

Palau

RISK & COMPLIANCE REPORT

DATE: March 2018

Executive Summary

Sanctions:	None
FAFT list of AML Deficient Countries	No
Higher Risk Areas:	<p>Compliance with FATF 40 + 9 Recommendations</p> <p>Weakness in Government Legislation to combat Money Laundering</p> <p>Corruption Index (Transparency International & W.G.I.)</p> <p>Not on EU White list equivalent jurisdictions</p> <p>EU Tax Blacklist</p>
Medium Risk Areas:	<p>Corruption Index (Transparency International & W.G.I.))</p> <p>World Governance Indicators (Average Score)</p> <p>Failed States Index (Political Issues)(Average Score)</p>
<p>Major Investment Areas:</p> <p>Agriculture - products:</p> <p>coconuts, copra, cassava (tapioca), sweet potatoes; fish</p> <p>Industries:</p> <p>tourism, craft items (from shell, wood, pearls), construction, garment making</p> <p>Exports - commodities:</p> <p>shellfish, tuna, copra, garments</p> <p>Imports - commodities:</p> <p>machinery and equipment, fuels, metals; foodstuffs</p>	
<p>Investment Restrictions:</p> <p>According to Palauan law, the following businesses are solely reserved for Palauan citizens:</p> <p style="padding-left: 40px;">“ (i) wholesale or retail sale of goods; (ii) all land transportation including bus services, taxi services and car rentals; (iii) tour guides, fishing guides, diving guides and any other form of water transportation services; (iv) travel and tour agencies; and (v) commercial fishing for other than highly migratory species”</p>	

While all of the businesses above are officially closed to foreign investment, there is a prevalent use of partnership companies in several categories, in which the foreign investor owns less than fifty percent. The retail sector, as well as travel- and tour-related businesses, currently has numerous foreign investors via such partnership companies.

Regulatory changes that occurred in 2010 created a new category of "semi-restricted" sectors. These sectors had been closed to foreign investors from the passage of the 1991 Foreign Investment Act through October 2010. Now, these formerly-restricted businesses can include foreign ownership, as long as a Palauan citizen also has an ownership interest. There are no minimum or maximum requirements for percentage ownership for the foreign investor, as long as the monetary and/or Palauan-employment minimums for all foreign investments are met (as discussed below).

These semi-restricted businesses are as follows:

- (i) handicraft and gift shops;
- (ii) bakeries;
- (iii) bar services;
- (iv) operations [selling] products being produced by wholly Palauan-owned manufacturing enterprise;
- (v) equipment rentals for both land and water within the Republic, including equipment for purpose of tourism; and
- (vi) any such other businesses, as the Foreign Investment Board may determine

Sectors not listed as either closed or semi-restricted are presumed to be open for foreign investment. The Foreign Investment Board may, however, amend the semi-restricted sector list for "*any such other businesses as the Board may determine.*"

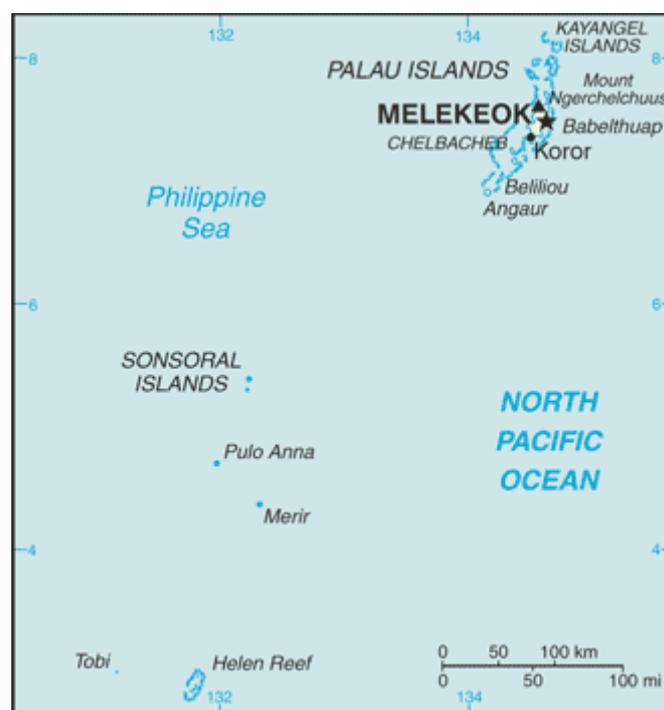
Other than the foreign-ownership restrictions for certain business sectors, there are no restrictions on private entities to engage in all forms of remunerative activity. However, establishing secure land title may be complicated due to the complexity of the traditional land ownership system and occasional over-lapping claims.

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Section 1 - Background

After three decades as part of the UN Trust Territory of the Pacific under US administration, this westernmost cluster of the Caroline Islands opted for independence in 1978 rather than join the Federated States of Micronesia. A Compact of Free Association with the US was approved in 1986 but not ratified until 1993. It entered into force the following year when the islands gained independence.



