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NATIONAL DEVELOPMENT BANK OF PALAU
(A COMPONENT UNIT OF THE REPUBLIC OF PALAU)

FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2017 AND 2016

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INDEPENDENT AUDITORS' REPORT

Board of Directors
National Development Bank of Palau:

Report on the Financial Statements

We have audited the accompanying financial statements of the National Development Bank of Palau (the Bank), a component unit of the Republic of Palau, which comprise the statements of net position as of September 30, 2017 and 2016, 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 audits 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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the National Development Bank of Palau as of September 30, 2017 and 2016, and the changes in its net position 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

Financial Statement Presentation

As discussed in note 2 to the financial statements, the Bank elected to present an unclassified statement of net position because current assets are not matched with current liabilities. 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 3 through 9 as well as the Schedule of Proportional Share of the Net Pension Liability on page 32 and the Schedule of Pension Contributions on page 33 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. This supplementary information is the responsibility of the Bank's management. 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 f
or 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 Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated May 4, 2018 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 LLC

May 4, 2018

MANAGEMENT'S DISCUSSION AND ANALYSIS
YEAR ENDED SEPTEMBER 30, 2017

This Management Discussion and Analysis (MD&A) of the National Development Bank of Palau's (the Bank) financial performance and condition for the fiscal year ended 2017 is intended to contribute to the reader's better understanding of the Bank's structure and activities. The report should be read in conjunction with the audited financial statements and associated reports.

Note that this report may at times anticipate future events that are based upon current assumptions subject to risk and uncertainties. Actual events may differ materially from these expectations.

Organization of the Bank

The Bank is a corporation established to initiate and promote economic development in the Republic of Palau (ROP) and was created in February 1982 by Public Law Number 1-27 as codified in Title 26 of the Palau National Code Annotated (PNCA), as amended. The Bank is wholly owned by ROP and operates independently under its own Board of Directors. Its main goals are to promote economic development by providing financing for new enterprise, industry, exports and housing.

The President of ROP appoints six of its seven Board members for three-year terms subject to Senate confirmation. The seventh member is the President of the Bank who shall serve as an ex-officio member of the Board. The Board of Directors elects their own officers to the posts of Chairman, Vice Chairman and Secretary/Treasurer, to serve the length of their terms.

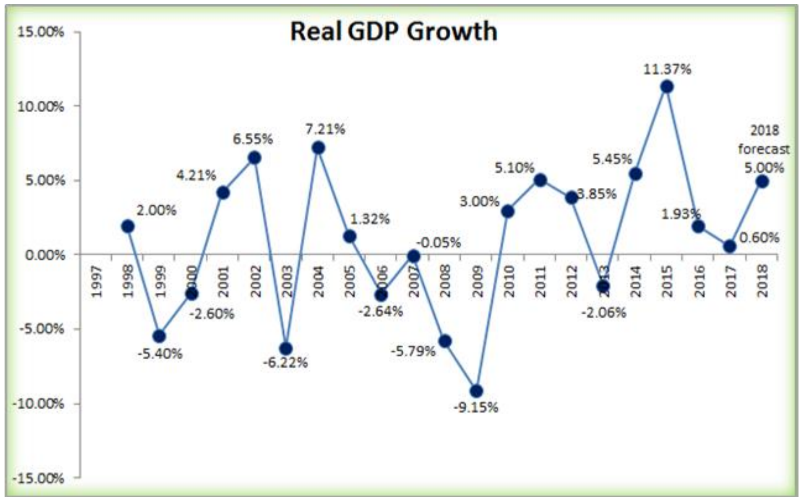
The Bank achieves its mission and goals by relending funds obtained from lenders, donors and the government. Its financial objective is not to maximize profit but to attain sufficient financial strength to achieve its objectives. Therefore, the Bank functions as a development financial institution and not a commercial or central bank.

The Bank's policies and strategies are implemented through the Bank's President and management. The Bank is organized by three functional areas: Finance, Lending and Risk & Compliance. The Board of Directors approves the hiring of candidates for the manager of each functional area. The Bank's President has the authority over all the other positions of the Bank. Staff levels and funding are determined against strategic, corporate and budget plans proposed by management and approved by Board. At fully staffed capacity, the Bank has nineteen full-time equivalent employees, including the President/Chief Executive Officer (CEO).

All Bank operations are conducted from its main office in Ngetkib Village, Airai State. There are no branches, other offices or subsidiaries operating in 2017. Plans for expansion of the Bank's building are set forth in the Bank's ten-year Strategic Plan.

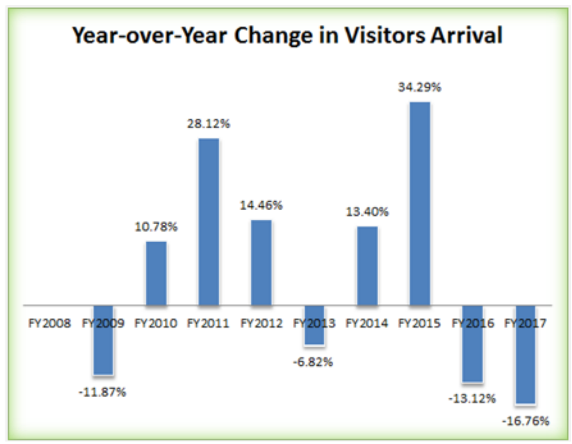
Economic Outlook

Although Palau's tourist industry is expected to slowdown, overall economic growth in 2018 is forecasted around 5%. This forecast is attributed to economic output increases in other industries. Construction (including infrastructures and housing) is also expected to boost the 2018 economy, despite the forecasted slowdown in the tourist sector.



In 2017, visitor arrivals to Palau significantly dropped by 16.76%, thereby negatively impacting the tourist industry. However, real Gross Domestic Product (GDP) grew modestly by 0.6% due to moderate increases in economic activities of other areas in the economy.

The tourist industry, the major economic driver of ROP, declined due to several factors. The most significant contribution to this decline was a decrease in the number of flights to Palau which drove down the monthly average tourist arrival from 12,219 in fiscal year 2016 to just 10,171 in fiscal year 2017. Another factor is the planned increase in tax through the Palau Pristine Paradise Environmental Fee (PPPEF) which may have discouraged visitors prior to the actual effective date of the PPPEF. Construction activity also saw a downturn in 2017, but is expected to rebound in 2018.



As we look forward to 2018, the expected increase in economic activities for agriculture/forestry, fishing and construction, presents an ongoing opportunity for the Bank to finance these important developments for ROP and make a real impact on peoples' lives.

	2016	2017	
Business Gross Receipt Tax			
Accommodation and Food Service	2,729,862	2,509,063	-8.09%
Administrative and Support Services	495,698	497,030	0.27%
Agriculture and Forestry	28,721	32,160	11.97%
Construction	972,452	843,572	-13.25%
Financial and Insurance	291,094	338,741	16.37%
Fisheries	73,784	81,276	10.15%
Manufacturing	222,655	203,202	-8.74%
Mining and Quarrying	106,876	122,580	14.69%
Other Industries	215,981	222,737	3.13%
Other Service Activities	119,143	155,469	30.49%
Professional, Scientific, and Technical	207,595	138,709	-33.18%
Real Estate	610,511	983,861	61.15%
Transportation and Storage	1,122,291	1,092,512	-2.65%
Wholesales, Retail, and Vehicle Repair	7,706,569	7,775,665	0.90%
Grand Total	**14,903,232**	**14,996,577**	**0.63%**

	2015	2016	2017
Agriculture and Forestry			
Business Gross Receipt Tax	26,686	28,721	32,160
Number Employed	473	550	555
Registered Business Licenses	204	148	167
Wages & Salaries	495,000	618,000	660,000
Construction			
Business Gross Receipt Tax	1,101,128	972,452	843,572
Number Employed	3,270	3,559	5,812
Registered Business Licenses	560	516	549
Wages & Salaries	6,556,000	7,379,000	8,745,000
Fisheries			
Business Gross Receipt Tax	41,589	73,784	81,276
Number Employed	307	345	389
Registered Business Licenses	140	150	155
Wages & Salaries	505,000	661,000	783,000

Financial Policies

The Bank's financial policies follow accounting principles generally accepted in the United States of America (GAAP) applicable to governmental entities and specifically proprietary funds. Management is required to make estimates, disclosures and assumptions in preparation of financial statements in conformity with GAAP and actual results may differ from amounts reported during the reporting period. The basis of accounting used is the flow of economic resources measurement focus, which means all assets and liabilities are included within the statements of net position. The accrual basis of accounting is utilized whereby revenues are recorded when earned and expenses recorded when liabilities are incurred.

