



# Fiscal Year 2015 Annual Report

March 22, 2016

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## I. Introduction and Summary

The Annual Report for the Trust Fund for the People of the Federated States of Micronesia (the Fund) is presented per Article 20 of the Trust Fund Agreement between the governments of the United States and the Federated States of Micronesia:<sup>1</sup>

*“Within six months of the end of each Fiscal Year, the Joint Trust Fund Committee shall publish and shall submit to the Government of the United States and to the Government of the Federated States of Micronesia:*

- (a) an annual report on the activities and management of the Fund, including on the operations of the Accounts described in Article 16 of this Agreement, and on the effectiveness of the Fund to accomplish its purpose as described in Article 3 of this Agreement, which annual report may include recommendations regarding improving the effectiveness of the Fund to accomplish that purpose;*
- (b) the accounts of the Fund for that year audited in accordance with Article 19; and,*
- (c) reports of the Auditor under Article 19.”*

All documentation provided pursuant to Article 20 should be considered together.

The Annual Report’s information is mainly sourced from the annual financial statements prepared by the Fund’s bookkeeper and verified by the Fund’s auditor, and quarterly investment reports prepared by the Fund’s Investment Adviser with information from the Custodian. Any questions or comments regarding the Annual Report can be sent to Anthony Costanzo, Executive Administrator, at [apcostanzo@bgsi.net](mailto:apcostanzo@bgsi.net).


The Trust Fund Committee (the Committee) approved the Annual Report on 22 March 2015.

Summary highlights for FY15 are:

- The Fund’s restricted fiduciary net position value increased 4.3% to \$397,313,588 for FY15 from \$380,901,011 for FY14. The increase was primarily due to contributions from the United States government (\$26,976,960) and interest and dividend income from investments (\$19,765,695). There was a net investment income loss of -\$10,271,651.
- The Fund had a weighted annual rate of return of -2.6%, following three consecutive growth years: 9.1% for FY14, 14.4% for FY13, and 15.9% for FY12. On a performance basis, net of fees, the Fund lost 2.8% but outperformed the benchmark loss of 3.4%.
- No transfer was made to the C account for FY15 since there was no annual income earned over the 6% threshold.<sup>2</sup> The C account amounts to \$78,150,771 as of the end of

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<sup>1</sup> The full text of the Agreement between the Government of the United States of America and the Government of the Federated States of Micronesia Implementing Section 215 and 216 of the Compact, as Amended, Regarding a Trust Fund (the “Trust Fund Agreement”) and other relevant documents is available at [www.doi.gov/oia/press/trustfund/FSMTrustFunds](http://www.doi.gov/oia/press/trustfund/FSMTrustFunds).



FY15. The ending balance now reflects an approximate \$4,478,409 cumulative adjustment to the account from the A account given a change to the methodology to calculate the weighted annual rate of return to conform to the Global Investment Performance Standards (GIPS®). The change in the methodology was a result of a recommendation by an independent and objective external evaluation that occurred in FY15. The Committee adopted the recommendation by Resolution 2015-7 Weighted Annual Rate of Return and C Account Methodology Adjustment.

- Investment expenses increased to \$3,031,087 for FY15 from \$2,849,842 for FY14. As a percent of restricted fiduciary net position, investment expenses were at 0.76% for FY15 compared to 0.75% for FY14, in line with the Investment Policy Statement's agreed fee schedule.
- Administrative expenses increased to \$292,732 for FY15 from \$154,481 for FY14. As a percent of restricted fiduciary net position, administrative expenses increased to 0.07% for FY15 compared to 0.04% for FY14. The main reason for the increase was the contracting for the one-time independent and objective external evaluation. Without that cost, administrative expenses would be reduced to 0.04% of restricted fiduciary net position.
- An analysis by the Investment Advisor estimates that if the Fund were to achieve an average 8% return annually, the Fund would provide for FY24 an amount equivalent to 83.5% of estimated FY23 sector grant assistance with the partial inflation adjustment. There would also be a build-up of the C account but not to the maximum level permitted under the Trust Fund Agreement. Since inception, the Fund has an annual average growth rate of 4.6%, net of fees.
- The Trust Fund Committee contracted a firm to conduct an independent and objective external evaluation of the Fund to help guide the Trust Fund Committee as the Fund proceeds past the mid point of the 20-year build-up period that ends in FY23. The evaluation found the Fund to be generally well governed with competent Committee and service provider performance according to industry standards and no areas of non-compliance with the Trust Fund Agreement or Amended Compact.
- A major finding of the independent and objective external evaluation was that costs for investment and administrative services were within the ranges of similar trust, endowment, and foundation funds. The Committee has remained vigilant to contain such costs as an appropriate percentage of the Fund.

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<sup>2</sup> The C account contains any annual income on the Fund over 6%. The C account shall contain no more than three times the estimated equivalent of the fiscal year 2023 annual grant assistance, including the estimated inflation adjustment provided in the Amended Compact of Free Association (Section 217). After fiscal year 2023, the C account may be drawn on, to the extent it has sufficient funds, to address any shortfall in the B account, if income from the A account falls below the previous year's distribution adjusted for inflation. Transfers were made to the C account in fiscal years 2006, 2007, 2010, 2012, 2013, and 2014, the years with over 6% annual income. The A and C accounts are managed collectively and are only separated for accounting purposes.

- The main recommendations for improvement were:
  - Review and adjust the Investment Policy Statement's asset allocation strategy so that it conforms to Committee interests as the build-up period nears its end so capital is protected. If the Committee's interest is to protect capital, a more conservative investment strategy may be required, based on Investment Adviser advice. The Committee is working with the Investment Adviser to adjust the asset allocation by applying a "glide path" to investment allocation adjustments to FY23.
  - An adjustment to the methodology of the weighted annual rate of return calculation to conform to the Global Investment Performance Standards (GIPS®). As noted above, the Committee accepted the recommendation.
  - Review the objectives of the Fund during the distribution period in terms of possible distribution scenarios and eventually more fully define a distribution policy for the post FY23 distribution period.

## II. Trust Fund Background, Committee Updates, Contributions and Service Providers

### A. Trust Fund Background

The Compact of Free Association, as Amended (the “Amended Compact”) -- as codified in the Compact of Free Association Amendments Act of 2003 (U.S. Public Law 108-188, December 17, 2003; “the Amended Compact Act”) -- under Title Two: Economic Relations, Section 215, provides for the establishment of a trust fund in accordance with the Trust Fund Agreement between the Original Parties: the United States government (U.S. government) and the Federated States of Micronesia government (FSM government). Sections 215 through 217 of the Amended Compact set forth the funding to be contributed by both governments to 2023.

The Fund was incorporated as a non-profit corporation under the laws of the District of Columbia in August 2004. The Trust Fund Agreement is supported by a set of by-laws initially approved by the Committee on 24 March 2006. Resolutions are considered and approved periodically to improve the overall management and operations of the Fund, as determined by the Committee. The Investment Policy Statement provides the Fund’s main investment guidance. The latest version of the Investment Policy Statement was approved in September 2010 and was most recently amended in January 2014.

As stated in Article 3 of the Trust Fund Agreement:

*“The Purpose of the Fund is to contribute to the economic advancement and long-term budgetary self-reliance of the Federated States of Micronesia by providing an annual source of revenue, after Fiscal Year 2023, for assistance in the sectors described in Section 211 of the Compact, as amended, or other sectors as mutually agreed by the Original Parties, with priorities in education and health care.”*

The broad investment objective, as set forth in the Investment Policy Statement, is to:

*“maximize investment returns, subject to constraints aimed at containing fluctuations in returns over shorter periods within acceptable limits. Over shorter periods, outperformance will be sought relative to the notional return on a benchmark portfolio designed to reflect the risk profile according to which the assets are invested at the time.”*

### B. Trust Fund Committee Updates

Under Article 7 of the Trust Fund Agreement, the Trust Fund Committee’s functions include overseeing the:

1. Operation, supervision, and management of the Fund;

2. Investment and distribution of Fund resources; and
3. Conclusion of agreements and arrangements with Subsequent Contributors and other organizations.

For FY15, the Committee consisted of 5 members. According to the Trust Fund Agreement, the U.S. government maintains a majority of voting members including the Chairman. The FSM government appoints two voting members. Other voting or non-voting members may be appointed from Subsequent Contributors. Currently, the Fund does not have any Subsequent Contributors.

The FY15 Committee members were:

1. Nikolao Pula, Chairman (Department of the Interior), U.S.
2. Evelyn Adolph, Member (Office of the President), FSM
3. Stephen Schwartz, Member (Department of State), U.S.
4. Aren Palik, Member (Private Sector), FSM
5. Phil Maestri, Member (Department of Education), U.S.

Phil Maestri replaced Jeanette Lim during February 2015. Stephen Schwartz replaced J. Paul Reid during August 2015.

The Committee met quarterly during FY15 to review investment performance and conduct Fund business on the following dates. Minutes were recorded, approved, and signed for each meeting.

1. 9 December 2014 (Washington, DC-based teleconference)
2. 24 March 2015 (Washington, DC-based teleconference)
3. 23 June 2014 (Washington, DC-based teleconference)
4. 4 September 2015 (Honolulu, HI)

The Committee approved 9 resolutions in FY15. Following are the title and brief description of each resolution.