Section 2 - Anti – Money Laundering / Terrorist Financing

FATF status

Palau is not on the FATF List of Countries that have been identified as having strategic AML deficiencies

Compliance with FATF Recommendations

The last Mutual Evaluation Report relating to the implementation of anti-money laundering and counter-terrorist financing standards in Palau was undertaken by the Financial Action Task Force (FATF) in 2008. According to that Evaluation, Palau was deemed Compliant for 4 and Largely Compliant for 10 of the FATF 40 + 9 Recommendations. It was Partially Compliant or Non-Compliant for 5 of the 6 Core Recommendations.

Key Findings from latest Mutual Evaluation Report (2008):

Palau has recently strengthened its AML/CFT legislative framework that has been in place since 2001 with the amendments to the Money Laundering and Proceeds of Crime Act of 2001 (MLPCA) and the Financial Institutions Act of 2001 (FIA), and with the enactments of the Counter- Terrorism Act of 2007 (CTA) and the Cash Courier Disclosure Act of 2007 (CCDA). Even though legislation has been in place for several years, there has not been sufficient implementation. Now that Palau has adopted additional legislative measures to safeguard its financial sector from misuse for money laundering (ML) and financing of terrorism (FT), the authorities should now expeditedly devote the resources to implementing the legislation.

The offense of money laundering is criminalized in the MLPCA; however, only about half of the twenty FATF designated categories of predicate offenses are covered by the money laundering offense. The financing of terrorism has been criminalized in 2007, yet the freezing of terrorist assets under UN Security Council Resolutions (UNSCRs) 1267 and 1373 is not adequately addressed. Palauan law shows several deficiencies with respect to the provisional measures of seizing of evidence and property and the freezing of capital and financial transactions.

The amended MLPCA does not cover the preventive measures in a satisfactory manner. There remain significant deficiencies in the areas of customer due diligence, record keeping, monitoring of transactions and relationships, and supervisory and oversight systems. Under the MLPCA, the Financial Institutions Commission (FIC) is the AML/CFT supervisor for the banks, the finance companies, the credit unions, and the money and value transfer services (MVTs). The insurance agents are covered by the MLPCA, yet not for AML/CFT supervision. The FIC does not have the resources to ensure AML/CFT compliance nor to issue any regulations or guidelines. The only designated non-financial businesses and professions (DNFBPs) that

operate in Palau are attorneys who also provide company formation services; they are not covered by the MLPCA.

The Financial Intelligence Unit (FIU) has very recently been moved from the Office of the Attorney General (OAG) to the FIC; however, the FIC has not been provided with additional human, technical or financial resources to adequately carry out this additional FIU task. Without Palau dedicating additional resources, the overall AML/CFT systems remain deficient in several areas.

US Department of State Money Laundering assessment (INCSR)

Palau was deemed a 'Monitored' Jurisdiction by the US Department of State 2016 International Narcotics Control Strategy Report (INCSR).

Key Findings from the report are as follows: -

Perceived Risks:

Palau is not a regional or offshore financial center. The primary sources of illegal proceeds are illegal drugs and prostitution. Corruption in the governmental sector includes the misuse of government funds and cronyism, in part due to Palau's small size and extensive family networks. Palau is a low-risk jurisdiction for organized crime and terrorism financing.

Palau has one free trade zone, the Ngardmau Free Trade Zone (NFTZ). A public corporation, Ngardmau Free Trade Zone Authority, oversees the development of the NFTZ and issues licenses for businesses to operate there. NFTZ licensing exempts businesses from Foreign Investment Act requirements and certain import and export taxes. To date, no development has taken place within the designated free trade zone area, and the NFTZ directors continue to search for developers and investors.

DO FINANCIAL INSTITUTIONS ENGAGE IN CURRENCY TRANSACTIONS RELATED TO INTERNATIONAL NARCOTICS TRAFFICKING THAT INCLUDE SIGNIFICANT AMOUNTS OF US CURRENCY; CURRENCY DERIVED FROM ILLEGAL SALES IN THE U.S.; OR ILLEGAL DRUG SALES THAT OTHERWISE SIGNIFICANTLY AFFECT THE U.S.: NO

CRIMINALIZATION OF MONEY LAUNDERING:

"All serious crimes" approach or "list" approach to predicate crimes: List approach
Are legal persons covered: criminally: YES civilly: YES

KNOW-YOUR-CUSTOMER (KYC) RULES:

Enhanced due diligence procedures for PEPs: Foreign: NO Domestic: NO
KYC covered entities: Banks, credit unions, money remitters, casinos, real estate agents, dealers in precious metals, lawyers, and trust company providers

REPORTING REQUIREMENTS:

Number of STRs received and time frame: Not available
Number of CTRs received and time frame: Not available

STR covered entities: Banks, credit unions, money remitters, and non-governmental organizations

MONEY LAUNDERING CRIMINAL PROSECUTIONS/CONVICTIONS:

Prosecutions: 0 in 2015

Convictions: 0 in 2015

RECORDS EXCHANGE MECHANISM:

With U.S.: MLAT: NO Other mechanism: YES

With other governments/jurisdictions: YES

Palau is a member of the Asia/Pacific Group on Money Laundering (APG), a FATF-style regional body.