Significant financial policies include a 10% reserve requirement for the Bank's commercial guaranteed loans. The reserve is held in a time certificate of deposit with a commercial bank. A reserve of $500,000 is also held at a commercial bank as required by the U.S. Department of Agriculture Rural Development (USDA RD) for program loans guaranteed by the Bank.

All current guarantees are granted under recourse loan purchase agreements. While the Bank offers 90% loan guarantees to local banks, the Bank may also guarantee up to 100% of select home loans from commercial banks to Palauan citizens as in the case of USDA RD.

A Memorandum of Understanding (MOU) was signed on April 1, 2014, between the Bank of Guam (BOG), the Bank and the Palau Housing Authority (PHA) pursuant to the Belau Real Estate Financing Program.

Other financial policies include ROP's full faith and credit guarantee backing for Bank loans up to $15 million in the aggregate, subject to specific purpose limitations. Maximum Bank external borrowing authorized by ROP is $100 million. The maximum single exposure to a single borrowing entity is 20% of the Bank's unimpaired paid-in capital, earned surpluses and reserves.

Operations

Financial assistance is provided by the Bank for projects involving housing, agriculture, marine resources, commerce and industry. Authorized financing schemes include guarantees, direct loans and direct investment. Further, the Bank is required to provide technical assistance services as part of its operations. The Bank's MOU, financial and logistical support from the Palau Small Business Development Center (SBDC) to assist client with such things as creating business plans; collaboration with the Palau SBDC and the Ministry Natural Resources, Environment and Tourism on the Farm Loan Program; and the MOU with PHA on providing subsidy for Energy Efficient Homes are efforts towards this responsibility. Information on other financial and technical service providers including government agencies is also provided for client or applicant consideration. Currently, the Bank's financial activities are limited to projects within ROP. All financial transactions are US dollar denominated.

Guaranteed Loans

The Bank offers guarantees backed by the Bank or ROP to commercial banks and other institutions. There are only guarantees outstanding from the Bank for the USDA RD loans. Popularity is low with these programs as they often take months to receive approval and are stricter in terms and loan covenants. Belau Real Estate Financing Program through BOG is a new addition to our guaranteed loans program. As of September 30, 2017, no completed loan packages from BOG were received by the Bank.

Energy Programs

Energy is one of the national policy directions for industry under Palau's leadership. The Bank continuously works to secure grants to expand its Energy Program.

Direct Loans

In the category of small business loans, the Bank offers customers four programs: Small Business, WEDAP, Microfinance and Pre-Development Loan. The Bank's general policy is for all loans to be fully secured, except for Microfinance loans, which are up to $15,000. Microfinance loans are administered like signature loans; however, the Bank may take collateral if it deems necessary for caution. The Bank's Microfinance and Pre-Development Loan programs are small loans for housing or business purposes at a 6% interest rate targeting those borrowers who are able to secure their loan with an assignment of income. No collateral is required and turnover is intended to be quick. These programs appear to be successful and are popular. Specifically, interests in Microfinance loans, which are also available for home projects such as extensions and renovations have been popular.

Short to medium-term financing is extended to new or existing businesses to fund short-term working capital and equipment acquisitions. Longer term financing is extended to individuals for housing and business facilities. Rates are fixed depending on the type of financing provided. Posted interest rates range from 3% to 10%. Rates are considered to include the cost of funds, the lending spread to cover the cost of operations, risk components, and a small return for growth purposes. Fees are usually 2% of financing extended. Originating and closing costs are also charged to borrowers. Specific programs offered under direct financing are agriculture, fishing, small business, housing and business loans.

Direct housing loans are provided in two categories, the first-time homeowner program which offers an 8% interest rate and all other housing loans at a 10% interest rate. Owner contribution to projects is required at 15% of project cost with a maximum amount of $10,000 under the Pre-Development Loan program and a loan term not to exceed five years. The purpose of Pre-Development Loan program is to help borrowers pay for plan design, appraisal, title search and all related soft costs associated with packaging loans and cash equity contribution. Eligible purposes for housing loans include new construction, renovation and extension.

Overview of Financial Performance

A condensed year-to-year comparison of operating activity reflecting the foregoing statements follows:

Statements of Revenues, Expenses and Changes in Net Position

	2017	2016	$ Change	% Change	2015 As Restated
Revenues:					
Interest income on loans	$ 1,611,157	$ 1,491,715	$ 119,442	8%	$ 1,661,610
Loan fees and late charges	97,570	95,428	2,142	2%	90,417
Other	28,449	53,510	(25,061)	-47%	41,128
Total operating revenues	1,737,176	1,640,653	96,523	6%	1,793,155
(Provision for) recovery of loan losses and doubtful accounts	(190,930)	492,375	(683,305)	-139%	411,892
Net operating revenues	1,546,246	2,133,028	(586,782)	-28%	2,205,047
Operating expenses:					
Salaries, wages and fringe benefits	598,852	544,977	53,875	10%	436,483
Training and travel	91,497	116,306	(24,809)	-21%	59,244
Depreciation	40,667	36,953	3,714	10%	42,122
Other expenses	207,603	244,025	(36,422)	-15%	216,312
Total operating expenses	938,619	942,261	(3,642)	-0%	754,161
Operating income	607,627	1,190,767	(583,140)	-49%	1,450,886

Overview of Financial Performance, Continued

Statements of Revenues, Expenses and Changes in Net Position, Continued

	2017	2016	$ Change	% Change	2015 As Restated
Nonoperating revenues (expenses), net	(639,762)	(179,988)	(459,774)	255%	(19,765)
Change in net position	(32,135)	1,010,779	(1,042,914)	-103%	1,431,121
Net position at beginning of year	18,489,494	17,478,715	1,010,779	6%	16,047,594
Net position at end of year	$ 18,457,359	$ 18,489,494	$ (32,135)	-0%	$ 17,478,715

A condensed year-to-year comparison of the Statements of Cash Flows follows:

Statements of Cash Flows

	2017	2016	$ Change	% Change	2015 As Restated
Cash flows from operating activities	$ 550,265	$ 660,318	$ (110,053)	-17%	$ 1,847,254
Cash flows from capital and related financing activities	(1,609,957)	3,517,938	(5,127,895)	-146%	1,599,229
Cash flows from investing activities	(1,204,063)	639,932	(1,843,995)	-288%	1,271,222
Cash flows from noncapital financing activities	32,682	(28,919)	61,601	-213%	(2,210,021)
Net (decrease) increase in cash and cash equivalents	(2,231,073)	4,789,269	(7,020,342)	-147%	2,507,684
Cash and cash equivalents at beginning of year	14,049,504	9,260,235	4,789,269	52%	6,752,551
Cash and cash equivalents at end of year	$ 11,818,431	$ 14,049,504	$ (2,231,073)	-16%	$ 9,260,235

Revenue

Operating revenues include all direct revenues such as interest income and fees on loans and other miscellaneous fees, such as late and performance bonds fees. Operating revenues in 2017 increased by 6% over 2016 largely due to the increase in the Bank's loan portfolio and decreased by 9% in 2016 over 2015.

Loan Interest Rates

The Bank's interest rates remained fixed according to the type of loan funded. Rates ranged from 3% for agriculture loans, 6% for microfinance and pre-development loans, 8% for fishing, WEDAP and first-time homeowner loans and 10% for commercial and housing loans. Other accounts in collection continue to be assessed the statutory rate of 9% as required by a court-ordered judgment. At the end of fiscal year 2017, the average yield on the Bank's portfolio decreased from 8.25% in 2016 to 8.24% in 2017 due to increases in agriculture/aquaculture micro-finance, pre-development and non-performing loans.

Expenses

Total operating expenses for 2017 was $3,642 less than 2016. Savings were realized in professional fees, travel and training, communications and supplies, printing and reproduction. The Bank's commitment for training new and existing staff with internet-based, bank-designed and on and off-island training continues each year.

Overview of Financial Condition

The following condensed Statements of Net Position highlights the aforementioned changes in condition with comparative information from prior years.