*FSM Resolution 2015-1      Independent and Objective Trust Fund Evaluation Search and Approval*

The resolution approved a request for proposals (RFP) process and terms of reference for a firm to conduct an objective and independent external evaluation of the Fund.

*FSM Resolution 2015-2      Independent and Objective Trust Fund Evaluation Firm Selection*

The resolution approved the selection of Funston Advisory Services LLC to conduct the independent and objective external evaluation. The resolution approved the contract amount and authorized the Chairman to sign the contract. The resolution also allowed the firm access to Fund records and service providers.

*FSM Resolution 2015-3*      *FSM Trust Fund Annual Report, Fiscal Year 2014*  
Approved the FY14 Annual Report and approved the transmission of the Annual Report and Audited Financial Statements to the respective governments.

*FSM Resolution 2015-4*      *Executive Administrator Contract Renewal*

The resolution approved the Executive Administrator's contract for the period 4/6/15 to 10/5/15, pending the completion of the external evaluation.

*FSM Resolution 2015-5*      *Engagement Agreement with Baker Tilly LLP for Audit Services FY15 and FY16*

The resolution authorized the Chairman to sign client agreements with Baker Tilly, the Fund's auditor, for the FY15 and FY16 audits. The resolution also approved each agreement's amount.

*FSM Resolution 2015-6*      *FY15 Budget Approval*

The resolution approved an FY15 budget for investment adviser, custodial, and administrative expenses. The resolution also included reporting procedures if the budget categories are exceeded.

*FSM Resolution 2015-7*      *Weighted Annual Rate of Return and C Account Calculation Methodology Adjustment*

The resolution approved the adjustment of the weighted annual rate of return and C account calculation methodology to conform to the Global Investment Performance Standard (GIPS®) utilizing the Modified Dietz Method. The adjustment is a result of the recommendation to follow GIPS® standards made by the independent and objective external evaluation conducted during FY15. The resolution also authorized the Fund's bookkeeper (Bookminders) to adjust the calculations from FY05 to FY14. The resolution indicated the adjusted values would be reported in the FY15 Annual Report and, as necessary, in the FY15 audited financial statements.

*FSM Resolution 2015-8*      *Executive Administrator Contract Renewal*

The resolution approved the Executive Administrator's contract for the period 10/5/15 to 10/4/17. The resolution also approved the hourly rate and reimbursements for Committee-approved quarterly expenses and Fund-related meetings in the Federated States of Micronesia once annually.

*FSM Resolution 2015-9*      *Engagement Agreement with Bookminders for Accounting Support Services*

Approved a service proposal with Bookminders for accounting services for a 12-month period as of 9/7/15 and a maximum amount for those services.

### C. Contributions to the Fund

The U.S. contributed \$26,976,960 on 6 October 2014, per Table 1.

Contributions to the Fund by the U.S. and FSM governments are governed by the schedule in Section 216 of the Amended Compact. The U.S. government is obligated to contribute \$16 million in FY04 through FY06 and to contribute \$16 million, plus a cumulative amount that increases by \$0.8 million annually beginning in FY07, until FY23. This additional amount corresponds to the amount by which direct sector grant assistance provided under the Amended Compact is reduced in that fiscal year. A partial inflation adjustment is also added to the amount of the U.S. contribution as indicated in the Amended Compact.<sup>3</sup> The FSM government was to contribute at least \$30 million prior to 30 September 2004. Initial contributions began in FY05 as the U.S. contribution was dependent on the FSM contribution that occurred in FY05.

**Table 1: Contributions to the Trust Fund through FY15**  
Dollars in millions

Year	U.S.	FSM	Total
<b>FY04</b>	0.00	0.00	0.00
Date Contributed			
<b>FY05</b>	32.19	30.30	62.49
Date Contributed	10/5/04	10/1/04	
<b>FY06</b>	16.44		16.44
Date Contributed	10/6/05		
<b>FY07</b>	17.69		17.69
Date Contributed	10/6/06		
<b>FY08</b>	19.00		19.00
Date Contributed	10/9/07		
<b>FY09</b>	20.91		20.91
Date Contributed	10/6/08		
<b>FY10</b>	21.52		21.52
Date Contributed	10/2/09		
<b>FY11</b>	22.39		22.39
Date Contributed	10/14/10		
<b>FY12</b>	23.59		23.59
Date Contributed	10/14/11		
<b>FY13</b>	24.99		24.99
Date Contributed	10/4/12		
<b>FY14</b>	26.10		26.10
Date Contributed	10/21/13		

<sup>3</sup> As stated in Section 217 of the Amended Compact, the U.S. government contribution “shall be adjusted for each United States Fiscal Year by the percent that equals two-thirds of the percent change in the United States Gross Domestic Product Implicit Price Deflator, or 5 percent, whichever is less in any one year, using the beginning of Fiscal Year 2004 as a base.”



Year	U.S.	FSM	Total
<b>FY15</b>	27.00		27.00
Date Contributed	10/6/14		
<b>Invested to Date</b>	<b>\$251.82</b>	<b>\$30.30</b>	<b>\$282.12</b>

Source: Trust Fund for the People of the Federated States of Micronesia Financial Statements, September 30, 2015 and 2014

## D. Service Providers

### **Executive Administrator**

The Fund contracts an Executive Administrator who serves in support of the governance, administration, and operations of the Fund. The current Executive Administrator began providing services in April 2011 and is contracted through October 2017 per FSM Resolution 2015-8.

The Executive Administrator's key duties are to maintain all official Committee documents and records; update the Chairman and Committee members on Fund activities; maintain agreements with and coordinate Fund service providers; provide administrative services regarding payments, decisions and deliberations; assist in audit preparation and prepare the annual report; prepare periodic performance and other assessments to inform Committee members and staff; organize, conduct and provide follow-up for the four quarterly review meetings including meeting agenda, support documents and meeting minute preparation; and coordinate with U.S. and FSM government members and staff in support of the above activities.

### **Custodian**

State Street Bank and Trust Company (State Street), as the Custodian, provides all the services of the Trust Fund Agreement's Article 13. In addition, they also provide a record keeping function and maintain a web site portal for Fund financial information. Key services provided, consistent with Article 13, include:

- Collect and receive any and all money and other property of whatever kind or nature due or owing or belonging to the Fund.
- Follow written directions of the Committee with respect to retention, purchase, sale or encumbrance of trust property, and the investment and reinvestment of principal and income.
- Disburse income or corpus only pursuant to the conditions set forth in the Trust Fund Agreement.
- Make all payment of liabilities and administrative expenses.
- Provide plan accounting that helps track each contributor's balance and the C account.<sup>4</sup>

<sup>4</sup> Plan accounting is a breakdown of the Fund by contributor (U.S. and FSM governments) and by the A and C account. The breakdown allows the allocation of contributions, investment gains and losses, and expenses to each contributor and helps to calculate the proportions of each contributor of the A and C accounts.

State Street's fee is 3 basis points annually of the Fund's value assessed quarterly plus an additional flat fee -- a Supplemental Custody and Accounting Fee. State Street has served as Custodian since September 2010.

### **Investment Adviser and Money Managers**

Mercer Investment Management, Inc. (Mercer), serves as Fund Investment Adviser and as a Money Manager, providing the services described in Article 14 of the Trust Fund Agreement. The Fund also engages other Money Managers with non-discretionary oversight provided by Mercer. Key services provided include:

- Advise and recommend to the Committee one or more Money Managers who will invest the assets of the Fund to produce a diversified portfolio.
- Provide the Committee with data relating to any prospective Money Manager, indicating performance and relevant comparisons with similar Money Managers to assist the Committee in evaluating the performance of the prospective Money Managers.
- Direct trades and manage liquidity, amongst other Money Manager-type functions.
- Provide monthly and quarterly performance reports on all Fund assets and compare performance to agreed upon industry standard benchmarks and to similar trusts, endowments and foundations within the Mercer client pool.

Mercer has served as the Fund's Investment Adviser since 2005. Mercer is currently engaged under a contract between Mercer and the Committee signed in September 2010. Mercer's managed asset fee (including sub-advisors) is 63 basis points annually. It is assessed daily with one part of the managed asset fee as compensation for Mercer's services and another as compensation to underlying Money Managers who are independent of Mercer. The fee rate was agreed to in December 2013 per FSM Resolution 2014-1 Fixed Income Asset Category Adjustment and was applied beginning in February 2014.


In addition, Mercer applies a 9 basis point annual advisory fee on the non-discretionary assets. Each of the non-discretionary asset allocations has a Money Manager. Each non-discretionary Money Manager charges its own rates on the assets it invests which range from 0.70 to 1.25 basis points. These Money Managers are identified in Table 3, below, under Non-Discretionary Funds. The fee schedule is provided as Attachment 1.

### **Bookkeeper**

Bookminders has prepared the Fund's financial records since inception in 2004. Bookminders produces monthly financial statements and the annual financial statements that include the year-end reporting package with supporting schedules for the annual audit. The service agreement with Bookminders was extended by one year to September 2016 per FSM Resolution 2015-9.