ENFORCEMENT AND IMPLEMENTATION ISSUES AND COMMENTS:

The Money Laundering Prevention and Control Act does not include all predicate crimes prescribed in the international standards and currently lacks implementing regulations. The Palau National Code Annotated (PNCA), with particular reference to Title 17, was ratified by the President of Palau on April 24, 2014. The PNCA strengthens record-keeping requirements and expands the definition of DNFBPs to include casinos, real estate agents, dealers in precious metals, lawyers, and trust company providers. However, regulations to implement customer due diligence (CDD) procedures for these entities have not been adopted. Significant deficiencies remain in the areas of CDD, monitoring of transactions, and supervision. Regulations to correct deficiencies in CDD have been pending since 2012, including regulations to establish enhanced due diligence procedures for both domestic and foreign politically exposed persons (PEPs). The Financial Institutions Commission is the AML/CFT supervisor; however, it does not have the resources to issue any regulations nor to ensure compliance.

The Palau financial intelligence unit (FIU) operates under very limited budget and staff constraints. The FIU has a database of financial information, with a mechanism for electronic report submission, in order to increase the effectiveness of the FIU. Unfortunately, reporting institutions continue to send reports in hard copy, which causes hardship for the FIU, which already operates at a deficit due to the lack of resources.

The government continues to have in place a multi-agency suspicious transaction report (STR) review team to analyze the reports to help identify and initiate investigations, but it has not been active in recent years. Historically, the multi-agency approach has enabled the FIU to function and has fostered information sharing and joint investigations among the relevant law enforcement agencies. However, the meetings seldom occur and there are no joint investigations currently.

The Cash Courier Disclosure Act is used by Palau Customs and Security to make bulk cash currency seizures at the airport. There have been a number of instances of undeclared bulk cash coming in via foreign nationals at the airport. When questioned after finding reportable cash in their luggage, passengers often claim they do not speak English and do not understand the customs form. Current customs legislation and low penalties for failure to declare are not sufficient deterrents to curb this activity.

Palau's Counter-Terrorism Act does not adequately address provisional measures for seizing of evidence and property, or the freezing of capital and financial transactions related to the financing of terrorism.

The Government of Palau should remedy the shortfalls in the AML legislation, adopt its pending CDD regulations, and bolster its supervision regime. Palau should also dedicate additional funds and permanent staff to the FIU. The FIU should release statistics, including the annual numbers of reports filed. The government should extend its effective monitoring of the airport to all its border points of entry and exit to protect against the smuggling of bulk cash, narcotics, and other contraband and review its penalties for cash smuggling to determine if they are adequate deterrents. Palau should strengthen its ability to freeze and confiscate assets related to terrorism financing, including by circulating the UNSCR 1267 Sanctions Committee's consolidated list of terrorist entities. Palau also should become a party to the 1988 UN Drug Convention and the UN Convention against Transnational Organized Crime.

EU Tax Blacklist

Palau facilitates offshore structures and arrangements aimed at attracting profits without real economic substance and refused to engage in a meaningful dialogue to ascertain its compliance of with criterion 2.2.

Palau's commitment to comply with criteria 1.1, 1.2, 1.3 and 3 will be monitored.

Current Weaknesses in Government Legislation (2013 INCRS Comparative Tables):

According to the US State Department, Palau does not conform with regard to the following government legislation: -

System for Identifying/Forfeiting Assets - The jurisdiction has enacted laws authorizing the tracing, freezing, seizure, and forfeiture of assets identified as relating to or generated by money laundering activities.

Arrangements for Asset Sharing - By law, regulation or bilateral agreement, the jurisdiction permits sharing of seized assets with third party jurisdictions that assisted in the conduct of the underlying investigation.

States Party to UN 1988 Convention - States parties to the 1988 United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, or a territorial entity to which the application of the Convention has been extended by a party to the Convention.

States Party to United Nations Transnational Organised Crime Convention - States party to the United Nations Convention against Transnational Organized Crime (UNTOC), or a territorial entity to which the application of the Convention has been extended by a party to the Convention.

States Party to United Nations Convention Against Corruption - States party to the United Nations Convention against Corruption (UNCAC), or a territorial entity to which the application of the Convention has been extended by a party to the Convention.

EU White list of Equivalent Jurisdictions

Palau is not currently on the EU White list of Equivalent Jurisdictions

World Governance indicators

[To view historic Governance Indicators Ctrl + Click here and then select country](#)

Failed States Index

[To view Failed States Index Ctrl + Click here](#)

Offshore Financial Centre

Palau is not considered to be an Offshore Financial Centre

US State Dept Narcotics Report

No report available

US State Dept Trafficking in Persons Report 2016 (introduction):

Palau is classified a Tier 2 country - a country whose government does not fully comply with the Trafficking Victims Protection Act's minimum standards, but is making significant efforts to bring themselves into compliance with those standards.