Overview of Financial Condition, Continued

Statements of Net Position

	2017	2016	$ Change	% Change	2015 As Restated
Economic development loans receivable, net	$ 19,136,177	$ 18,112,014	$ 1,024,163	6%	$ 18,249,508
Capital assets	675,502	623,208	52,294	8%	631,916
Other assets	13,037,438	15,525,773	(2,488,335)	-16%	10,517,114
Total assets	32,849,117	34,260,995	(1,411,878)	-4%	29,398,538
Deferred outflows of resources from pension	337,651	198,993	138,658	70%	153,041
Total assets and deferred outflows of resources	$ 33,186,768	$ 34,459,988	$ (1,273,220)	-4%	$ 29,551,579
Loans payable	$ 12,340,586	$ 13,433,219	$ (1,092,633)	-8%	$ 9,478,214
Net pension liability	1,837,001	1,630,006	206,995	13%	1,566,224
Other liabilities	335,778	670,695	(334,917)	-50%	818,695
Total liabilities	14,513,365	15,733,920	(1,220,555)	-8%	11,863,133
Deferred inflows of resources from pension	216,044	236,574	(20,530)	-9%	209,731
Total liabilities and deferred inflows of resources	14,729,409	15,970,494	(1,241,085)	-8%	12,072,864
Net position:					
Net investment in capital assets	675,502	623,208	52,294	8%	631,916
Restricted	17,781,857	17,866,286	(84,429)	-0%	16,846,799
Total net position	18,457,359	18,489,494	(32,135)	-0%	17,478,715
Total liabilities, deferred inflows of resources and net position	$ 33,186,768	$ 34,459,988	$ (1,273,220)	-4%	$ 29,551,579

Loan Portfolio

The Bank's loan portfolio includes new, amended and renewed loans and bonds. The Bank approved two hundred eleven loans in 2017 for $9.3 million and one hundred and ninety-two loans in 2016 for $9.7 million.

The Bank's goal during the year remained growth in income and assets while maintaining credit quality. Emphasis was also made towards increasing the agriculture and fishing sectors of the portfolio which were challenging given the less than favorable industry and economic conditions. Simultaneously, emphasis was placed on adjusting the portfolio distribution to reduce exposure and diversify risk. The outstanding loans by sector for 2017 and 2016 are presented in the following table:

Sector	2017			2016			CHANGE		
	Number	Amount	Percent	Number	Amount	Percent	Number	Amount	Percent
Agriculture	64	$ 847,471	4.23%	26	$ 281,106	1.47%	38	$ 566,365	201.48%
Fishing	41	374,316	1.87%	38	278,350	1.46%	3	95,966	34.48%
Commercial	160	7,618,347	38.04%	105	7,869,329	41.18%	55	(250,982)	-3.19%
Housing	517	11,187,398	55.86%	549	10,679,208	55.89%	-32	508,190	4.76%
Totals	782	$ 20,027,532	100.00%	718	$ 19,107,993	100.00%	64	$ 919,539	4.81%

The total number of loans at the end of 2017 was seven hundred eighty-two accounts for $20,027,532 and seven hundred eighteen for $19,107,993 at the end of 2016, which is an increase of $919,539 or 4.81% of total outstanding notes in 2017 compared to 2016.

Total Assets

The Bank's total assets for 2017 was $32,849,117 compared to $34,260,995 for 2016 and $29,398,538 for 2015. Total assets decreased by $1,411,878 or 4% in 2017 largely due to solar equipment installations in various homes and business. Total assets increased by $4,862,457 or 17% in 2016 over 2015.

Overview of Financial Condition, Continued

Capital Assets and Long-Term Debt

At September 30, 2017, 2016 and 2015, the Bank had net investment in capital assets of $675,502, $623,208 and $631,916, respectively, net of accumulated depreciation where applicable, including leasehold rights, leasehold improvements, furniture, fixtures and equipment and vehicles. The increase in 2017 is due to a new server and replacement of old equipment. See note 5 to the financial statements for more detailed information on the Bank's capital assets. No additions to long-term debt occurred in fiscal year 2017. For additional information on long-term debt, please see notes 3 and 7 to the financial statements.

Affiliations

The Bank's membership and partnership affiliations locally and abroad include the Palau Chamber of Commerce, the Risk Management Association, various foreign government agencies, the Association of Development Finance Banks and the Association of Development Finance Institutions in Asia and the Pacific. Benefits received from these associations include information exchanges, professional networking and training opportunities.

Risk Management

Primary risks the Bank faces include Strategic/Operational, Credit, Technology, Economic, Reputation/Political and Climatic/Environmental risks (in no particular order). The Board of Directors manages these risks with the assistance of management.

Monitoring is conducted primarily through management and external audit reporting. Mandatory reporting to the National Government is also provided during the National budget process and through specific reporting requirements under the Bank's enabling legislation.

Loss Provisioning

The Bank's provisions for loan losses with a general provision of 3% and specific provisions of 3%, 5%, 20%, 50% and 100% depending on the extent loans are past due and the value of security held as collateral. The Bank manages its loans by assigning credit and security risk ratings to each account.

Loans and associated security are rated on a scale of "A thru F" similar to the World Bank system. All loans are individually managed by this system. Loan accounts are required to be reviewed regularly.

The loan provision as of September 30, 2017 totaled $891,355 versus $995,979 as of September 30, 2016. The decrease is due to the Bank's continued efforts to seek remedies or foreclose on non-performing loans.

The Management's Discussion and Analysis for the year ended September 30, 2016 is set forth in the Bank's report on the audit of financial statements, which is dated May 15, 2017. That Discussion and Analysis explains the major factors impacting the 2016 financial statements and can be viewed at the Office of the Public Auditor's website at www.palauopa.org.

Contacting the Bank's Financial Management

This financial report is designed to provide a general overview of the Bank's finances and to demonstrate the Bank's accountability for the money it receives. If you have questions about this report or need additional information, please contact the Comptroller/Chief Financial Officer at the National Development Bank of Palau at P.O. Box 816, Koror, Republic of Palau 96940, or e-mail sbasilio@ndbp.com or call (680) 587-6327.

NATIONAL DEVELOPMENT BANK OF PALAU

Statements of Net Position
September 30, 2017 and 2016

ASSETS AND DEFERRED OUTFLOWS OF RESOURCES	2017	2016
Assets:		
Cash and cash equivalents	$ 11,818,431	$ 14,049,504
Time certificates of deposit	456,143	455,004
Economic development loans receivable, net	19,136,177	18,112,014
Accrued interest receivable	116,096	98,580
Other receivables	74,433	80,011
Inventory	154,826	415,326
Prepaid expenses	20,061	29,922
Restricted cash and cash equivalents	50,249	50,227
Capital assets, net	675,502	623,208
Foreclosed real estate	347,199	347,199
Total assets	32,849,117	34,260,995
Deferred outflows of resources from pension	337,651	198,993
Total assets and deferred outflows of resources	$ 33,186,768	$ 34,459,988
LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION		
Liabilities:		
Loans payable	$ 12,340,586	$ 13,433,219
Accounts payable and accrued expenses	139,873	474,563
Payable to grantor agencies	123,844	128,175
Interest payable	72,061	67,957
Net pension liability	1,837,001	1,630,006
Total liabilities	14,513,365	15,733,920
Deferred inflows of resources from pension	216,044	236,574
Total liabilities and deferred inflows of resources	14,729,409	15,970,494
Commitments and contingencies		
Net position:		
Net investment in capital assets	675,502	623,208
Restricted	17,781,857	17,866,286
Total net position	18,457,359	18,489,494
Total liabilities, deferred inflows of resources and net position	$ 33,186,768	$ 34,459,988

See accompanying notes to financial statements.

NATIONAL DEVELOPMENT BANK OF PALAU

Statements of Revenues, Expenses and Changes in Net Position
Years Ended September 30, 2017 and 2016

	2017	2016
Operating revenues:		
Interest income on loans	$ 1,611,157	$ 1,491,715
Loan fees and late charges	97,570	95,428
Other	28,449	53,510
Total operating revenues	1,737,176	1,640,653
(Provision for) recovery of loan losses and doubtful accounts	(190,930)	492,375
Net operating revenues	1,546,246	2,133,028
Operating expenses:		
General and administrative expenses:		
Salaries, wages and fringe benefits	598,852	544,977
Training	69,270	89,576
Depreciation	40,667	36,953
Professional fees	32,719	69,222
Dues and subscriptions	31,623	32,228
Communications	28,622	30,372
Travel and transportation	22,227	26,730
Repairs and maintenance	21,591	20,501
Supplies, printing, and reproduction	21,119	27,271
Rental	13,200	9,140
Marketing and advertising	12,338	6,219
Utilities	12,004	12,789
Honorariums and meeting expense	10,107	18,215
Insurance	9,322	8,123
Miscellaneous	14,958	9,945
Total general and administrative expenses	938,619	942,261
Operating income	607,627	1,190,767
Nonoperating revenues (expenses), net:		
Other income	38,949	19,917
Grant revenues	23,700	1,107,866
Interest income on interest bearing accounts	12,191	10,765
Interest expense and loan fees	(428,467)	(394,970)
Energy Loan Program	(262,435)	(815,700)
Energy Efficiency Home Loan Project	(23,700)	(85,600)
Energy Retrofit Program	-	(22,266)
Total nonoperating revenues (expenses), net	(639,762)	(179,988)
Change in net position	(32,135)	1,010,779
Net position at beginning of year	18,489,494	17,478,715
Net position at end of year	$ 18,457,359	$ 18,489,494

See accompanying notes to financial statements.