### **Auditor**

Baker Tilly Virchow Krause, LLP serves as the Fund's auditor. Baker Tilly conducts the audits in accordance with U.S. Generally Accepted Auditing Standards and Generally Accepted



Government Auditing Standards issued by the Comptroller General of the United States. FSM Resolution 2015-5 authorized the audit services for the FY15 and FY16 audits. ParenteBeard has performed the annual audits dating back to FY04. On 1 October 2014 ParenteBeard LLC combined with Baker Tilly Virchow Krause, LLP.

### **Legal Counsel**

Vorys, Sater, Seymour and Pease LLP (Vorys) provides support, as requested by the Committee, on any legal matters per a Letter of Engagement and Representation. Vorys has served as legal counsel since February 2012.

### **External Evaluator**

The Committee determined that an external evaluation by an independent and objective external evaluator be conducted in FY15 since the Trust Fund passed the mid-point of its 20-year build-up. Resolution FSM 2015-1 approved a terms of reference and RFP process for the external evaluation. Resolution FSM 2015-2 appointed Funston Advisory Services LLC to conduct the evaluation. The external evaluation covered management and administration; investment allocation, benchmarks, and performance; and service providers' fees and performance.

### III. FY15 Account Balances and Performance

#### A. Changes to Trust Fund Asset Classes and Allocations

There were no major asset allocation changes for FY15, as indicated in Tables 2 and 3.<sup>5</sup> The adjustments that did occur were a result of the past asset allocations in prior years. These changes included transferring all fixed income assets to the managed asset strategy of the portfolio during FY14. Also, the build-up of the managed hedge fund and private equity fund (both “funds of funds,”<sup>6</sup>) continued from FY14 into FY15 and is expected to continue in future fiscal years, especially for the private equity assets as the non-discretionary private equity assets mature.

For FY15, the portfolio’s managed assets consisted of U.S. equity (small, medium, and large cap asset strategy), non-U.S. equity (international developed and emerging market asset strategy), and fixed income (core fixed income and opportunistic fixed income strategy). The portfolio’s non-discretionary component consisted of private real estate, a hedge fund, and private equity.

**Table 2: Investment Policy Statement Asset Allocations and Targets, FY14 and FY15**

Asset Class	Strategic Target Allocation & Permitted Range 9/30/14	Strategic Target Allocation & Permitted Range 9/30/15	Allocation as of 9/30/14	Allocation as of 9/30/15	Actual % Difference
<b>Managed Assets</b>					
<b>Domestic Equity</b>	25.5% 20.5%-30.5%	25.5% 20.5%-30.5%	28.3%	26.5%	-1.8%
U.S. Large Cap Equity	18%	18%	20.6%	19.1%	-1.5%
U.S. Small/Med Cap Equity	7.5%	7.5%	7.7%	7.4%	-0.3%
<b>Non-U.S. Equity</b>	25.5% 20.5%-30.5%	25.5% 20.5%-30.5%	26.6%	25.3%	-1.3%
<b>Fixed Income</b>	19% 14%-24%	19% 14%-24%	19.8%	18.3%	-1.5%
Core Fixed Income	2.50%	2.5%	2.7%	2.7%	0.0%
Opportunistic Fixed Income	16.50%	16.5%	17.1%	15.6%	-1.5%
<b>Hedge Fund (Managed)</b>	5.5 3%-8%	5.5 3%-8%	4.8%	6.0%	1.2%

<sup>5</sup> The Investment Policy Statement asset allocations and targets are provided in Table 2 and the individual asset changes are provided in Table 3.

<sup>6</sup> A “fund of funds” is a combination of multiple independent funds managed by sub-advisers who are contracted to Mercer.

Asset Class	Strategic Target Allocation & Permitted Range 9/30/14	Strategic Target Allocation & Permitted Range 9/30/15	Allocation as of 9/30/14	Allocation as of 9/30/15	Actual % Difference
Private Equity Fund (Managed)	0% 0%-10%	0% 0%-10%	1.3%	3.2%	1.9%
<b>Total Managed Assets</b>	<b>75.5%</b>	<b>75.5%</b>	<b>80.8%</b>	<b>79.3%</b>	<b>-1.5%</b>
<b>Non-Discretionary Assets</b>					
Private Equity*	9.5% 0%-10%	9.5% 0%-10%	5.0%	4.0%	-1.0%
Private Real Estate	10% 5%-15%	10% 5%-15%	9.8%	12.3%	2.5%
Hedge Fund	5% 2.5%-7.5%	5% 2.5%-7.5%	4.3%	4.3%	0.0%
Cash	0% 0%-3%	0% 0%-3%	0.1%	0.1%	0.0%
<b>Total Non-Discretionary</b>	<b>25%</b>	<b>24.5%</b>	<b>19.2%</b>	<b>20.7%</b>	<b>1.5%</b>
<b>Total</b>	<b>100%</b>	<b>100%</b>	<b>100.0%</b>	<b>100.0%</b>	

\*Allocation to Non-Discretionary Private Equity will shift to Managed Assets Private Equity as capital is called for that fund.

Source: Investment Policy Statement, December 2013 amendment; Mercer Quarterly Reports- September 30, 2014 and September 30, 2015.

**Table 3: Asset Change FY14 to FY15**

Asset Class	Assets Held as of 9/30/14	Assets Held as of 9/30/15
<b>Managed Assets</b>		
<b>Domestic Equity</b>		
U.S. Large Cap Equity	SSgA S&P 500 Index Fund	SSgA S&P 500 Index Fund
U.S. Small/Med Cap Equity	Mercer Small/Mid Cap Growth Equity Fund Mercer Small/Mid Cap Value Equity Fund	Mercer Small/Mid Cap Growth Equity Fund Mercer Small/Mid Cap Value Equity Fund
<b>Non-U.S. Equity</b>	Mercer Non-U.S. Core Equity Fund Mercer Emerging Markets Equity	Mercer Non-U.S. Core Equity Fund Mercer Emerging Markets Equity
<b>Fixed Income</b>	Mercer Core Fixed Income Fund Mercer Opportunistic Fixed Income	Mercer Core Fixed Income Fund Mercer Opportunistic Fixed Income
<b>Hedge Fund</b>	Mercer Hedge Fund Investors	Mercer Hedge Fund Investors
<b>Private Equity</b>	Mercer Private Investment Partners III	Mercer Private Investment Partners III

Asset Class	Assets Held as of 9/30/14	Assets Held as of 9/30/15
<b>Non-Discretionary Funds</b>		
<b>Private Equity</b>	HarbourVest Partners- VIII Venture Fund; VIII Buyout Fund; VIII Mezzanine & Distressed Debt Fund; Private Equity V Portfolio Advisors Private Equity Fund I	HarbourVest Partners- VIII Venture Fund; VIII Buyout Fund; VIII Mezzanine & Distressed Debt Fund; Private Equity V Portfolio Advisors Private Equity Fund I
<b>Private Real Estate</b>	Prudential Real Estate Investors	Prudential Real Estate Investors
<b>Hedge Fund</b>	Blackstone Alternative Asset Management	Blackstone Alternative Asset Management

Source: Trust Fund for the People of the Federated States of Micronesia Investment Performance, September 30, 2014 and September 30, 2015, Mercer Investment Management.

Fund performance is measured utilizing a set of performance standards established in the Investment Policy Statement. Individual asset class benchmarks are identified in the Statement, and the Investment Adviser also measures performance according to its Total Trust Benchmark and Foundation Performance Universe Median. A summary of benchmarks for the entire Fund and for each asset class is provided as Attachment 2. Table 6 provides information on the Fund's annual performance compared to the relevant benchmarks.

### B. Summary of FY15 Performance and Expenses

The Fund ended FY15 with a net position of \$397,313,588. The amount is a 4.3% gain from FY14, as shown in Table 4. The gain is mainly attributable to two factors: 1) continued and increasing U.S. contributions; and 2) investment gains and losses with overall losses resulting in negative gross investment income (-\$9,153,078).

The U.S. contribution increased to \$26,976,960 based on the FY15 scheduled amount per the Amended Compact, including the partial inflation adjustment. No other contributions were provided to the Fund.

Net investment income was -\$10,271,651, a significant decrease from the \$31,867,396 gain in FY14. Investment income was mainly a result of positive interest and dividend income (\$19,765,695), and negative realized and unrealized gains, other income losses and investment expenses (totaling -\$28,918,773). Annual net positions since inception are provided in Attachment 3, Table A.

**Table 4: Trust Fund Income Change FY13- FY14 and Percent Change**

	FY14	FY15	% Change
<b>Additions</b>			
<b>Contributions</b>			
U.S. Government	<u>26,104,960</u>	<u>26,976,960</u>	3.3%

	FY14	FY15	% Change
<b>Investment Income</b>			
Interest and dividends	12,348,471	19,765,695	60.1%
Net increase in the fair value of investments	<u>20,624,284</u>	<u>(28,918,773)</u>	-240.2%
Gross investment income	32,972,755	(9,153,078)	-127.8%
<b>Less: Investment expenses</b>			
	<u>1,105,359</u>	<u>1,118,573</u>	1.2%
Net investment income	<u>31,867,396</u>	<u>(10,271,651)</u>	-132.2%
Total additions	<u>57,972,356</u>	<u>16,705,309</u>	-71.2%
<b>Deductions</b>			
Administrative expenses	<u>154,481</u>	<u>292,732</u>	89.5%
Change in net position	57,817,875	16,412,577	-71.6%
<b>Restricted Net Position, Beginning</b>	<b><u>323,083,136</u></b>	<b><u>380,901,011</u></b>	17.9%
<b>Restricted Net Position, Ending</b>	<b>380,901,011</b>	<b>397,313,588</b>	<b>4.3%</b>

Source: Trust Fund for the People of the Federated States of Micronesia Financial Statement, September 30, 2015 and 2014

Note: Investment expenses do not reflect Money Manager fees directly subtracted from Fund asset values. These expenses are reflected in Table 5. Amounts rounded to the nearest dollar.

