of the allowance based upon reviews of individual loans, recent loss experience, current economic conditions, the risk characteristics of the various categories of loans and other pertinent factors. Loans deemed uncollectible are charged to the allowance. Provisions for losses and recoveries on loans previously charged off are added to the allowance.

Interest on loans is accrued and credited to income based on the principal amount outstanding. The accrual of interest on loans is discontinued when, in the opinion of management, there is an indication that the borrower may be unable to meet payments as they become due. Upon such discontinuance, all unpaid accrued interest is reversed.

(1) Purpose and Summary of Significant Accounting Policies, Continued

New Accounting Standards

During the year ended December 31, 2016, the Funds implemented the following pronouncements:

- GASB Statement No. 72, *Fair Value Measurement and Application*, which addresses accounting and financial reporting issues related to fair value measurements and requires entities to expand their fair value disclosures by determining major categories of debt and equity securities within the fair value hierarchy on the basis of the nature and risk of the investment. The implementation of this statement did not have a material effect on the accompanying financial statements.

- GASB Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, which eliminates two of the four categories of authoritative GAAP that exist under the existing hierarchy prescribed by Statement No. 55. The two categories that will remain under the new standard are (1) GASB Statements and (2) GASB technical bulletins and implementation guides in addition to AICPA guidance that the GASB clears. The implementation of this statement did not have a material effect on the accompanying financial statements.

- GASB Statement No. 77, *Tax Abatement Disclosures*, which requires governments that enter into tax abatement agreements to disclose certain information about the agreements. The implementation of this statement did not have a material effect on the accompanying financial statements.

- GASB Statement No. 78, *Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans*, which addresses a practice issue regarding the scope and applicability of Statement No. 68, *Accounting and Financial Reporting for Pensions*. The implementation of this statement did not have a material effect on the accompanying financial statements.

- GASB Statement No. 79, *Certain External Investment Pools and Pool Participants*, which addresses for certain external investment pools and their participants the accounting and financial reporting implications that result from changes in the regulatory provisions referenced by previous accounting and financial reporting standards. Those provisions were based on the Investment Company Act of 1940, Rule 2a7. Rule 2a7 contains the Securities and Exchange Commission's regulations that apply to money market funds and were significantly amended in 2014. The implementation of this statement did not have a material effect on the accompanying financial statements.

In June 2015, GASB issued Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not Within the Scope of GASB Statement No. 68, and Amendments to Certain Provisions of GASB Statements No. 67 and No. 68*, which aligns the reporting requirements for pensions and pension plans not covered in GASB Statements No. 67 and No. 68 with the reporting requirements in Statement No. 68. The provisions in Statement No. 73 are effective for fiscal years beginning after June 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

(1) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In June 2015, GASB issued Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which replaces Statements No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans,* as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, and addresses financial reporting requirements for governments whose employees are provided with postemployment benefits other than pensions (other postemployment benefits or OPEB). The provisions in Statement No. 74 are effective for fiscal years beginning after June 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In June 2015, GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which replaces the requirements of Statements No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, and provides guidance on reporting by governments that provide OPEB to their employees and for governments that finance OPEB for employees of other governments. The provisions in Statement No. 75 are effective for fiscal years beginning after June 15, 2017. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In January 2016, GASB issued Statement No. 80, *Blending Requirements for Certain Component Units - an amendment of GASB Statement No. 14*, which improves financial reporting by clarifying the financial statement presentation requirements for certain component units. The provisions in Statement No. 80 are effective for fiscal years beginning after June 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In March 2016, GASB issued Statement No. 81, *Irrevocable Split-Interest Agreements*, which improves accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement. The provisions in Statement No. 81 are effective for fiscal years beginning after December 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In March 2016, GASB issued Statement No. 82, *Pension Issues - an amendment of GASB Statements No. 67, No. 68, and No. 73*, which addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements. The provisions in Statement No. 82 are effective for fiscal years beginning after June 15, 2016. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

(1) Purpose and Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In November 2016, GASB issued Statement No. 83, *Certain Asset Retirement Obligations*, which establishes criteria for determining the timing and pattern of recognition of a liability and a corresponding deferred outflow of resources for Asset Retirement Obligations (ARO). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. The provisions in Statement No. 82 are effective for fiscal years beginning after June 15, 2018. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

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 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) Deposits

The deposit policies of the Funds are governed by their enabling legislation.