NATIONAL DEVELOPMENT BANK OF PALAU

Statements of Cash Flows
Years Ended September 30, 2017 and 2016

	2017	2016
Cash flows from operating activities:		
Cash received from customers	$ 1,725,238	$ 1,613,802
Cash payments to employees for services	(613,917)	(511,640)
Cash payments to suppliers for goods and services	(561,056)	(441,844)
Net cash provided by operating activities	550,265	660,318
Cash flows from capital and related financing activities:		
Proceeds from issuance of long-term debt	-	5,000,000
Acquisition of capital assets	(92,961)	(28,245)
Repayments of long-term debt	(1,092,633)	(1,044,995)
Interest paid on long-term debt	(424,363)	(408,822)
Net cash (used for) provided by capital and related financing activities	(1,609,957)	3,517,938
Cash flows from investing activities:		
Net change in time certificates of deposit	(1,139)	(684)
Interest received on interest bearing deposits	12,191	10,765
Net change in restricted cash and cash equivalents	(22)	(18)
Loan (originations) collections, net	(1,215,093)	629,869
Net cash (used for) provided by investing activities	(1,204,063)	639,932
Cash flows from noncapital financing activities:		
Other income received	38,949	19,917
Subsidy paid for energy program	(55,331)	(143,711)
Cash received from grantor	-	39,995
Cash received from sale of solar system	49,064	54,880
Net cash provided by (used for) noncapital financing activities	32,682	(28,919)
Net (decrease) increase in cash and cash equivalents	(2,231,073)	4,789,269
Cash and cash equivalents at beginning of year	14,049,504	9,260,235
Cash and cash equivalents at end of year	$ 11,818,431	$ 14,049,504
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	$ 607,627	$ 1,190,767
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	40,667	36,953
Provision for (recovery of) loan losses and doubtful accounts	190,930	(492,375)
Noncash pension cost	47,807	44,673
(Increase) decrease in assets:		
Accrued interest receivable	(17,516)	(29,071)
Other receivables	5,578	2,220
Prepaid expenses	9,862	786
Decrease in liabilities:		
Accounts payable and other liabilities	(334,690)	(93,635)
Net cash provided by operating activities	$ 550,265	$ 660,318
Supplemental schedule of noncash investing activities:		
Increase in inventory	$ -	$ 1,000,000
Increase in Energy Loan Program grant revenue	-	(1,000,000)
	$ -	$ -
Subsidy for Energy Loan Program:		
Increase in Energy Loan Program expense	$ 260,499	$ 738,422
Decrease in inventory	(260,499)	(738,422)
	$ -	$ -

See accompanying notes to financial statements.

(1) Organization

The National Development Bank of Palau (the Bank), a component unit of the Republic of Palau (ROP), was formed on February 24, 1982, under the provisions of Republic of Palau Public Law (RPPL) No. 1-27, as amended by RPPL 3-4, 4-48, 5-37 and 6-18. The law created a wholly-owned government corporation managed by a Board of Directors appointed by the President of ROP with the advice and consent of the Olbiil Era Kelulau (OEK - Palau National Congress). The purpose of the Bank is to be the central financial institution responsible for initiating and promoting economic development within ROP, and the Bank considers all of its net position, except net investment in capital assets, to be restricted for such purposes.

(2) Summary of Significant Accounting Policies

The accounting policies of the Bank conform to accounting principles generally accepted in the United States of America, as applicable to governmental entities, specifically proprietary funds. The Bank utilizes the flow of economic resources measurement focus. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

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 disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Basis of Accounting

Proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operation of this fund are included within the statements of net position. Proprietary fund operating statements present increases (e.g. revenues) and decreases (e.g. expenses) in net position. The accrual basis of accounting is utilized by proprietary funds. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

GASB Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments,* requires assets and liabilities of proprietary funds be presented in a classified format to distinguish between current and long-term assets and liabilities. The Bank is a government-owned bank. Banks do not present a classified statement of net position because current assets are not matched with current liabilities. The statements of net position of the Bank present assets and liabilities in order of their relative liquidity, rather than in a classified format.

Concentrations of Credit Risk

Financial instruments which potentially subject the Bank to concentrations of credit risk consist principally of cash demand deposits, investments, receivables and loans receivable from related party.

(2) Summary of Significant Accounting Policies, Continued

Concentrations of Credit Risk, Continued

At September 30, 2017 and 2016, the Bank has cash deposits in bank accounts that exceed federal depository insurance limits. The Bank has not experienced any losses on such accounts.

As of September 30, 2017 and 2016, concentrations of credit risk result from receivables from significant customers and receivable from a related party which represent 17% and 19% of total receivables, respectively. Management assesses the risk of loss and provides an allowance for doubtful accounts to compensate for known credit risk.

Cash and Cash Equivalents and Time Certificates of Deposit

For purposes of the statements of net position and of cash flows, the Bank considers all highly liquid investments, with maturities of three months or less when purchased, to be cash and cash equivalents. Time certificates of deposit with initial maturities of greater than three months are separately classified. The Bank does not require collateralization of its bank accounts. Restricted and unrestricted cash and cash equivalents and time certificates of deposit maintained in Federal Deposit Insurance Corporation (FDIC) insured banks amounted to $12,416,458 and $14,578,256 at September 30, 2017 and 2016, respectively. Of this amount, bank deposits of $750,000 were FDIC insured at September 30, 2017 and 2016. Accordingly, the deposits are exposed to custodial credit risk. The Bank does not require collateralization of its deposits; therefore, deposit levels in excess of FDIC coverage are uncollateralized.

RPPL 4-48, Section 126, as amended by RPPL 5-37, stipulates that the Bank shall maintain a reserve account to be applied to all defaults on commercial loans guaranteed by the Bank. The reserve account shall equal ten percent (10%) of the total amount of all loan guarantees on commercial bank loans, whether or not protected by the full faith and credit of ROP. The Bank has restricted $50,249 and $50,227 of cash and cash equivalents as of September 30, 2017 and 2016, respectively, to comprise this reserve. The Bank has internally restricted (not reflected as restricted in the Statements of Net Position) cash and cash equivalents held solely for the guarantee of U.S. Department of Agriculture Rural Development (USDA RD) loans in the amount of $541,271 and $540,980 as of September 30, 2017 and 2016, respectively. Additionally, $82,673 and $64,974 of cash received from grantor agencies was internally restricted at September 30, 2017 and 2016, respectively.

Loans and Allowance for Loan Losses

The Bank grants loans to eligible borrowers, including affiliates, officers and employees, all of which are located in ROP. Loans are stated at the amount of unpaid principal and interest, reduced by an allowance for loan losses.

The allowance for loan losses is established through a provision for loan losses charged to expense. Loans are charged against the allowance for loan losses when management believes that the collection of the principal is unlikely. The allowance is an amount that management believes will be adequate to absorb possible losses on existing loans that may be uncollectible, based on evaluations of the collectability of loans and prior loan loss experience. The evaluations take into consideration such factors as changes in the nature and volume of the loan portfolio, overall portfolio quality, review of specific problem loans and current economic conditions that may affect the borrowers' ability to pay.

(2) Summary of Significant Accounting Policies, Continued

Loans and Allowance for Loan Losses, Continued

All of the Bank's loans are subject to review for impairment as a part of management's internal asset review process. A loan is considered impaired when, based on current information and events, the borrower is deemed unable to repay the outstanding amount of the obligation under the loan. When a loan is determined to be impaired, a valuation allowance is established based upon the difference between the outstanding amount due under the loan and the amount considered recoverable given the existing financial condition of the borrower and the underlying collateral. Subsequent collections of cash may be applied as a reduction to the principal balance or recorded as income, depending upon management's assessment of the ultimate collectability of the loan.

Inventory

Inventory of on-grid and off-grid solar photovoltaic systems and commemorative coins are stated at the lower of cost (first-in, first-out) or market.