Total Fund expenses increased by 10.6% compared to FY14, per Table 5, and increased as a total percentage of the Fund's net position to 0.84% compared to 0.79% for FY14 ending a downward trend in Fund expenses as a percentage of net position from FY12. All expenses are within those rates agreed to by the Committee. Annual expense history since inception is provided in Attachment 3, Table B.

**Table 5: Investment and Administrative Expenses, FY14 and FY15**

	FY14	FY15	% Change
<b>Investment Expenses</b>	<b>\$2,849,842</b>	<b>\$3,031,087</b>	<b>6.4%</b>
Custodian	98,437	99,777	1.4%
Investment Adviser	402,713	426,352	5.9%
Money Manager	604,209	592,444	-1.9%
Money Manager*	1,744,483	1,912,514	9.6%
<i>% of Net Position</i>	<i>0.75%</i>	<i>0.76%</i>	<i>1.23%</i>

	FY14	FY15	% Change
<b>Administrative Expenses</b>	<b>\$154,481</b>	<b>\$292,732</b>	<b>89.5%</b>
Executive Administrator	99,904	105,756	5.9%
Audit Fees	42,395	41,994	-0.9%
Accounting Fees	6,059	6,036	-0.4%
Legal Fees	376	2,997	697.0%
Miscellaneous	5,747	135,949	2265.4%
<i>% of Net Position</i>	<i>0.04%</i>	<i>0.07%</i>	<i>54.1%</i>
<b>Total Dollar Expenses</b>	<b>\$3,004,323</b>	<b>\$3,323,819</b>	<b>10.6%</b>
<b>Total % of Net Position</b>	<b>0.79%</b>	<b>0.84%</b>	<b>6.1%</b>

Note: Amounts rounded to nearest dollar.

\* Money Manager Fees directly subtracted from Fund asset value.

Source: FY14 and FY15 Annual Audited Annual Financial Statements and Fund Data Collection

Custodian expense increased 1.4% mainly due to the Fund's increased value.

The Investment Adviser's expense increased 5.9% to \$426,352. Total Money Manager fees increased 6.6% to \$2,504,958.<sup>7</sup> Money Manager fees are based on the amount of assets being managed. The investment expense increase was due to the 4.3% increase in value of the Fund on which the fees are based, driven by additional contributions and market appreciation during points of the year, as well as full asset strategy implementation for the entire fiscal year based on a fee adjustment made during fiscal year 2014.<sup>8</sup> The Investment Adviser category also includes the 9 basis point fee for non-discretionary asset oversight by the Investment Adviser.

Administrative expenses increased by 89.5% for FY15 totaling \$292,732 compared to \$154,481 for FY14. The increase was mainly due to the contracting of a firm to conduct an independent and objective external evaluation of the Fund as described above by FSM Resolution 2015-2 Independent and Objective Trust Fund Evaluation Firm Selection. Eliminating that contract cost, contained in the 'Miscellaneous' category, administrative expenses would have decreased to .04% of net position and the total percent of net position would have decreased to 0.80%, just above the 0.79% for FY14. Executive Administrator expenses increased mainly based on the support and follow-up to the external evaluation. Legal fees increased based on additional legal counsel use. And, accounting and audit fees decreased because of less accounting time requirements and a smooth FY14 audit process, respectively.

The Fund's annual audit was completed in March 2016, within the 6 month time period after the end of the previous fiscal year, as required per the Trust Fund Agreement. The audit is according to generally accepted U.S. accounting standards and U.S. *Government Auditing Standards* issued by the Comptroller General of the United States. The standard includes the design, implementation, and maintenance of internal control relevant to the preparation and fair

<sup>7</sup> Money Manager fees range from 0.70% to 1.25% of assets under their respective management.

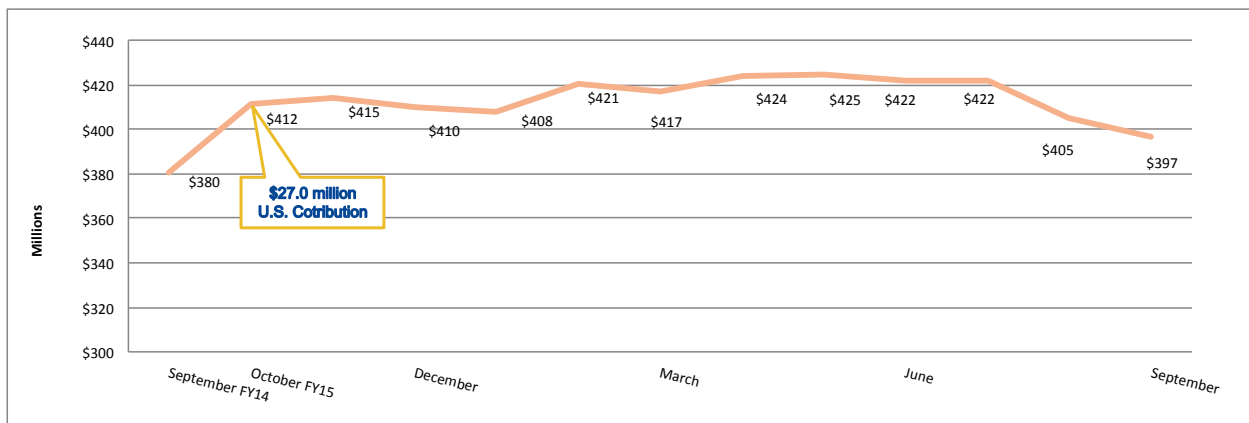
<sup>8</sup> The Investment Adviser fee increased to 63 basis points from 58 basis points for the managed assets during the second quarter of FY14 so for FY15 the new fee amount was charged for the entire fiscal year.



presentation of financial statements that are free from material misstatement, whether due to fraud or error. The audit found no deficiency in internal control over finance reporting and found that there were no instances of non-compliance or other matters that are required to be reported under *Government Auditing Standards*.

Per Figure 1, the Fund followed the moderate to negative performance of U.S. and non-U.S. public equity markets throughout the fiscal year. An increase in the Fund value occurred when the U.S. contribution was deposited in addition to when positive investment performance was experienced. The Fund was most negatively impacted by the August-September financial market downturn.

**Figure 1: FY15 Monthly Trust Fund Net Position**  
Dollars in millions



Source: Mercer Monthly Reports; contribution information from State Street Statement

For the fiscal year, in terms of performance measurement, the Fund decreased -2.8% net of fees.<sup>9</sup> The return rate outperformed the Total Trust Benchmark of -3.4%.<sup>10</sup> The Fund was negatively impacted by the poor performance of U.S. and non-U.S. public equities as well as fixed income assets. The Fund was positively impacted by the performance of the non-discretionary assets and the managed hedge fund and private equity fund.

Table 6 provides Fund performance measures for the fund as whole, per portfolio category (managed assets and non discretionary assets), and per asset strategy, net of fees.

<sup>9</sup> The performance rates in this section are from the Mercer September 30, 2015 Quarterly Report and other updates since that time. The report contains performance measurements over different time periods and comparisons to various benchmarks for the fund as a whole, asset categories, and individual asset strategies. The rates are different than the weighted annual rate of return that results from the audited asset values and all expenses including accrued expenses. The weighted return includes weighted earnings, expenses and contributions for a more true performance measurement. Figure 4 contains the dollar-weighted annual rate of return.

<sup>10</sup> As of 1/1/14, the Total Trust Benchmark is comprised of 25.5% Russell 3000, 25.5% MSCI ACWIxU.S. Net Dividend, 19.0% fixed income benchmark, 10% NCREIF NFI ODCE, 9.5% S&P 500+3%, and 10.5% T-Bills+3%.