Palau is a destination country for women subjected to sex trafficking and for women and men subjected to forced labor. Palau's foreign population, about one-third of the country's population of 21,000, is the most vulnerable to trafficking. Filipino, Bangladeshi, Nepalese, Chinese, and Korean men and women pay thousands of dollars in recruitment fees and willingly migrate to Palau for jobs in domestic service, agriculture, restaurants, or construction; upon arrival, some are forced to work in conditions substantially different from what had been presented in contracts or recruitment offers, and some become trafficking victims. Women from China and the Philippines are recruited to work in Palau as waitresses or clerks, but some are subsequently forced into prostitution in karaoke bars or massage parlors—many operated by Taiwanese, Filipino, or Palauan nationals. Foreign workers on fishing boats in Palau waters experience conditions indicative of human trafficking. Regulations that make it difficult for foreign workers to change employers once they arrive in Palau place foreign workers at increased risk of involuntary servitude and debt bondage. Official complicity plays a role in facilitating trafficking; government officials—including a governor, a police officer, a labor official, and an immigration official—have been investigated for complicity in trafficking crimes during previous reporting periods.

The Government of Palau does not fully meet the minimum standards for the elimination of trafficking; however, it is making significant efforts to do so. In 2015, the government initiated two investigations of trafficking cases, assisted potential victims involved in court cases to find new employment, and convicted one labor trafficker. The government instituted a sex offender registry and deported some fraudulent labor recruiters. It held weekly anti-trafficking taskforce meetings. The government, however, did not apply sufficiently stringent punishments, as it regularly charged suspected traffickers with lesser crimes and sentenced convicted traffickers to probation or inadequate prison sentences. The government did not provide shelter or protection services to identified victims.

Latest US State Dept Terrorism Report 2009

Palau worked closely with the United States on counterterrorism. Local law enforcement officers from the Ministry of Justice, Ministry of Public Infrastructure, Industries and Commerce, and the Division of Customs continued to receive training on counterterrorism from U.S. counterparts. In addition, the Federal Aviation Administration and the Transportation Security

Administration regularly inspected airport facilities and trained airport officials on security procedures.

Responding to UN Security Council Resolution 1373, the national congress passed a Foreign Evidence Act, a Money Laundering and Proceeds of Crime Act, a Mutual Assistance in Criminal Matters Act, and an Extradition and Transfer Act in 2001. These laws are intended to regulate the banking system, criminalize money laundering, and provide a legal basis for international law enforcement cooperation. A Financial Intelligence Unit was established to detect money laundering and other financial crimes.

International Sanctions

None Applicable

Index	Rating (100-Good / 0-Bad)
Transparency International Corruption Index	N/A
World Governance Indicator – Control of Corruption	38

Corruption and Government Transparency - Report by US State Department

Palau acceded to the United Nations Convention Against Corruption (UNCAC) in March, 2009. It has been a member of the Asian Pacific Group on Money Laundering (APGML) since 2002. Palau's legal system is based on common law (as understood and applied in the United States) and customary laws. Its criminal bribery offences have not been externally reviewed. The Code of Ethics Act spells out what is illegal for government officials, and the Public Auditor and the Special Prosecutor hold them accountable for failure to observe the law.

Palau is currently the only one of the Micronesian nations to employ a Special Prosecutor; however this position has been vacant since 2010. Prior to this vacancy, successive Special Prosecutors successfully prosecuted a large number of elected Federal and State officials, recovering substantial sums of money. Most corruption (proved and alleged) involves improper use of government funds or property, and/or fraudulent collaborations of various kinds. Even without a sitting special prosecutor, there have been several high profile prosecutions/resignations by public officials related to violations of Palau's government ethics law. None involved alleged abuse targeting foreign investors. Government extortion or semi-extortion of private companies is virtually unknown.

Local media often reports on alleged corruption cases, and serves as an informal watchdog. Palau does not appear in Transparency International's Index of Corruption (which includes ratings of 184 countries). However, in a 2004 country report, Transparency International praised the fairness and professionalism of Palau's judiciary. There are no formal anti-corruption NGOs or international watchdogs based in Palau.

Palau is not a member of the OECD Convention on Combating Bribery.

Section 3 - Economy

The economy consists of tourism and other services such as trade, subsistence agriculture, and fishing. Government is a major employer of the work force relying on financial assistance from the US under the Compact of Free Association (Compact) with the US that took effect after the end of the UN trusteeship on 1 October 1994. The US provided Palau with roughly \$700 million in aid for the first 15 years following commencement of the Compact in 1994 in return for unrestricted access to its land and waterways for strategic purposes. The population enjoys a per capita income roughly double that of the Philippines and much of Micronesia.