In 2011, the Bank implemented the Energy Loan Program to provide loans to business and housing customers to acquire renewable energy technologies. The Bank received on-grid and off-grid solar photovoltaic systems amounting to $402,819 from the United Nations Development Programme through the ROP Energy Office under the Sustainable Economic Development through Renewable Energy Applications (SEDREA) Program. On March 29, 2016, the Bank received one hundred (100) 1.7 kilowatt (kW) solar systems amounting to $1,000,000 from ROP, through Palau Public Utilities Corporation, under the Abu Dhabi Fund for Development (ADFD) allocated grant. On August 30, 2016, the Bank transferred remaining off-grid solar photovoltaic systems of $113,302 to the ROP Energy Office. Inventory of on-grid solar photovoltaic systems and 1.7 kW solar systems and commemorative coins amounted to $154,826 and $415,326 as of September 30, 2017 and 2016, respectively.

Capital Assets

Capital assets are stated at cost, net of accumulated depreciation. Depreciation is calculated using the straight-line method over the estimated useful lives of the respective assets. Current policy is to capitalize items in excess of $1,000.

Foreclosed Real Estate

Real estate properties acquired through, or in lieu of, loan foreclosures are held for sale and are initially recorded at the lower of the carrying amount of the loan or the fair value of the property at the date of foreclosure less estimated selling costs. Write-downs of the asset at, or prior to, the date of foreclosure are charged to the allowance for losses on loans. Subsequent write downs, income and expense incurred in holding such assets, and gains and losses realized from the sales of such assets, are included in current operations.

(2) Summary of Significant Accounting Policies, Continued

Deferred Outflows of Resources

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period and so will not be recognized as an outflow of resources (deduction of net position) until then. The Bank has determined the changes in assumptions, changes in proportion and difference between the Bank's contributions, difference between projected and actual earnings on pension plan investments, and proportionate share of contributions and pension contributions made subsequent to the measurement date qualify for reporting in this category.

Deferred Inflows of Resources

In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period and so will not be recognized as an inflow of resources (additions to net position) until then. The Bank has determined the changes in assumption, differences between projected and actual earnings on pension plan investments and changes in proportion and difference between the Bank's contributions and proportionate share of contributions qualify for reporting in this category.

Pensions

Pensions are required to be recognized and disclosed using the accrual basis of accounting. The Bank recognizes a net pension liability for the defined benefit pension plan, which represents the Bank's proportional share of excess total pension liability over the pension plan assets - actuarially calculated - of a single employer defined benefit plan, measured one year prior to fiscal year-end and rolled forward. Changes in the net pension liability during the period are recorded as pension expense, or as deferred inflows of resources or deferred outflows of resources depending on the nature of the change, in the period incurred. Those changes in net pension liability that are recorded as deferred inflows of resources or deferred outflows of resources that arise from changes in actuarial assumptions or other inputs and differences between expected or actual experience are amortized over the weighted average remaining service life of all participants in the qualified pension plan and recorded as a component of pension expense. Differences between projected and actual investment earnings are reported as deferred inflows of resources or deferred outflows of resources and amortized as a component of pension expense on a closed basis over a five-year period beginning with the period in which the difference occurred.

Revenue Recognition

Operating revenues include all direct revenues such as interest and fees on loans and interest on investments.

(2) Summary of Significant Accounting Policies, Continued

Revenue Recognition, Continued

Interest on loans is calculated by using the simple interest method on daily balances of the principal amount outstanding. Interest on loans is accrued and credited to income based on the principal amount outstanding. The accrual of interest on loans is discontinued when principal or interest payments are delinquent ninety days or more, or when, in the opinion of the Bank, there is an indication that the borrower may be unable to meet payments as they become due. Interest income thereafter is recognized only to the extent of cash payments received. Nonaccrual loans approximated $582,907 and $695,664 at September 30, 2017 and 2016, respectively.

Compensated Absences

Vested or accumulated vacation leave is recorded as benefits accrue to employees. No liability is recorded for nonvesting accumulating rights to receive sick pay benefits. Accumulated sick pay benefits as of September 30, 2017 and 2016 were $58,304 and $52,190, respectively.

Net Position

The Bank's net position is classified as follows:

- Net investment in capital assets; capital assets, net of accumulated depreciation.
- Restricted:

  Nonexpendable - Net position subject to externally imposed stipulations that the Bank maintains them permanently. At September 30, 2017 and 2016, the Bank does not have nonexpendable net position.

  Expendable - Net position whose use by the Bank is subject to externally imposed stipulations that can be fulfilled by actions of the Bank pursuant to those stipulations or that expire by the passage of time. As described in note 1, the Bank considers all assets, except investments in capital assets, to be restricted for economic development.

- Unrestricted; net position that is not subject to externally imposed stipulations. As the Bank considers all assets, except investments in capital assets, to be restricted for economic development, the Bank does not have unrestricted net position of September 30, 2017 and 2016.

New Accounting Standards

During the year ended September 30, 2017, the Bank implemented the following pronouncements:

- GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not Within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*, which aligns the reporting requirements for pensions and pension plans not covered in GASB Statements 67 and 68 with the reporting requirements in Statement 68.

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

- GASB 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).

- GASB Statement No. 77, *Tax Abatement Disclosures*, which requires governments that enter into tax abatement agreements to disclose certain information about the agreements.

- 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*.

- GASB 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.

- GASB 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 implementation of these statements did not have a material effect on the accompanying 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 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.

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In November 2016, GASB issued Statement No. 83, *Certain Asset Retirement Obligations*, which addresses accounting and financial reporting for certain asset retirement obligations (AROs) associated with the retirement of a tangible capital asset. The provisions in Statement No. 83 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.

In January 2017, GASB issued Statement No. 84, *Fiduciary Activities*, which establishes criteria for identifying fiduciary activities of all state and local governments. The provisions in Statement No. 84 are effective for fiscal years beginning after December 15, 2018. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In March 2017, GASB issued Statement No. 85, *Omnibus 2017*, which address practice issues that have been identified during implementation and application of certain GASB Statements including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits). The provisions in Statement No. 85 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 May 2017, GASB issued Statement No. 86, *Certain Debt Extinguishment Issues*, which improves consistency in accounting and financial reporting for in-substance defeasance of debt. The provisions in Statement No. 86 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 June 2017, GASB issued Statement No. 87, *Leases*, which establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. The provisions in Statement No. 87 are effective for fiscal years beginning after December 15, 2019. Management has yet to determine whether the implementation of this statement will have a material effect on the financial statements.

Off-Balance Sheet Financial Instruments

In the ordinary course of business, the Bank has entered 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.

(3) Employees' Retirement Plan

Defined Benefit Plan

A. General Information About the Pension Plan:

Plan Description: The Bank contributes to the Republic of Palau Civil Service Pension Trust Fund (the Plan), a defined benefit, cost sharing multi-employer plan, which is a component unit of the Republic of Palau (ROP) National Government, providing retirement, security and other benefits to employees, their spouses and dependents, of the ROP, ROP State Governments and ROP agencies, funds and public corporations. The Plan was established pursuant to RPPL No. 2-26 passed into law on April 3, 1987, and began operations on October 1, 1987. Portions of RPPL No. 2-26 were revised by RPPL 3-21, RPPL 4-40, RPPL 4-49, RPPL 5-30, RPPL 6-37, RPPL 7-56, RPPL 8-10 and RPPL 9-2.

A single actuarial valuation report is performed annually covering all plan members and the same contribution rate applies to each employer. The Plan issues a publicly available financial report that includes financial statements and required supplementary information for the defined benefit plan. That report may be obtained by writing to the Plan's Administrator at the Republic of Palau Civil Service Pension Trust Fund, P.O. Box 1767, Koror, Republic of Palau 96940, or e-mail cspp@palaunet.com or call (680) 488-2523.

Plan Membership. As of September 30, 2015, the date of the most recent valuation, plan membership consisted of the following:

Inactive members currently receiving benefits	1,507
Inactive members entitled to but not yet receiving benefits	1,151
Active members	3,120
Total members	5,778

Pension Benefits. Retirement benefits are paid to members who are required, with certain exceptions, to retire no later than their sixtieth birthday or after thirty years of service. A member may retire after his or her fifty-fifth birthday at a reduced pension amount if the member has completed at least twenty years of government employment. A married member of a former member receiving a distribution of benefits under the Pension Fund receives reduced benefit amounts to provide survivors' benefits to his or her spouse. An unmarried member or former member may elect to receive a reduced benefit amount during his or her lifetime with an annuity payable to his or her designated beneficiary. Disability benefits are paid to qualified members for the duration of the disability. Effective May 17, 1996, through RPPL 4-49, members, who have twenty-five years or more of total service, are eligible for retirement regardless of their age and, upon such retirement, are eligible to receive pension benefits at a level established by the Board.