**Table 6: Periodic and Since Inception Performance Compared to Benchmarks**

	Market Value 9/30/15	%	FY15	3 Years	5 Years	Since Inception	Date of Inception
<b>Total Fund</b>	<b>\$396,692,319</b>	<b>100.00%</b>	<b>-2.80%</b>	<b>6.50%</b>	<b>6.90%</b>	<b>4.60%</b>	<b>Sep. 2004</b>
Total Trust Benchmark			-3.40%	6.90%	7.70%	5.00%	
<b>Total Managed Assets</b>	<b>\$315,039,582</b>	<b>79.30%</b>	<b>-6.10%</b>	<b>6.50%</b>	<b>NA</b>	<b>6.10%</b>	<b>Oct. 2010</b>
<b>U.S. Domestic Equity</b>	<b>\$105,541,165</b>	<b>26.60%</b>	<b>-1.00%</b>	<b>11.70%</b>	<b>12.60%</b>	<b>6.90%</b>	<b>Jul. 2006</b>
Russell 3000 Index			-0.50%	12.50%	13.30%	7.00%	
U.S. Large Cap Equity	\$75,823,646	19.10%	-0.60%	12.40%	NA	12.70%	Oct. 2010
S&P 500			-0.60%	12.40%	13.30%	12.70%	
U.S. Small/Mid Cap Equity	\$29,717,519	7.40%	-1.50%	10.30%	NA	10.50%	Oct. 2010
Russell 2500			0.40%	12.40%	12.70%	12.10%	
<b>Non-U.S. Equity</b>	<b>\$100,347,250</b>	<b>25.30%</b>	<b>-8.50%</b>	<b>5.10%</b>	<b>3.30%</b>	<b>3.10%</b>	<b>Jul. 2006</b>
Total Non-U.S. Equity Benchmark			-12.20%	2.30%	1.90%	0.50%	
Mercer Non-U.S. Core Equity	\$80,591,038	20.30%	-6.00%	7.60%	NA	4.50%	Oct. 2010
MSCI EAFE			-8.70%	5.60%	4.00%	3.30%	
Mercer Emerging Markets Equity	\$19,756,212	5.00%	-17.80%	-4.50%	NA	-3.90%	May. 2012
MSCI Emerging Markets			-19.30%	-5.30%	-3.60%	-4.80%	
<b>Fixed Income</b>	<b>\$72,685,789</b>	<b>18.30%</b>	<b>-12.90%</b>	<b>-3.80%</b>	<b>NA</b>	<b>-0.10%</b>	<b>Oct. 2010</b>
Fixed Income Benchmark			-10.80%	-2.70%	0.40%	0.30%	
Fixed Income - Core	\$10,623,438	2.70%	2.00%	1.90%	NA	3.50%	Oct. 2010
Barclays Aggregate			2.90%	1.70%	3.10%	3.10%	
Fixed Income - Opportunistic Custom Opportunistic Fixed Income Benchmark	\$62,062,351	15.60%	-15.10%	NA	NA	-5.20%	Aug. 2013
			-12.70%	NA	NA	-3.90%	
<b>Hedge Fund (managed)</b>	<b>\$23,278,815</b>	<b>5.90%</b>	<b>1.50%</b>	<b>NA</b>	<b>NA</b>	<b>7.00%</b>	<b>Oct. 2012</b>
T-Bills +3%			3.00%	3.00%	3.00%	3.00%	
HFRI Fund of Funds Composite Index			0.00%	4.20%	2.70%	4.40%	

<b>Private Equity (managed)</b>	\$12,800,579	3.20%	9.60%	NA	NA	-4.10%	Apr. 2013
S&P 500 +3%			2.40%	15.70%	16.70%	13.50%	
Burgiss Global Private Equity Index			10.90%	13.80%	14.30%	14.30%	
<b>Total Non Discretionary Assets</b>	<b>\$82,038,722</b>	<b>20.70%</b>	<b>11.80%</b>	<b>9.80%</b>	<b>10.20%</b>	<b>6.00%</b>	<b>Oct. 2004</b>
<b>Real Estate</b>	<b>\$48,794,837</b>	<b>12.30%</b>	<b>14.90%</b>	<b>13.00%</b>	<b>14.20%</b>	<b>2.50%</b>	<b>Mar. 2008</b>
NCREIF NFI ODCE			14.90%	13.40%	14.00%	3.90%	
<b>Hedge Fund</b>	<b>\$16,980,397</b>	<b>4.30%</b>	<b>3.20%</b>	<b>6.80%</b>	<b>5.60%</b>	<b>5.60%</b>	<b>Dec. 2009</b>
T-Bills +3%			3.00%	3.00%	3.00%	3.10%	
<b>Private Markets (Private Equity)</b>	<b>\$15,771,689</b>	<b>4.00%</b>	<b>14.40%</b>	<b>14.40%</b>	<b>14.00%</b>	<b>7.20%</b>	<b>Sep. 2006</b>
S&P 500 +3%			2.40%	15.70%	16.70%	9.50%	
Burgiss Global Private Equity Index			10.90%	13.80%	14.30%	11.20%	
Cash	\$491,799	0.10%					

Source: Mercer Quarterly Report, Period Ending September 30, 2015 and updates provided by Mercer  
Notes: NA= Not Available; percents based on performance, net of fees

The Fund's asset class performance is described below, net of fees.

Total managed assets (79.3% of Fund value as of September 30, 2015) had a performance loss of -6.1 based on losses in the U.S. and non-U.S. public equity strategies and the fixed income strategy.

U.S. domestic equity investments (26.6% of the portfolio) decreased -1.0% compared to a benchmark return of -0.5%. The large cap fund decreased -0.6% equaling its benchmark. The small/mid cap equity strategy was down 1.5%, underperforming its benchmark of a 0.4% gain.

The non-U.S. equity strategy (25.3% of the portfolio) declined more significantly by -8.50% but outperformed its benchmark that had a -12.2% decline. The non-U.S. core equity asset had a return of -6.0, outperforming its benchmark of -8.7. The emerging market equity asset contributed to the asset strategy's significant decline by losing -17.8% yet outperforming its benchmark of -19.3%.

The fixed income strategy (18.3% of the portfolio) also had a significant decline by -12.9%, underperforming its benchmark return of -10.8%. The core income asset returned 2.0%, underperforming its benchmark that had a 2.9% return. The opportunistic fixed income asset returned -15.1% underperforming its benchmark (-12.7%).

The managed hedge fund strategy (5.9% of the portfolio) gained 1.5%, underperforming its benchmark that returned 3.0%.

The managed private equity fund strategy slightly grew as a component of the portfolio in FY15 (3.2% of the portfolio for FY15 compared to 1.0% for FY14) and has become a positive contributor to returns as of the end of FY15 returning 9.6%, far outperforming a benchmark of 2.4%. Given the nature of private equity funds, the fund will continue to call capital over the next several years as the underlying Money Managers invest in private equity deals that may or may not come to fruition for several years. The managed private equity fund should also be considered with the more mature private equity investments, described below.

The non-discretionary assets comprised 20.7% of the portfolio. The component outperformed the managed asset component with an overall 11.8% performance increase for FY15, providing additive returns to the Fund.

The real estate strategy (12.3% of the portfolio) had another significant annual gain with an 11.8% return, yet underperformed its benchmark of 14.9%. The gain followed three years with similar gains (12.1% for FY14, 11.9% for FY13, and 10.4% for FY12).

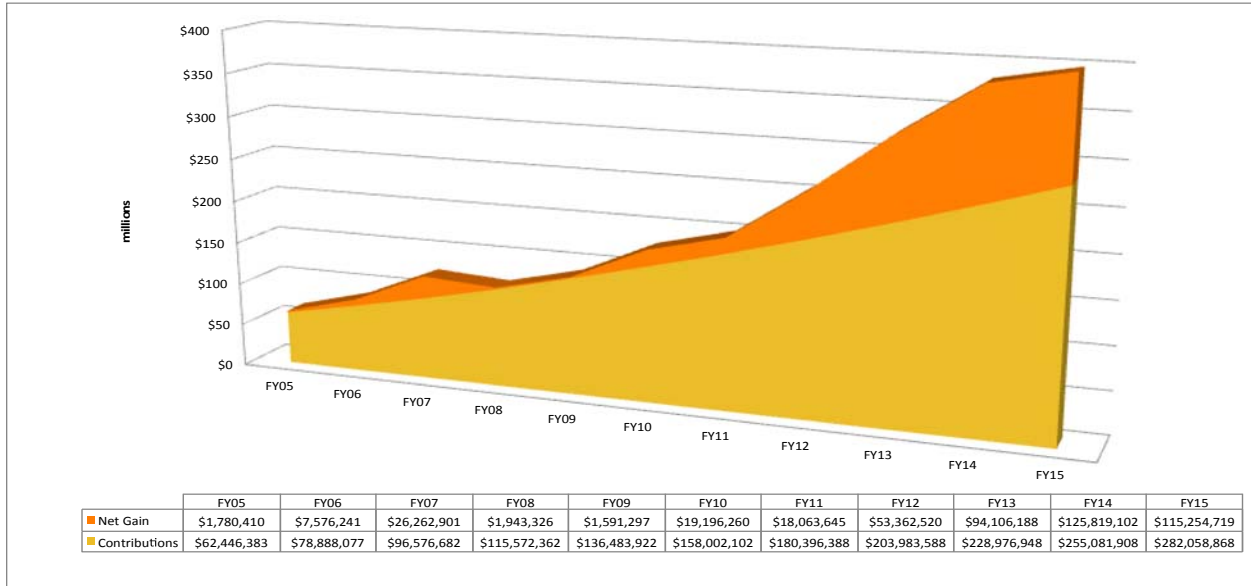
The non-discretionary hedge fund (4.3% of the portfolio) gained 3.2%, just above its benchmark of 3.0%.

The non-discretionary private equity strategy (4.0% of the portfolio) gained 14.4%, well above the benchmark return of 2.4% (S&P 500 +3%) and above the Burgiss Global Private Equity Index (10.9% gain). For the more mature non-discretionary private equity strategy, distributions from the investments are being realized. As of the end of FY15, for both the managed and non-discretionary private equity strategy, the Fund had paid in capital of \$35,161,129 of a total \$59,811,000 commitment. Since the inception of these investments, \$18,213,429 in distributions were received resulting in a 7.9% net internal rate of return that compares to a 6.9% net internal rate of return up to the end of FY14.