Business and leisure tourist arrivals numbered over 125,000 in fiscal year 2014, a 13.4% increase over the previous year. Long-run prospects for tourism have been bolstered by the expansion of air travel in the Pacific, the rising prosperity of industrial East Asia, and the willingness of foreigners to finance infrastructure development. Proximity to Guam, the region's major destination for tourists from East Asia, and a regionally competitive tourist infrastructure enhance Palau's advantage as a destination.

Agriculture - products:

coconuts, copra, cassava (manioc, tapioca), sweet potatoes; fish

Industries:

tourism, craft items (from shell, wood, pearls), construction, garment making

Exports - commodities:

shellfish, tuna, copra, garments

Imports - commodities:

machinery and equipment, fuels, metals; foodstuffs

Banking

The Palau banking industry consists of seven banks that are licensed by the FIC to operate as banks as defined under the Financial Institutions Act of 2001 (FIA). There are four branches of foreign banks, of which three are chartered in the U.S. and one in Taiwan. These four foreign-owned banks are, besides being supervised by the FIC, also regulated by their domestic regulators: the FDIC and other competent U.S. authorities for the U.S. banks and the Taiwanese supervisor for the Taiwanese bank. These four banks make up 80 percent of the market in Palau; the remainder is split amongst the three locally-chartered banks. These three local banks are chartered in Palau and are licensed and subject to regulation and supervision by the FIC.

Palau law does not allow for the establishment of offshore banks and the FIC is the primary licensing authority for institutions that engage in banking activities in the country. Currently, local banks are unable to establish branches outside Palau. Banks licensed in Palau are required to incorporate and the FIC has exclusive authority for the licensing of these institutions. The banking sector also includes the National Development Bank of Palau which is solely engaged in business financing and mortgage lending and is not allowed to take

deposits as per its enabling statute that created this institution. This bank is not licensed or regulated by the FIC, as it is exempted under the FIA.

Executive Summary

Palau's economy is dominated by tourism, subsistence agriculture, and fishing. The government is the country's largest employer. The Compact of Free Association with the United States governs the relationship between the U.S. and Palau. Palau's per capita income is over \$10,500 per year.

The Foreign Investment Act provides the approval-process guidance for foreign investment, and the Foreign Investment Regulations reserves some businesses to Palauan citizens, including wholesale or retail sale of goods, all land and water transportation, travel and tour agencies, and commercial fishing. Other sectors are semi-restricted, requiring a Palauan partner, though no fixed percent of ownership is required.

Palau's economy uses the U.S. dollar. Palau has a strong banking sector with three FDIC-insured U.S. banks.

Palau's judicial system is viewed by Transparency International and other observers as professional and fair. Regulatory and accounting systems are generally transparent and consistent with international norms.

Foreigners cannot own land in Palau, but they can lease land and own buildings on leased land. Establishing secure land title may be complicated due to the complexity of the traditional land ownership system and occasional over-lapping claims.

Palau is not a member of the World Intellectual Property Organization, the WTO, or any other organization or convention protecting intellectual property rights.

Palau has no bilateral investment protection agreements, and is not a member of any free trade associations. Foreign labor comprises a large proportion of Palau's labor force.

U.S. citizens are exempt from the Palau's normal resident visa requirements. A visa is not required for U.S. citizens visiting Palau for one year or less, provided the visitor otherwise complies with applicable regulations.

1. Openness to, and Restrictions Upon, Foreign Investment

Palau's economy is dominated by tourism, subsistence agriculture, and fishing. The government is the country's largest employer. The Compact of Free Association with the United States, entered into after the end of the UN trusteeship on 1 October 1994, provided Palau with up to \$700 million in U.S. aid for the following 15 years. Foreign assistance grants comprise approximately 20 percent of GDP and finance roughly 50 percent of government spending. Palau's per capita income is over \$10,500 per year.

Palau's economy contracted in 2008 and 2009, due to the global economic crisis, and its effect on tourism spending and other outside investment into Palau. The number of tourist visitors rebounded in 2010, and hit new records in 2011 and 2012, though the number of arrivals fell slightly in 2013. New markets, such as Russia, have barely been tapped, and offer great potential. However, Palau's present hotel and other infrastructure limit its ability to absorb potential major increases in tourist numbers.

A 15-year renewal of grants for the U.S. Compact of Free Association is currently under review in the U.S. Congress. However, Palau must prepare for the eventual conclusion of Compact Grant funds. With Palau's current deficit, the Asian Development Bank estimates that an appropriate fiscal policy would require Palau to reduce its current deficit by 1½ percent of current GDP each year for the next 10 years. A 2012 IMF review applauded Palau's deficit-reduction efforts, but noted the need for reduced government employment and revenue reforms.