Effective July 1, 1999, pursuant to RPPL 4-49 and RPPL 5-30, retirement is mandatory for all members who have thirty years or more of total service and all employees who are sixty years of age or older with certain exceptions. Beginning October 1, 2003, pursuant to RPPL 6-37, mandatory retirement may be delayed for up to five years, by specific exemption by the Board. In December 2008, RPPL 7-56 eliminated early retirement and thirty-year mandatory service provisions. These provisions were restored through RPPL 8-10 in October, 2009. On April 30, 2013, RPPL 9-2 eliminated the mandatory service retirement after thirty years of service. After December 31, 2013, no employee shall be entitled to pension benefits until reaching the age of sixty.

(3) Employees' Retirement Plan, Continued

Defined Benefit Plan, Continued

A. General Information About the Pension Plan, Continued:

In accordance with the directives of RPPL 5-7, the Board adopted a resolution which provides that "no person who retires after October 1, 1997, may receive benefits under the Plan unless he or she has contributed to the Plan for at least five years or has made an actuarially equivalent lump sum contribution". In accordance with RPPL 9-2, members who retire after April 30, 2013 must not receive benefits greater than thirty thousand dollars per year. Further, the amount of benefits that a member receives should not be recalculated if the member is re-employed after the member begins receiving benefits under the Plan. Additionally, a member should not receive benefits during the time the member is re-employed subsequent to retirement.

Currently, normal benefits are paid monthly and are two percent of each member's average monthly salary for each year of credited total service up to a maximum of thirty years total service. The average annual salary is the average of the highest three consecutive fiscal years of compensation received by a member during his or her most recent ten full fiscal years of service. For members who have not completed three consecutive fiscal years of employment during his or her most recent ten full fiscal years of service, the average annual salary is the average monthly salary during the term of the member's service multiplied by twelve.

The benefit amount that married members or unmarried members receive, who have elected to designate a beneficiary, is based on the normal benefit amount reduced by the following factors:

Factor	If the Spouse or Beneficiary is:
1.00	21 or more years older than the member
0.95	16 to 20 years older than the member
0.90	11 to 15 years older than the member
0.85	6 to 10 years older than the member
0.80	0 to 5 years younger than the member or 0 to 5 years older than the member
0.75	6 to 10 years younger than the member
0.70	11 to 15 years younger than the member
0.65	16 or more years younger than the member

Surviving beneficiaries of an employee may only receive benefits up to the total present value of the employee's accrued benefit pursuant to RPPL 9-2.

A member that meets the requirements for early retirement and elects to retire on an early retirement date is entitled to receive payment of an early retirement benefit equal to the member's normal retirement benefit reduced according to the following schedule based on the age at which early retirement benefit payments begin:

- $1/12^{th}$ per year for the first 3 years before age 60;
- plus an additional $1/18^{th}$ per year for the next 3 years;
- plus an additional $1/24^{th}$ per year for the next 5 years; and
- plus an additional $1/50^{th}$ per year for each year in excess of 11 years.

(3) Employees' Retirement Plan, Continued

Defined Benefit Plan, Continued

A. General Information About the Pension Plan, Continued:

Upon the death of a member or former member with eligible survivors before commencement of the members' normal, early, or late retirement benefits or disability retirement benefits the following shall be payable:

- If the former member is not an employee at his date of death and a spouse or beneficiary survives, the total death benefits payable shall be the actuarial equivalent of the member's present value of accrued benefit.
- If the member is an employee at his date of death and a spouse or beneficiary survives, the total death benefit payable shall be the actuarial equivalent of the greater of 3 times the member's average annual salary or the member's present value of accrued benefits.

Upon the death of a member or former member before commencement of his normal, early, or late retirement benefit or disability retirement benefit leaving no persons eligible for survivor benefits, the following shall be payable:

- If the former member is not an employee at the date of death, a refund of the total amount of contributions made by the member.
- If the member was an employee at the date of death and had completed one year of total service, the estate of the member shall be entitled to a death benefit equal to the greater of three times the member's annual salary or the present value of the member's accrued benefit payable in the form of a single lump sum payment.

Any member who is not otherwise eligible to receive normal, early or late retirement benefits, who shall become totally and permanently disabled for service regardless of how or where the disability occurred, shall be entitled to a disability retirement annuity, provided that he or she is not receiving disability payments from the United States Government or its agencies for substantially the same ailment, and further provided that to be eligible for a disability retirement annuity from a cause unrelated to service, the member shall have had at least ten (10) years of total service credited. The amount of disability retirement annuity shall be an amount equal to the actuarial equivalent at the attained age of the member's present value of accrued benefit and shall be paid in the same form as a normal retirement benefit. Any special compensation allowance received or payable to any member because of disability resulting from accidental causes while in the performance of a specific act or acts of duty shall be deducted from the disability annuity payable by the Plan on account of the same disability.

(3) Employees' Retirement Plan, Continued

Defined Benefit Plan, Continued

A. General Information About the Pension Plan, Continued:

Contributions. Member contribution rates are established by RPPL No. 2-26 at six percent of total payroll and are deducted from the member's salary and remitted by participating employers. Upon complete separation from service, a member with less than fifteen years membership service may elect to receive a refund of all of his or her contributions. Subsequent changes in the percentage contributed by members may be made through an amendment of the Trust Fund Operation Plan subject to the requirements of Title 6 of the Palau National Code. RPPL 9-2 requires each employee of the National Government and all State Governments, without regard to whether the employee is employed part-time or on a temporary basis, seasonal or an impermanent basis, to contribute to the Plan through payroll deduction.

Employers are required to contribute an amount equal to that contributed by employees. Pursuant to RPPL No. 2-26 and RPPL No. 3-21, the Government of the Republic of Palau must from time to time contribute additional sums to the Plan in order to keep the Plan on a sound actuarial basis. RPPL 9-2 requires the Government of ROP to make regular contributions to the Plan equal to the amount contributed by each and every employee of ROP. Additionally, an excise tax of four percent (4%) is levied against each non-citizen person transferring money out of ROP. The money transfer tax must be remitted to the Plan.

The Bank's contributions to the Plan for the years ended September 30, 2017 and 2016 were $24,518 and $23,081, respectively, which were equal to the required contributions for the years then ended.

Actuarial Assumptions. The total pension liability was determined by an actuarial valuation as of September 30, 2016, for the same measurement date, using the following actuarial assumptions:

Actuarial Cost Method:	Normal costs are calculated under the entry age normal method
Amortization Method:	Level dollar, open with remaining amortization period of 30 years
Asset Valuation Method:	Market Value of Assets
Investment Income:	7.5% per year, net of investment expenses
Expenses:	$300,000 each year
Inflation:	3.0%
Salary Increase:	3.0% per year

(3) Employees' Retirement Plan, Continued

Defined Benefit Plan, Continued

A. General Information About the Pension Plan, Continued:

Actuarial Assumptions, Continued

Mortality:	RP 2000 Combined Healthy Mortality Table, set forward four years for all members except disability recipients, where the table is set forward ten years
Termination of Employment:	5% per year prior to age 35; none after age 35
Disability:	

Age	Disability
25	0.21%
30	0.18%
35	0.25%
40	0.35%
45	0.50%
50	0.76%
55	1.43%
60	2.12%

Retirement Age:	100% at age 60
Form of Payment:	Single: Straight life annuity; Married: 100% joint and survivor
Duty vs Non-duty related disability:	100% Duty related
Pre-retirement Beneficiary Benefit Members:	Present value of accrued benefit earned by the member. 80% of the workers are assumed to be married and males are assumed to be 3 years older than their spouses
Post Retirement Survivor's Benefit:	100% of the benefit the retiree was receiving prior to death. 80% of active workers are assumed to be married when they retire. Males are assumed to be 3 years older than their spouses

Long-Term Expected Rate of Return

The long-term expected rate of return on the Bank's investments of 7.5% was determined using log-normal distribution analysis, creating a best-estimate range for each asset class.