As of the end of FY15, the Fund's average annual return rate since inception was 4.6%, net of fees, slightly underperforming the Total Trust Benchmark (5.0%). The FY15 gain was a decrease from the FY14 average annual return rate of 5.3%.

Figure 2 shows the growth of the Fund with a steady incline of contributions and the periodic investment income gains and losses. As of FY15 a total of \$282,058,868 has been contributed to the Fund. The U.S. government provided 89.3% of total contributions and the FSM government provided 10.7%. As of the end of FY15, the Fund has gained a total of \$115,254,719 from those contributions - 40.9% of the value of the contributions. No contributor's capital investment has been diminished since Fund inception.

**Figure 2: Total Cumulative Contribution and Net Position Annual Gain, FY04-FY15**



Source: Audited Financial Statements FY04-FY15

### C. The C Account

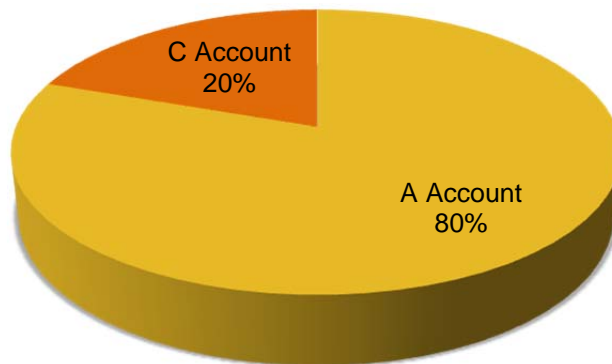
Article 16 of the Trust Fund Agreement requires that any annual income on the Fund over 6% (up to a specific limit) shall be transferred to the C account. The C account may be drawn upon, to the extent it contains sufficient funds, to address any shortfall in the B account after FY23, if income on the A account falls below the previous year's distribution adjusted for inflation and for Special Needs agreed to by the Committee.

The C account is maintained as a sub account for accounting purposes. It is not invested separately but as part of the overall corpus. The end-of-year financial statements provide a calculation to determine if the Fund achieved

the 6% annual income threshold and, if so, the amount to be transferred to the C account. Also, the breakdown of the A and C accounts is reported annually by contributor as shown in Table 7. Historical account balances are provided as Attachment 3, Table C.

**Figure 3: FY15 A and C Account Breakdown**

Source: FY15 Audited Financial Statements



Given the negative annual performance and investment losses in FY15, the 6% threshold was not surpassed for FY15. Therefore, no transfer was made to the C account. The C account value remains the same as in FY14 at \$78,150,771.

**Table 7: A and C Account Net Position Balances, FY14-FY15**

	FY14	FY15	FY15 % of Account
<b>Total Assets</b>	<b>\$380,901,010</b>	<b>\$397,313,587</b>	
<b>A Account</b>	<b>\$302,750,239</b>	<b>\$319,162,816</b>	<b>100.00%</b>
U.S.	\$265,649,090	\$282,447,788	88.50%
FSM	\$37,101,149	\$36,715,028	11.50%
<b>C Account</b>	<b>\$78,150,771</b>	<b>\$78,150,771</b>	<b>100.00%</b>
U.S.	68,573,625	\$69,160,665	88.50%
FSM	\$9,577,146	\$8,990,107	11.50%

Note: Amounts rounded to the nearest dollar.

Source: Audited Annual Financial Statements FY14 and FY15 and Fund recalculations

The C account has gained income in FY06, FY07, FY10, FY12, FY13, and FY14. Per the Trust Fund Agreement, the C account is allowed to contain up to three times the estimated equivalent of the Amended Compact's FY23 sector grant assistance plus an inflation adjustment. The current amount in the C account is 98.0% of estimated annual Amended Compact sector grant assistance for FY23.

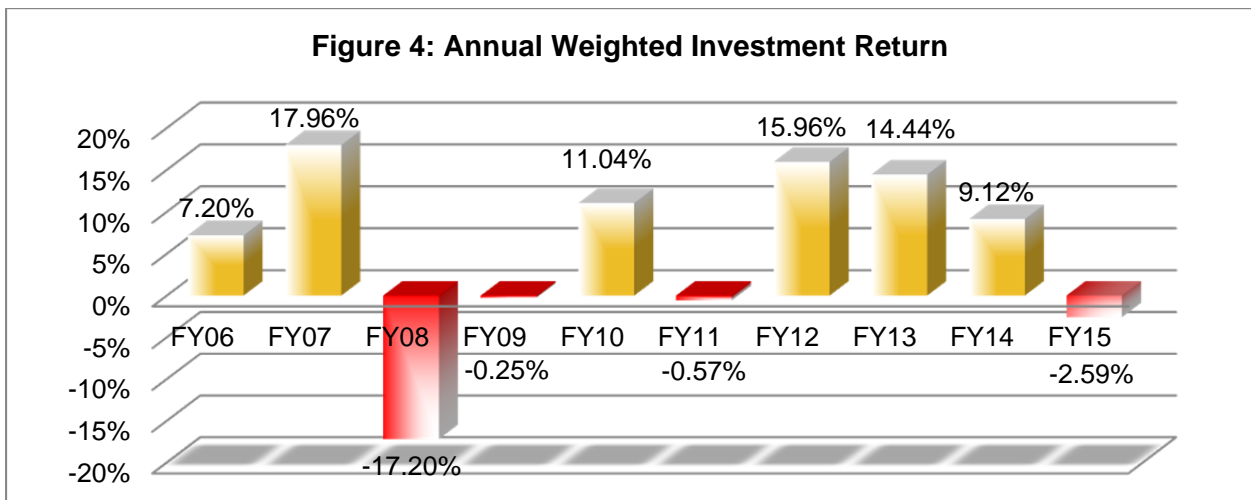
In addition, the firm conducting the independent and objective evaluation recommended that the methodology to calculate the weighted annual rate of return be adjusted to conform to the Global Investment Performance Standards (GIPS®). The Committee accepted this recommendation by approving Resolution FSM 2015-7 Weighted Annual Rate of Return and C Account Calculation Methodology Adjustment. The change to the methodology resulted in slightly increased weighted annual rates of return and, thus, slight additions to the C account transfers. The total adjustment for all fiscal years added \$4,478,409 to the C account from the A account. The A and C account adjustments are reflected in Table 7 and, for all fiscal years, Attachment 3, Table C. The weighted annual rates of return are adjusted in Figure 4.

## IV. Trust Fund Effectiveness

### A. Effectiveness to Achieve Purpose

Article 3 of the Trust Fund Agreement between the U.S. and FSM governments states that, “The purpose of the Fund is to contribute to the economic advancement and long-term budgetary self-reliance of the Federated States of Micronesia by providing an annual source of revenue, after Fiscal Year 2023, for assistance in the sectors described in Section 211 of the Compact, as amended, or other sectors as mutually agreed by the Original Parties, with priorities in education and health care.”

The Trust Fund Agreement states in Article 20 that the Committee shall publish an annual report that includes the “effectiveness of the Fund to accomplish its purpose” and may include “recommendations regarding improving the effectiveness of the Fund to accomplish that purpose.”



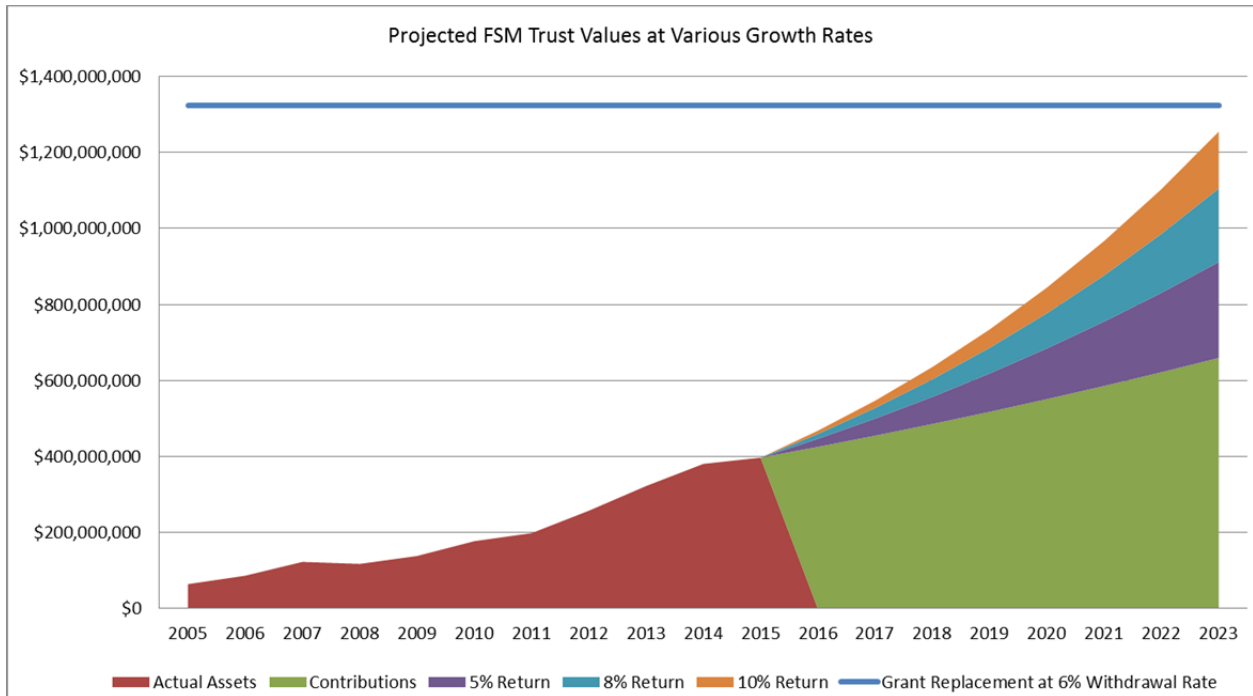
Source: The Weighted Annual Investment Return calculation was adjusted per Resolution FSM 2015-7 Weighted Annual Rate of Return and C Account Calculation Methodology Adjustment.