The 1991 Foreign Investment Act provides the approval-process guidance for foreign investment. In late 2010 the Government of Palau revised its implementing regulations, changing several key requirements in a bid to encourage more foreign investment. A broader reform of the investment law stalled in Palau's bicameral National Congress, or Olbiil Era Kelulau (OEK). The new "Regulations Implementing the Foreign Investment Act, 28 Pnc Section 101 *et seq.*," were signed by President Johnson Toribiong on August 1, 2010, and went into effect on November 1, 2010.

The 2011 Foreign Investment Regulations detail the significant number of restricted and semi-restricted sectors. There are no specific financial incentives extended to foreign investors.

According to Palauan law, the following businesses are solely reserved for Palauan citizens:

"(i) wholesale or retail sale of goods; (ii) all land transportation including bus services, taxi services and car rentals; (iii) tour guides, fishing guides, diving guides and any other form of water transportation services; (iv) travel and tour agencies; and (v) commercial fishing for other than highly migratory species"

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- i. handicraft and gift shops;
- ii. bakeries;
- iii. bar services;
- iv. operations [selling] products being produced by wholly Palauan-owned manufacturing enterprise;
- v. equipment rentals for both land and water within the Republic, including equipment for purpose of tourism; and

- vi. any such other businesses, as the Foreign Investment Board may determine

Sectors not listed as either closed or semi-restricted are presumed to be open for foreign investment. The Foreign Investment Board may, however, amend the semi-restricted sector list for “any such other businesses as the Board may determine.”

Measure	Year	Rank or value
TI Corruption Perceptions index	2013	N/A
Heritage Foundation’s Economic Freedom index	2013	N/A
World Bank’s Doing Business Report “Ease of Doing Business”	2014	100 of 189
Global Innovation Index	2013	N/A
World Bank GNI per capita	2012	USD 9,860

2. Conversion and Transfer Policies

Other than best practices to review suspicious money transfers (e.g. money laundering), there are no restrictions on converting or transferring funds associated with an investment. Palau’s economy uses the U.S. dollar, so there are no issues in obtaining U.S. currency.

3. Expropriation and Compensation

The government of Palau has not demonstrated property-expropriation actions. The Palauan constitution provides for the right of the government to condemn land for national interest (“eminent domain”). There are no reported notable property-expropriation cases.

4. Dispute Settlement

There are no ongoing investment disputes involving the Government of Palau and foreign investors. There is currently no official “dispute resolution” procedure, apart from civil suits and other legal action. However, trained and licensed arbitrators exist, and the establishment of a privately-supported dispute arbitration system is underway. Palau’s judicial system is viewed by Transparency International and other observers as professional and fair.

There is no Uniform Commercial Code (UCC). The lack of a UCC complicates the business environment, as it difficult to obtain trustworthy information on existing titles and liens, and the scope of lender and investor rights and protections in the event of disputes can be unclear. A draft UCC is pending in the Palau legislature, but has been bottled up in committee for three years. The Asian Development Bank (ADB) has recommended adoption of UCC elements to improve Palau’s incomplete commercial legal system. Palau also has no bankruptcy law.

Palau is not a member of the Party to the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (ICSID).

5. Performance Requirements/Incentives

The Government of Palau does not apply performance requirements or incentives to domestic or foreign investors. Businesses in Palau must pay a straight 3% duty on all imported items, with no exemptions; duties are higher for alcohol and tobacco. There are no taxes on exports. Apart from two small Free Trade Zones located outside Koror, there are no “tax holidays” or other incentives offered to investors; however, taxes are low.

Per the reciprocity arrangements of the Compact of Free Association, U.S. citizens are exempt from the Government of Palau’s normal resident visa requirements. A visa is not required for U.S. citizens visiting Palau for one year or less, provided the visitor otherwise complies with applicable regulations, for example, on employment.

Palau does not offer citizenship by marriage to a Palauan, parental relationship to a Palauan, or through an established length of time as a legal resident in Palau. This prohibition on Palauan naturalization applies to all foreigners, including U.S. citizens. A foreign investor living in Palau needs to adhere to the procedures and regulations of the Foreign Investment Board.

Palau is not a member of the World Trade Organization (WTO).

6. Right to Private Ownership and Establishment

Other than the foreign-ownership restrictions for certain business sectors, there are no restrictions on private entities to engage in all forms of remunerative activity. However, establishing secure land title may be complicated due to the complexity of the traditional land ownership system and occasional over-lapping claims.

7. Protection of Property Rights

Intellectual Property: Palau is not a member of the World Intellectual Property Organization (WIPO), the WTO, or any other organization or convention protecting intellectual property rights. Pirated DVDs imported from off-island are readily available. According to Palau’s Attorney General, Palau will extend copyright protection to any resident of Palau and any offshore individual or company that registers its products in Palau, and pays the related \$200 fee (see below). Palauan copyright law explicitly covers materials in which:

1. one or more of the authors is or was on the date of first publication a national or resident of the United Nations Trust Territory of the Pacific Islands, Palau District, or the Republic of Palau;
2. the work is or was initially published in the Republic of Palau;
3. the work is or was initially published in another country and also published in the Republic of Palau within 30 days thereafter, irrespective of the nationality or residence of the author;
4. the work is an audiovisual work, the author of which is a resident of Palau; or

5. the work is an architectural work erected in the Republic of Palau or is an artistic work incorporated into a building or other structure located in Palau.