As of September 30, 2016, the arithmetic real rates of return for each major investment class are as follows:

(3) Employees' Retirement Plan, Continued

Defined Benefit Plan, Continued

A. General Information About the Pension Plan, Continued:

Long-Term Expected Rate of Return, Continued

Asset Class	Target Allocation	Expected Rate of Return
Cash	3%	4.55%
Equity	61%	6.35%
Governmental fixed income	31%	7.75%
Corporate fixed income	5%	4.00%
	100%	

Discount Rate

The discount rate used to measure the total pension liability was 2.98% at the current measurement date and 3.83% at the prior measurement date. The discount rate was determined using the current assumed rate of return until the point where the plan fiduciary net position is negative. Using the current contribution rates, a negative position happens in 2019 for the 2016 measurement date. For years on or after 2019, a discount rate of 2.93% is used. This rate is based on the Bond Buyer General Obligation 20-year Municipal Bond Index.

Sensitivity of Net Pension Liability to Changes in the Discount Rate

The following presents the net pension liability of the Bank as of September 30, 2016, calculated using the discount rate of 2.98%, as well as what the net pension liability would be if it were calculated using a discount rate that is 1.00% lower (1.98%) or 1.00% higher (3.98%) from the current rate.

1% Decrease 1.98%	Current Single Discount Rate Assumption 2.98%	1% Increase 3.98%
$ 2,131,602	$ 1,837,001	$ 1,593,117

B. Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

Pension Liability. At September 30, 2017 and 2016, the Bank reported a liability of $1,837,001 and $1,630,006, respectively, for its proportionate share of the net pension liability. The Bank's proportion of the net pension liability was based on the projection of the Bank's long-term share of contributions to the Plan relative to the projected contributions of Republic of Palau, Republic of Palau's component units and other Government agencies, actuarially determined. At September 30, 2017 and 2016, the Bank's proportion was 0.7364% and 0.7562%, respectively.

Pension Expense. For the years ended September 30, 2017 and 2016, the Bank recognized pension expense of $72,325 and $67,754, respectively.

(3) Employees' Retirement Plan, Continued

Defined Benefit Plan, Continued

B. Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions, Continued

	2017			
	Salary and Other Benefits	Pension Expense Total Contributions	Others	Total
Personnel and fringe benefits	$ 526,527	$ 24,518	$ 47,807	$ 598,852

	2016			
	Salary and Other Benefits	Pension Expense Total Contributions	Others	Total
Personnel and fringe benefits	$ 477,223	$ 23,081	$ 44,673	$ 544,977

Deferred Outflows and Inflows of Resources. At September 30, 2017 and 2016, the Bank reported total deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	2017		2016	
	Deferred Outflows of Resources	Deferred Inflows of Resources	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between expected and actual experience	$ -	$ 47,083	$ -	$ 58,360
Change of assumptions	281,540	43,443	133,732	66,806
Net difference between projected and actual earnings on pension plan investments	15,775	3,571	18,491	-
The Bank's contributions subsequent to measurement date	24,518	-	23,081	-
Changes in proportion and difference between the Bank's contributions and proportionate share of contributions	15,818	121,947	23,689	111,408
	$ 337,651	$ 216,044	$ 198,993	$ 236,574

Deferred outflows resulting from contributions subsequent to measurement date will be recognized as a reduction of the net pension liability in the following year. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions at September 30, 2017 will be recognized in pension expense as follows:

Year ending September 30,	
2018	$ 7,071
2019	$ 7,126
2020	$ 21,704
2021	$ 19,522
2022	$ 21,309
Thereafter	$ 20,357

(4) Economic Development Loans and Allowance for Loan Losses

Major classifications of loans receivable as of September 30, 2017 and 2016 are as follows:

	2017	2016
Housing	$ 11,187,398	$ 10,679,208
Commercial	7,618,347	7,869,329
Agriculture	847,471	281,106
Fishing	374,316	278,350
Loans receivable	20,027,532	19,107,993
Less allowance for loan losses	(891,355)	(995,979)
	$ 19,136,177	$ 18,112,014

Maturities of the above principal balances subsequent to September 30, 2017, will be as follows:

	2017	2016
Fully matured and others	$ 10,576	$ 19
1 - 6 months	1,830,918	1,059,515
7 - 18 months	3,491,555	2,027,679
19 months - 3 years	4,347,803	2,310,339
After 3 years	10,346,680	13,710,441
	$ 20,027,532	$ 19,107,993

An analysis of the change in the allowance for loan losses is as follows:

	2017	2016
Balance - beginning of year	$ 995,979	$ 1,781,264
Recoveries of loan previously charged-off	285,544	201,678
Provision for (recovery of) loan losses	190,930	(492,375)
Loans charged-off	(581,098)	(494,588)
Balance - end of year	$ 891,355	$ 995,979

(5) Capital Assets

A summary of capital assets as of September 30, 2017 and 2016, is as follows:

	Estimated Useful Lives	Balance at October 1, 2016	Additions	Deletions	Balance at September 30, 2017
Depreciable assets:					
Leasehold rights	39 - 50 years	$ 493,206	$ -	$ -	$ 493,206
Leasehold improvements	5 years	279,427	39,800	-	319,227
Furniture, fixtures and equipment	2 - 20 years	224,135	23,770	-	247,905
Vehicles	5 years	83,719	29,391	-	113,110
		1,080,487	92,961	-	1,173,448
Less accumulated depreciation		(457,279)	(40,667)	-	(497,946)
		$ 623,208	$ 52,294	$ -	$ 675,502

(5) Capital Assets, Continued

	Estimated Useful Lives	Balance at October 1, 2015	Additions	Deletions	Balance at September 30, 2016
Depreciable assets:					
Leasehold rights	39 - 50 years	$ 493,206	$ -	$ -	$ 493,206
Leasehold improvements	5 years	252,422	27,005	-	279,427
Furniture, fixtures and equipment	2 - 20 years	222,895	1,240	-	224,135
Vehicles	5 years	83,719	-	-	83,719
		1,052,242	28,245	-	1,080,487
Less accumulated depreciation		(420,326)	(36,953)	-	(457,279)
		$ 631,916	$ (8,708)	$ -	$ 623,208

(6) Foreclosed Real Estate

Foreclosed real estate as of September 30, 2017 and 2016 amounted to $347,199. There are no additions or disposals in fiscal years 2017 and 2016. Title to foreclosed real estate of $347,199 is in the Bank's name as of September 30, 2017 and 2016.

(7) Loans Payable and Other Liabilities

On August 28, 2003, the Bank entered into a loan with the Republic of Palau Social Security Retirement Fund (the Fund), an affiliated entity and a component unit of ROP. The loan was for $3,000,000 with a subsequent $2,000,000 line of credit to be made available with terms and conditions to be agreed to by the parties at that time.

On August 7, 2008, the Bank entered into a new loan agreement to restructure the existing loan with the Fund. The loan ceiling increased to $6,000,000 which will be disbursed in increments of $500,000, bearing interest at a variable annual rate equal to the Fund's Fixed Income Fund Return Rate as reported monthly by Fund's investment consultant, plus 0.5%; provided, however that the interest rate to be charged and paid shall not be less than 4.5% nor more than 7.5% after addition of the 0.5% to the prime rate. Outstanding principal plus all unpaid interest is to be paid semi-annually, on or before June 30 and December 31 of each year, effective June 30, 2011 up to December 31, 2025.

The loan was $3,019,475 and $3,318,617 with interest at 4.5% as of September 30, 2017 and 2016, respectively. The loan is collateralized by the full faith and credit of the ROP Government.

On March 5, 2004, the Bank entered into a loan with Mega International Commercial Bank Co., Ltd. (formerly the International Commercial Bank of China) for $5,000,000 to be used as capital funds for the Bank. The note is uncollateralized and is due on July 1, 2024, with interest fixed at 3.5% per annum, payable in semi-annual installments of $142,858, and guaranteed by ROP. Interest is payable semi-annually and commences six months after the advance of proceeds. Annual expected principal repayments are $285,716. The balance outstanding is $1,999,982 and $2,285,698 at September 30, 2017 and 2016, respectively.

(7) Loans Payable and Other Liabilities, Continued

On December 5, 2006, the Bank entered into an agreement with the European Investment Bank (EIB) to borrow up to 5,000,000 euros, which will be converted to U.S. dollars at the effective exchange rate upon disbursement. The available credit shall be drawn in tranches upon written request by the Bank. Loan proceeds may be used for purposes of financing 50% of the total cost of projects and portfolio projects of the Bank. The agreement is backed by the full faith and credit of the government of ROP. As of September 30, 2017 and 2016, the Bank has drawn down two tranches of $3,016,465 and $1,391,285 with interest rates of 5.175% and 3.679%, respectively. Interest and principal are payable semi-annually until September 10, 2021. On December 12, 2011, EIB cancelled the remaining balance of the Bank's credit line of 1,739,427 euros. The balance outstanding at September 30, 2017 and 2016 is $1,639,046 and $2,008,753, respectively.