The weighted annual rate of return on investment for FY15, after discounting for contributions, fees, and expenses, was -2.59% for the year compared to three consecutive years of high returns: 9.12% for FY14, 14.44% for FY13, and 15.96% for FY12.

An analysis by the Investment Adviser (Figure 5) estimates that, assuming a 6% payout from the Fund, if the Fund manages an average 5% return annually from FY16 to FY23, the distribution from the estimated assets probably would provide for FY24 an amount equivalent to about 69.9% of the Amended Compact’s Section 211 estimated FY23 sector grant level with the partial inflation adjustment. There would also be a build-up of the C account but not to the maximum level permitted under the Trust Fund Agreement. As of FY15, the average annual rate of return is 4.6%, net of fees.

If the Fund were to achieve an average 8% return annually, the Fund would probably provide for FY24 an amount equivalent to 83.5% of estimated FY23 sector grant assistance with the partial inflation adjustment. There would also be a build-up of the C account but not to the maximum level permitted under the Trust Fund Agreement. The Fund has achieved 8% or more return in five fiscal years of its 12 years of existence: 2007, 2010, 2012, 2013, and 2014.

**Figure 5: Projected Growth Trends, FY04-FY23**



Source: Mercer Investment Management

If the Fund were to achieve an average 10% return annually, the Fund would probably provide FY24 revenue equivalent to about 94.7% of estimated partially inflation adjusted FY23 sector grant assistance. However, it is unlikely that post-2023 distributions would provide for future inflation adjustments beyond the FY23 amount. The C account would achieve the maximum level permitted under the Trust Fund Agreement prior to FY23. However, there is a low probability of achieving such growth annually.

In addition to potential earnings on investment, analysis shows that additional contributions beyond those currently scheduled would improve the Fund's potential to achieve a value to provide sustainable distributions such as the Amended Compact's Section 211 FY23 sector grant level with the partial inflation adjustment and at least partially inflation adjusted amounts beyond.

Any growth projections are estimates, subject to fluctuation based on actual market performance. This also extends to future fiscal planning. As intended in the Amended Compact, Trust Fund payments will be a post-2023 "source of revenue" to supplement other financial resources of the FSM government.



## B. Recommendations Moving Forward

During FY15 the Trust Fund Committee contracted, as described above, a firm to conduct an independent and objective external evaluation of the Fund to help guide the Trust Fund Committee as the Fund proceeds past the mid point of the 20-year build-up period that ends in FY23.

The external evaluation found the Trust Fund to be generally well governed with competent Committee, staff and key service providers, governance practices appropriate for the Fund's circumstances and no areas of non-compliance with the Trust Fund Agreement or Amended Compact.

A major finding of the external evaluation was that costs for investment and administrative services were within the ranges of similar trust, endowment, and foundation funds. The Committee has remained vigilant to contain such costs as an appropriate percentage of the Fund.

The firm provided a range of recommendations to the Committee. Chief among the main recommendations, which the Committee has implemented or is working to address, were to:

- Review and adjust the Investment Policy Statement's asset allocation strategy so that it conforms to Committee interests as the build-up period nears its end so capital is protected. If the Committee interest is to protect capital, a more conservative investment strategy may be required, based on Investment Adviser advice. The Committee is working with the Investment Adviser to adjust the asset allocation by applying a "glide path" to investment allocation adjustments to FY23.
- Adjust the Investment Policy Statement to include additional information to support the investment allocation determination. Mercer will be providing this additional information to the Committee.
- Adjust the methodology of the weighted annual rate of return calculation to conform to the Global Investment Performance Standards (GIPS®). As noted above, the Committee accepted the recommendation. The change to the methodology resulted in slightly increased weighted annual rates of return and, thus, slight additions to the transfers to the C account from the A account for years when such transfers were eligible to be made. The adjusted methodology will be applied annually.
- Review the objectives of the Trust Fund during the distribution period in terms of possible distribution scenarios and eventually more fully define a distribution policy for the post FY23 distribution period.
- Identify the Fund's key stakeholder's and develop a policy for two-way communications; this could include creating and maintaining a Trust Fund website available to the public.

Attachment 1: Manager Roster and Investment Manager Fee Schedule as of September 30, 2015

Account	Fee Schedule	Estimated Annual Fee (%)
<b>Trust Fund Managed Assets</b>	<b>0.63% in aggregate of assets</b>	<b>0.63%</b>
Private Equity- Mercer PIP III	0.50% of Committee Capital	0.50%
<b>Non-Discretionary Assets</b>		
<b>Real Estate</b>		
Prudential Real Estate Investors*	Effective Base Mgmt Fee+CF Distribution+Cash Mgmt Profit Distribution	0.95%
<b>Hedge Fund</b>		
Blackstone Alternative Asset Management*	1.25% of Assets	1.25%
<b>Private Equity*</b>		
HarbourVest Partners VIII Venture Fund	1.00% of Committed Capital	1.00%
HarbourVest Partners VIII Buyout Fund	1.00% of Committed Capital	1.00%
HarbourVest Partners VIII Mezzanine and Distressed Debt Fund	1.00% of Committed Capital	1.00%
HarbourVest International Private Equity V	1.00% of Committed Capital	1.00%
Portfolio Advisors Private Equity Fund I	0.70 of Committed Capital	0.70%
<b>Total Non Discretionary Overlay Fee</b>	<b>0.09% of Assets</b>	<b>0.09%</b>
<b>Total Investment Management Fee</b>		<b>0.78%</b>

Source: Trust Fund for the People of the Federated States of Micronesia Investment Performance, September 30, 2015, Mercer Investment Management, p. 89.

\*The fee schedule rates are based on the manager's standard management fees only and do not include performance-based fees, incentives fees, etc.

Note: The management fees payable to third party investment managers to underlying funds in which Mercer PIP III may invest will be borne by that fund and therefore, indirectly by the Discretionary Account.

## Attachment 2: Performance Standard Benchmarks

Asset Class	Benchmarks
<b>Overall</b>	Total Trust Benchmark <sup>11</sup> Ifx All Foundation Gross Median
<b>Total Managed Assets Benchmark</b>	Custom Bench Mark (as of 1/1/14): Russell 3000 (32.7%), MSCI ACWIxU.S. (33.8%), Fixed Income Benchmark (25.2%), T-Bills+3% (7.3%), and S&P 500+3% (1%)
<b>Domestic Equity</b>	Russell 3000 Index
<b>U.S. Large Cap Equity</b>	S&P 500 Index (total return) Mercer Institutional U.S. Equity Large Cap Core Median
<b>U.S. Small/Med Cap Equity</b>	Russell 2500 Growth Index Mercer Institutional U.S. Equity SMID Growth Median Russell 2500 Value Index Mercer Institutional U.S. Equity SMID Value Median
<b>Non-U.S. Equity</b>	Total Non-U.S. Equity Benchmark (MSCI ACWI ex U.S. Ne Div.) MSCI EAFE Mercer Institutional World ex U.S. EAFE Equity Median MSCI Emerging Markets Mercer Institutional Emerging Markets Equity Median
<b>Fixed Income</b>	Fixed Income Benchmark (13.2% Barclays U.S. Aggregate Bond Index and 86.8% Custom Opportunistic Fixed Income Benchmark consisting of: 50% BofA Merrill Lynch Global High Yield Constrained Index and 50% JP Morgan WGBI EM Global Diversified) Barclays Aggregate Bond Index (for Mercer Core Fixed Income Fund) Mercer Institutional U.S. Fixed Core Median Custom Opportunistic Fixed Income Benchmark (for Mercer Opportunistic Fixed Income) Mercer Institutional U.S. Fixed Core Median
<b>Hedge Fund (managed)</b>	T-Bills+3% HFRI Fund of Funds Composite Index Mercer Institutional Funds of Hedge Funds (Net) Median
<b>Private Equity (managed)</b>	S&P 500+3% Burgiss Global Private Equity Index
<b>Private Equity</b>	S&P 500+3%

<sup>11</sup> As of 1/1/14, the Total Trust Benchmark is comprised of 25.5% Russell 3000, 25.5% MSCI ACWIxU.S. Net Dividend, 19.0% fixed income benchmark, 10% NCREIF NFI ODCE, 9.5% S&P 500+3%, and 10.5% T-Bills+3%.