Any copyright owner who is the bona fide owner of a copyright or the owner of a transferred copyright shall be subject to the same protections provided above, provided he or she registers the work or works with the Office of the Attorney General and pays the requisite fee. The Attorney General shall charge a fee of \$200.00 per work registered, or \$2,000.00 for ten or more works registered to the same owner. For persons or businesses registering 10 or more works, additional works may be added at no charge during the same calendar year.

Land: Foreigners cannot own land in Palau, but they can own buildings that they have legally erected on leased land (e.g., prefabricated structures). Foreigners are able to lease government-owned land for lease terms of up to 99 years. In addition, foreigners are able to lease private land for up to 50 years, with an option to renew for up to an additional 49 years. Condominiums may be leased for 99 years.

The Land Court of Palau issues Certificates of Title. Portions of Palau are still un-surveyed and lack Certificates of Title. Ownership of much land remains unclear, and overlapping and contesting Warrantee Deeds and Deeds of Transfer are common in Palau. Land owned by Palau's clans is communal property and negotiating the terms for land requires the cooperation and agreement of many individuals.

8. Transparency of the Regulatory System

Regulatory and accounting systems are generally transparent and consistent with international norms. Proposed new regulations must go through a period of public comment before being adopted. Businesspeople in Palau do not report specific regulatory discrimination against foreign investors.

Regulations: A foreign investor will commonly have to submit for approval to the Foreign Investment Board (FIB), the Environmental Quality and Protection Board (EQPB), and the Historical Review.

Taxes and Fees: Palau places a 4% Gross Revenue Tax (GRT) on businesses, and allows deductions only for hiring Palauan employees and for donations to non-profit organizations. Businesses are unable to write-off business expenses or depreciation.

There is an occupancy tax on hotel rooms. Hotels with 20 or more rooms pay 12 percent or \$12 per room, whichever is larger. For hotels with less than 20 rooms, the minimum tax is \$7 per room.

Except for food, Palau charges a flat 3 percent ad valorem duty on most imports; import duties for alcohol and tobacco are higher. Immediate personal property imports (such as furniture for use in the investor's private home) are exempt from import duty. Palau also charges a fuel import tax of five cents per gallon on all imported diesel and gasoline.

9. Efficient Capital Markets and Portfolio Investment

Palau has a strong banking sector with three FDIC-insured U.S. banks as the foundation: the Bank of Hawaii, the Bank of the Pacific, and the Bank of Guam. The IMF has also praised

Palau's healthy and efficient banking sector. Total assets of these banks exceed \$125 million. There is no stock exchange in Palau.

10. Competition from State-Owned Enterprises

The state-owned enterprises in Palau include the utilities sector, telecommunications, and the national bank. As noted above, due to growing pressure on local infrastructure and encouragement from the Asian Development Bank (ADB) and others, some of these companies may be wholly or partially privatized in the future. There is a state-managed giant clam farming company, but this is not a barrier to private clam-farming initiatives.

11. Corporate Social Responsibility

Many businesses provide corporate donations to environmental and social Non-Governmental Organizations (NGOs), and /or engage in environmental corporate social responsibility programs to preserve Palau's environment and wildlife. Most CSR activities are conducted via donation, partly attributable to the available tax deduction of up to 10 percent of a company's Gross Revenue for donations to non-profit organizations. Apart from this tax incentive, there are few laws or regulations pertaining to CSR.

12. Political Violence

Palau experienced some political violence in the 1980's and early 1990's, but has become increasingly stable and peaceful since then. The World Bank placed Palau in the 98th percentile in its 2011 rating of country political stability.

13. Corruption

Palau acceded to the United Nations Convention Against Corruption (UNCAC) in March, 2009. It has been a member of the Asian Pacific Group on Money Laundering (APGML) since 2002. Palau's legal system is based on common law (as understood and applied in the United States) and customary laws. Its criminal bribery offences have not been externally reviewed. The Code of Ethics Act spells out what is illegal for government officials, and the Public Auditor and the Special Prosecutor hold them accountable for failure to observe the law.

Palau is currently the only one of the Micronesian nations to employ a Special Prosecutor; however this position has been vacant since 2010. Prior to this vacancy, successive Special Prosecutors successfully prosecuted a large number of elected Federal and State officials, recovering substantial sums of money. Most corruption (proved and alleged) involves improper use of government funds or property, and/or fraudulent collaborations of various kinds. Even without a sitting special prosecutor, there have been several high profile prosecutions/resignations by public officials related to violations of Palau's government ethics law. None involved alleged abuse targeting foreign investors. Government extortion or semi-extortion of private companies is virtually unknown.