Custodial credit risk is the risk that in the event of a bank failure, the Funds' deposits may not be returned to them. 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 Funds do not have a deposit policy for custodial credit risk.

As of December 31, 2016, the carrying amount and corresponding bank balances of the Funds' total cash and cash equivalents and time certificates of deposit was $268,053. All of the bank balances are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. However, none of the balances were covered as the FSMDB have already exceeded the insurable limit per depositor. For purposes of FDIC insurance termination, funds held in trust are not differentiable with regular accounts held by FSMDB. The Funds do not require collateralization of their cash deposits; therefore, deposit levels in excess of FDIC insurance coverage are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk. Management's confidence in the financial strength of their banking institutions was the basis of the decision to not require collateralization. No losses as a result of this practice were incurred for the year ended December 31, 2016.

(3) Subsequent Events

Management has evaluated subsequent events through April 17, 2017, which is the date that the financial statements are available to be issued. There were no material subsequent events that would require recognition or disclosure in the financial statements for the year ended December 31, 2016.

Deloitte.

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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 Directors
Federated States of Micronesia Development Bank:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Federated States of Micronesia Development Bank (the Bank), which comprise the statement of net position as of December 31, 2016, and the related statements of revenues, expenses and changes in net position and of cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated April 17, 2017.

Internal Control Over Financial Reporting

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

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

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

Deloitte.

Compliance and Other Matters

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

We noted certain matters that we reported to management of the Bank in a separate letter dated April 17, 2017.

Purpose of this Report

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

Deloitte & Touche LLP

April 17, 2017

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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 Directors
Federated States of Micronesia Development Bank:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Investment Development Fund and the Yap Development Loan Fund (the Funds), administered by the Federated States of Micronesia Development Bank (the Bank), which comprise the respective statement of fiduciary net position as of December 31, 2016, and the related statement of change in fiduciary net position for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated April 17, 2017.

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

Deloitte.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the respective financial statements of the Investment Development Fund and the Yap Development Loan Fund are free from material misstatement, we performed tests of their 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*.

We noted certain matters that we reported to management of the Bank in a separate letter dated April 17, 2017.

Purpose of this Report

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

Deloitte & Touche LLP

April 17, 2017

This 2016 Annual Report was printed on digital gloss paper and distributed to our shareholders, board members, partner-organizations, and the FSM leadership in limited copies, consistent with our commitment to reduce our carbon footprint. An electronic copy may be downloaded on our website, www.fsmdb.fm.

Staff Listing:

Headquarter Office:		
Rendy	Abraham	Loan Analyst
Carmihna	Abraham	Bookkeeper
Sincerlynn	Alten	Admin.Secretary
Charito	Soriano	Accountant
Joyleen	Charley	Loan Officer
Lenster	Donre	Loan Officer
Galverson	Eliou	Loan Officer
Leilani	Felix	Assistant Systems Administrator
Lover	Haimin	HR & Facilities Manager
Vicky	Hartman	Loan Officer
Dorian	Kiyoshi	Executive Secretary to the CEO
Augustine	Loyola	Loan Analyst
Nicole	Araceley	Accountant
Gabriel	Ramoloilug	Systems Administrator
Zenica	Yiftheg	Bookkeeper
Rohma	Silbanuz	Legal Secretary
Marleen	Tom	Loan Security Officer
Kedise	Villazon	Accountant
Peterika	White	Admin.Secretary
Michael	Watson	Assistant Legal Counsel
Kosrae Branch:		
Andriet	Tilfas	Branch Manager
Arthur	Sigrah	Loan Officer
Serah	Robert	Loan Officer
Luna	Youngstrom	Administrative Secretary
Chuuk Branch:		
Masashi	Mori	Branch Manager
Jayleen	Kansou	Loan Officer
Janet	Sisam	Loan Officer
Crystal	Sana	Loan Officer
Cereza	Narruhn	Administrative Secretary
Yap Branch:		
Katherine	Gisog	Branch Manager
Constantine	Yowbalaw	Loan Officer
Trudy	Munggol	Loan Officer
Wenifred	Faimau	Administrative Secretary