On May 17, 2012, the Bank entered into a $4,000,000 loan agreement with ROP to finance a loan to the Palau National Communications Corporation (PNCC) for the acquisition of underwater fiber-optic cable for $3,000,000 and for additional Bank lending activities. The note is uncollateralized and is due and payable 120 months after the loan date, with interest fixed at 2.0% per annum, payable in monthly installments. Interest and principal is payable monthly and commences thirty-six months after the advance of proceeds over the remaining period of the loan term. The PNCC fiber-optic project did not proceed and $3,000,000 was returned to ROP on April 5, 2013. The balance outstanding at September 30, 2017 and 2016 is $682,083 and $820,151, respectively.

On March 31, 2016, the Bank entered into a $5,000,000 loan agreement with ROP to finance the development of agriculture and aquaculture projects in Palau. ROP is to provide the Bank with up to $500,000 of loan losses coverage for losses suffered under the loan program applicable to payments five years after the agreement. The note is uncollateralized and is due on March 31, 2036, and with interest based on 6-month LIBOR plus one percent (1%) per annum (effective interest rates were 2.41989% and 3.52% as of September 30, 2017 and 2016, respectively), payable semi-annually until September 30, 2018 with the first semi-annual installment of $142,857 payable on March 31, 2019. Annual expected principal payments are $285,714. The outstanding balance is $5,000,000 at September 30, 2017 and 2016.

Principal payments for subsequent years ending September 30 and applicable interest due, are as follows:

Year ending September 30,	Principal	Interest	Total
2018	$ 1,174,745	$ 349,423	$ 1,524,168
2019	1,464,351	303,992	1,768,343
2020	1,495,469	254,268	1,749,737
2021	1,528,311	202,252	1,730,563
2022	1,057,684	155,094	1,212,778
2023 - 2027	3,191,297	363,902	3,555,199
2028 - 2032	1,428,570	147,167	1,575,737
2033 - 2036	1,000,159	47,018	1,047,177
	$ 12,340,586	$ 1,823,116	$ 14,163,702

(7) Loans Payable and Other Liabilities, Continued

Changes in loans payable and other liabilities for the years ended September 30, 2017 and 2016, are as follows:

	Balance October 1, 2016	Additions	Reductions	Balance September 30, 2017	Due Within One Year
Republic of Palau Social Security Retirement Fund	$ 3,318,617	$ -	$ (299,142)	$ 3,019,475	$ 363,117
ROP Government	5,820,151	-	(138,068)	5,682,083	140,853
Mega International Commercial Bank	2,285,698	-	(285,716)	1,999,982	285,716
European Investment Bank	2,008,753	-	(369,707)	1,639,046	385,059
	$ 13,433,219	$ -	$ (1,092,633)	$ 12,340,586	$ 1,174,745
Other liabilities:					
Net pension liability	$ 1,630,006	$ 206,995	$ -	$ 1,837,001	$ -

	Balance October 1, 2015	Additions	Reductions	Balance September 30, 2016	Due Within One Year
Republic of Palau Social Security Retirement Fund	$ 3,587,578	$ -	$ (268,961)	$ 3,318,617	$ 325,469
ROP Government	955,486	5,000,000	(135,335)	5,820,151	138,066
Mega International Commercial Bank	2,571,414	-	(285,716)	2,285,698	285,716
European Investment Bank	2,363,736	-	(354,983)	2,008,753	369,707
	$ 9,478,214	$ 5,000,000	$ (1,044,995)	$ 13,433,219	$ 1,118,958
Other liabilities:					
Net pension liability	$ 1,566,428	$ 63,578	$ -	$ 1,630,006	$ -

(8) Related Party Transactions

The Bank grants loans to affiliates, officers and employees. Loans made to related parties were extended in the normal course of business and at prevailing interest rates. Loans receivable from officers and employees are $283,655 and $227,271 as of September 30, 2017 and 2016, respectively. Loans receivables from an affiliate amount to $2,062,041 and $2,219,603 as of September 30, 2017 and 2016, respectively. Loans receivable from officers and employees and loans receivable from an affiliate are included within economic development loans receivable in the accompanying statements of net position.

(9) Commitments

Loans Approved

At September 30, 2017 and 2016, $8,209,569 and $7,862,728, respectively, of approved loans was undisbursed. Of the undisbursed loans as of September 30, 2017 and 2016, $4,822,798 and $4,673,297, respectively, relates to performance bonds on various construction contracts where the Bank acts as insurer and $137,398 and $153,574, respectively, relates to letters of credit. At September 30, 2017 and 2016, no performance bonds have been called.

Leases

On March 20, 2008, the Bank entered into an agreement with the Airai State Public Lands Authority for the lease of land to be used for bank operations and other related business. The term of the lease is fifty years commencing March 20, 2008.

(9) Commitments, Continued

Leases, Continued

Total future minimum lease payments for subsequent years ending September 30, are as follows:

Years ending September 30,	
2018	$ 3,441
2019	3,441
2020	3,441
2021	3,441
2022	3,441
2023 - 2027	17,205
2028 - 2032	17,205
2033 - 2037	29,249
2038 - 2042	34,410
2043 - 2047	34,410
2048 - 2052	34,410
2053 - 2057	34,410
2058	6,887
Total future minimum payments	$ 225,391

(10) Contingencies

On February 1, 2011, the Bank amended the MOU originally entered into on February 16, 1995 with the USDA RD to provide housing for low and very low income residents of ROP. Under the agreement, the USDA RD will make loans to the owners and lessees of ROP lands and the Bank will guarantee the repayment of the loan for which the Bank has issued a written guarantee. The Bank has approved guarantees for seventy-six loans aggregating $4,071,922 at September 30, 2017. Unpaid interest and subsidies related to the loan guarantees as of September 30, 2017 amounted to $22,265 and $998,268, respectively, for which the Bank becomes liable once the borrower defaults and a demand notice is issued. As of September 30, 2017, no demand notice has been received by the Bank.

RPPL 5-37 increased the ROP's full faith and credit backing for loans, loan guarantees, and obligations under recourse loan repurchase agreements made by the Bank to $15,000,000. Of this amount, $2,000,000 shall be for residential housing projects and $5,000,000 for the purpose of satisfying requirements for obtaining loans from a bank.

(11) Risk Management

The Bank is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions, injuries to employees; and natural disasters. The Bank has elected to purchase commercial insurance from independent third parties for the risks of loss to which it is exposed. Settled claims from these risks have not exceeded commercial insurance coverage for the past three years.

NATIONAL DEVELOPMENT BANK OF PALAU

Required Supplemental Information (Unaudited)
Schedule of Proportional Share of the Net Pension Liability
Last 10 Fiscal Years*

	September 30,			
	2016 Valuation	2015 Valuation	2014 Valuation	2013 Valuation
Civil Service Pension Trust Fund (Plan) total net pension liability	$ 249,453,960	$ 215,546,176	$ 204,281,232	$ 182,080,333
The Bank's proportionate share of the net pension liability	$ 1,837,001	$ 1,630,006	$ 1,566,428	$ 1,523,284
The Bank's proportion of the net pension liability	0.736%	0.756%	0.767%	0.837%
The Bank's covered employee payroll**	$ 390,026	$ 366,745	$ 360,465	$ 349,499
The Bank's proportionate share of the net pension liability as a percentage of its covered employee payroll	470.99%	444.45%	434.56%	435.85%
Plan fiduciary net position as a percentage of the total pension liability	10.55%	11.54%	14.01%	15.84%

* This data is presented for those years for which information is available.
** Covered-employee payroll data from the actuarial valuation date with one-year lag.

See accompanying Independent Auditors' Report.

NATIONAL DEVELOPMENT BANK OF PALAU

Required Supplemental Information (Unaudited)
Schedule of Pension Contributions
Last 10 Fiscal Years*

	September 30,			
	2016 Valuation	2015 Valuation	2014 Valuation	2013 Valuation
Actuarially determined contribution	$ 106,170	$ 82,427	$ 81,456	$ 84,209
Contribution in relation to the actuarially determined contribution	23,081	21,858	21,226	21,048
Contribution (excess) deficiency	$ 83,089	$ 60,569	$ 60,230	$ 63,161
The Bank's covered-employee payroll**	$ 390,026	$ 366,745	$ 360,465	$ 349,499
Contribution as a percentage of covered-employee payroll	5.92%	5.96%	5.89%	6.02%

* This data is presented for those years for which information is available.
** Covered-employee payroll data from the actuarial valuation date with one-year lag.

See accompanying Independent Auditors' Report.