Local media often reports on alleged corruption cases, and serves as an informal watchdog. Palau does not appear in Transparency International's Index of Corruption (which includes ratings of 184 countries). However, in a 2004 country report, Transparency International

praised the fairness and professionalism of Palau's judiciary. There are no formal anti-corruption NGOs or international watchdogs based in Palau.

Palau is not a member of the OECD Convention on Combating Bribery.

14. Bilateral Investment Agreements

Palau has no bilateral investment protection agreements, and is not a member of any free trade associations. Palau is currently negotiating with both the Philippines on a bilateral cooperation agreement and the European Union on a free trade and economic agreement.

15. OPIC and Other Investment Programs

The Overseas Private Investment Corporation (OPIC) has had an investment incentive agreement with Palau since March 15, 2002. Palau is a member of the Multilateral Investment Guarantee Agency of the World Bank Group.

16. Labor

With an estimated total of 14,000 Palauan nationals in country (including non-working individuals, such as children and elderly) and 4,000 estimated foreign workers, foreign labor comprises a large proportion of Palau's labor force. In July 2011, the U.S. Interior Department provided a grant to Palau for development of a comprehensive Labor Code.

In October 2013, Palau established the minimum wage for workers at USD \$2.75/hour with \$0.25 increases slated for future years until it reaches \$3.50/hour in 2016, though certain categories of workers are exempted from the minimum wage. Business owners must pay a tax of \$500 per foreign employee per year.

Palau is not a member of the International Labor Organization (ILO).

17. Foreign Trade Zones/Free Ports

The Free Trade Zone Act of 2003 established the Ngardmau Free Trade Zone Authority. Another "Tax Free Zone" has recently been established in the state of Melekeok, covering a one mile radius around the Federal capitol building. These zones, still largely undeveloped, offer potential investors tax and other incentives, but ownership and labor rules are the same as elsewhere in Palau.

18. Foreign Direct Investment Statistics

Foreign Direct Investment statistics are not readily available. Neither the Palau Bureau of Budget and Planning, nor the Foreign Investment Board track FDI after the initial FIAC is approved. There are currently 172 companies listed by the Foreign Investment Board as having FIACs.

Section 5 - Government

Chiefs of State and Cabinet Members:

For the current list of Chief of State and Cabinet Members, please access the following - [Central Intelligence Agency online directory of Chiefs of State and Cabinet Members of Foreign Governments](#)

Legal system:

Mixed legal system of civil, common, and customary law

International organization participation:

ACP, ADB, AOSIS, FAO, IAEA, IBRD, ICAO, ICRM, IDA, IFC, IFRC, ILO, IMF, IMO, IMSO, IOC, IPU, MIGA, OPCW, PIF, Sparteca, SPC, UN, UNAMID, UNCTAD, UNESCO, WHO

Section 6 - Tax

Exchange control

For more information - <http://www.palau.gov.net/>

Treaty and non-treaty withholding tax rates

For more information - <http://www.palau.gov.net/>

Methodology and Sources

Section 1 - General Background Report and Map

(Source: [CIA World Factbook](#))

Section 2 - Anti – Money Laundering / Terrorist Financing

	Lower Risk	Medium Risk	Higher Risk
FATF List of Countries identified with strategic AML deficiencies	Not Listed	AML Deficient but Committed	High Risk
Compliance with FATF 40 + 9 recommendations	>69% Compliant or Fully Compliant	35 – 69% Compliant or Fully Compliant	<35% Compliant or Fully Compliant
US Dept of State Money Laundering assessment (INCSR)	Monitored	Concern	Primary Concern
INCSR - Weakness in Government Legislation	<2	2-4	5-20
US Sec of State supporter of / Safe Haven for International Terrorism	No	Safe Haven for Terrorism	State Supporter of Terrorism
EU White list equivalent jurisdictions	Yes		No
International Sanctions UN Sanctions / US Sanctions / EU Sanctions	None	Arab League / Other	UN , EU or US
Corruption Index (Transparency International) Control of corruption (WGI) Global Advice Network	>69%	35 – 69%	<35%
World government Indicators (Average)	>69%	35 – 69%	<35%
Failed States Index (Average)	>69%	35 – 69%	<35%
Offshore Finance Centre	No		Yes

Section 3 - Economy

General Information on the current economic climate in the country and information on imports, exports, main industries and trading partners.

(Source: [CIA World Factbook](#))

Section 4 - Foreign Investment

Information on the openness of foreign investment into the country and the foreign investment markets.

(Source: [US State Department](#))

Section 5 - Government

Names of Government Ministers and general information on political matters.

(Source: [CIA World Factbook](#) / <https://www.cia.gov/library/publications/world-leaders-1/index.html>)

Section 6 - Tax

Information on Tax Information Exchange Agreements entered into, Double Tax Agreements and Exchange Controls.

(Sources: [OECD Global Forum on Transparency and Exchange of Information for Tax Purposes](#) [PKF International](#))

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