Asset Class	Benchmarks
	Burgiss Global Private Equity Index
<b>Private Real Estate</b>	NCREIF NFI ODE Mercer Institutional U.S. Real Estate Open End Median
<b>Hedge Funds</b>	T-Bills +3% Mercer Institutional Funds of Hedge Funds (Net) Median

Source: Trust Fund for the People of the Federated States of Micronesia Investment Performance, September 30, 2015, Mercer Investment Management.

### Attachment 3: Historical Tables

**Table A: Total Contributions, Income, Expenses and Net Positions Since Inception**  
(in millions)

	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15
<b>Net Assets (Beginning of Fiscal Year)</b>	<b>\$0.00</b>	<b>\$0.00</b>	<b>\$64.23</b>	<b>\$86.46</b>	<b>\$122.84</b>	<b>\$117.52</b>	<b>\$138.07</b>	<b>\$177.20</b>	<b>\$198.46</b>	<b>\$257.34</b>	<b>\$323.08</b>	<b>\$380.90</b>
<i>Contributions</i>												
U.S.	\$0.00	\$32.19	\$16.44	\$17.69	\$19.00	\$20.91	\$21.52	\$22.39	\$23.59	\$24.99	\$26.10	\$26.98
FSM	\$0.00	\$30.26	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00
Total	\$0.00	\$62.45	\$16.44	\$17.69	\$19.00	\$20.91	\$21.52	\$22.39	\$23.59	\$24.99	\$26.10	\$26.98
<i>Investment Earnings Less Fees and Expenses</i>												
Investment Earnings	\$0.00	\$1.79	\$5.94	\$19.41	-\$23.27	\$0.83	\$18.70	-\$0.34	\$36.19	\$41.90	\$32.97	-\$9.15
Fees and Expenses	\$0.00	\$0.01	\$0.14	\$0.73	\$1.05	\$1.18	\$1.09	\$0.79	\$0.89	\$1.15	\$1.26	\$1.41
Total	\$0.00	\$1.78	\$5.80	\$18.69	-\$24.32	-\$0.35	\$17.60	-\$1.13	\$35.29	\$40.74	\$31.71	-\$10.56
<b>Net Assets (End of Fiscal Year)</b>	<b>-</b>	<b>\$64.23</b>	<b>\$86.46</b>	<b>\$122.84</b>	<b>\$117.52</b>	<b>\$138.07</b>	<b>\$177.20</b>	<b>\$198.46</b>	<b>\$257.34</b>	<b>\$323.08</b>	<b>\$380.90</b>	<b>\$397.32</b>

Note: Amounts rounded.

Note: "Fees and Expenses" are not inclusive of all Money Manager fees given that in the Audited Annual Financial Statements some Money Manager fees are deducted directly from the respective asset's value. Table 5 provides all FY14 and FY15 expenses inclusive of Money Manager Fees deducted from the respective asset values.

Source: Audited Annual Financial Statements since FY05.

**Table B: Investment and Administrative Expenses Since Inception and Differences Between FY14 and FY15**

	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15	Diff FY14- FY15
<b>Investment Expenses</b>	<b>\$0</b>	<b>\$132,039</b>	<b>\$686,419</b>	<b>\$955,763</b>	<b>\$1,049,150</b>	<b>\$939,224</b>	<b>\$645,382</b>	<b>\$2,177,580</b>	<b>\$2,613,679</b>	<b>\$2,849,842</b>	<b>\$3,031,087</b>	<b>6.4%</b>
Custodian	-	1,997	12,908	42,117	16,280	23,508	59,312	67,313	85,449	98,437	99,777	1.4%
Investment Adviser	-	125,385	142,402	126,800	187,754	319,704	162,496	179,738	359,658	402,713	426,352	5.9%
Money Manager	-	4,657	531,109	786,846	845,116	596,012	423,574	490,898	555,169	604,209	592,444	-1.9%
Money Manager*								1,439,631	1,613,403	1,744,483	1,912,514	9.6%
<b>% of Net Position</b>	<b>0.00%</b>	<b>0.15%</b>	<b>0.56%</b>	<b>0.81%</b>	<b>0.76%</b>	<b>0.53%</b>	<b>0.33%</b>	<b>0.85%</b>	<b>0.81%</b>	<b>0.75%</b>	<b>0.76%</b>	<b>2.0%</b>
<b>Administrative Expenses</b>	<b>\$13,356</b>	<b>\$9,458</b>	<b>\$39,715</b>	<b>\$93,851</b>	<b>\$133,959</b>	<b>\$152,679</b>	<b>\$147,921</b>	<b>\$156,960</b>	<b>\$153,346</b>	<b>\$154,481</b>	<b>\$292,732</b>	<b>89.5%</b>
Executive Administrator	-	-	-	70,650	85,650	91,850	96,816	102,760	98,280	99,904	105,756	5.9%
Audit Fees	-	-	33,906	15,260	39,740	45,062	42,446	39,900	41,088	42,395	41,994	-0.9%
Accounting Fees	-	-	-	3,449	5,868	6,295	6,794	6,639	5,893	6,059	6,036	-0.4%
Legal Fees	13,356	9,458	5,809	4,457	245	4,344	1,258	780	2,889	376	2,997	697.0%
Miscellaneous Fees**	-	-	-	35	2,456	5,128	607	6,881	5,197	5,747	135,949	2265.4%
<b>% of Net Position</b>	<b>0.02%</b>	<b>0.01%</b>	<b>0.03%</b>	<b>0.08%</b>	<b>0.10%</b>	<b>0.09%</b>	<b>0.07%</b>	<b>0.06%</b>	<b>0.05%</b>	<b>0.04%</b>	<b>0.07%</b>	<b>81.7%</b>
<b>Total Expenses</b>	<b>\$13,356</b>	<b>\$141,497</b>	<b>\$726,134</b>	<b>\$1,049,614</b>	<b>\$1,183,109</b>	<b>\$1,091,903</b>	<b>\$793,303</b>	<b>\$2,334,540</b>	<b>\$2,767,025</b>	<b>\$3,004,323</b>	<b>\$3,323,847</b>	<b>10.6%</b>
<b>Total % of Net Position</b>	<b>0.02%</b>	<b>0.16%</b>	<b>0.59%</b>	<b>0.89%</b>	<b>0.86%</b>	<b>0.62%</b>	<b>0.40%</b>	<b>0.91%</b>	<b>0.86%</b>	<b>0.79%</b>	<b>0.84%</b>	<b>6.1%</b>

Note: Amounts rounded.

Source: Audited Annual Financial Statements since FY05

Note: Categories are organized and dollar figures reported per the Audited Annual Financial Statements except for the inclusion of Money Manager\* fees. These Money Manager\* fees are those fees directly deducted from individual fund asset values. The Money Manager\* fees were recorded as of FY12 by Trust Fund administration. Such Money Manager\* fees were incurred prior to FY12 but not fully recorded.

Miscellaneous Fees\*\* For FY15, a one-time charge of \$130,375 was incurred for independent and objective external evaluation. Without that additional expenditure, administrative expenses would remain at 0.04% of total net position and total expenses would amount to 0.80% of total net position.

**Table C: A and C Account Net Position Balances, FY06-FY15**

	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15
<b>Total Net Position</b>	<b>\$86,464,318</b>	<b>\$122,839,583</b>	<b>\$117,515,688</b>	<b>\$138,075,219</b>	<b>\$177,198,363</b>	<b>\$198,460,033</b>	<b>\$257,346,108</b>	<b>\$323,083,135</b>	<b>\$380,901,010</b>	<b>397,313,587</b>
<b>A Account</b>	<b>\$85,495,082</b>	<b>\$109,427,047</b>	<b>\$104,103,152</b>	<b>\$124,662,683</b>	<b>\$155,749,392</b>	<b>\$177,011,062</b>	<b>\$213,866,813</b>	<b>\$255,784,106</b>	<b>\$302,750,239</b>	<b>319,162,816</b>
U.S.	52,504,758	74,430,238	75,789,468	95,790,236	123,438,651	144,586,830	181,836,953	221,227,805	265,649,090	282,447,788
FSM	32,990,324	34,996,809	28,313,684	28,872,447	32,310,741	32,424,232	32,029,860	34,556,301	37,101,149	36,715,028
<b>C Account</b>	<b>\$969,236</b>	<b>\$13,412,536</b>	<b>\$13,412,536</b>	<b>\$13,412,536</b>	<b>\$21,448,971</b>	<b>\$21,448,971</b>	<b>\$43,479,295</b>	<b>\$67,299,029</b>	<b>\$78,150,771</b>	<b>78,150,771</b>
U.S.	595,218	9,122,957	9,764,632	10,306,131	16,999,309	17,520,028	36,967,599	58,206,965	68,573,625	69,160,665
FSM	374,018	4,289,579	3,647,904	3,106,405	4,449,662	3,928,943	6,511,696	9,092,064	9,577,146	8,990,107

Notes: Amounts rounded.

Note: The A and C account amounts since inception were recalculated per Resolution FSM 2015-7 Weighted Annual Rate of Return and C Account Calculation Methodology Adjustment to conform to the Global Investment Performance Standards (GIPS®). The proportions of each contributor were also adjusted so that the A and C account proportions were equal for all years per Resolution FSM 2011-7 Trust Fund A and C Account Income, Expenses and End-of-Year Calculation.

Source: Total asset value source: Audited Annual Financial Statements. A and C account amounts and contributor proportions prepared by Trust Fund bookkeeper and verified during audit process.

