**UNITED STATES**
**DEPARTMENT OF THE INTERIOR**
**OFFICE OF INSULAR AFFAIRS**

# A Private Sector Assessment for The U.S. Virgin Islands

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## 2006 Island Fellows

Prepared by:
Michael Ralles
Krystal-Lee Tabangcura

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This document has been prepared by MBA students to assess the business climate in The U.S. Virgin Islands for the purposes of the 2006 Island Fellows Program. The views and recommendations contained in this document are solely those of its authors and not the U.S. Government or any agency or officer thereof.

Questions and comments related to this report should be addressed to:

Ms. Angela Williams
Office of Insular Affairs
US Dept of the Interior
1849 C Street, N.W.
Mail Stop 4311A
Washington, D.C. 20240

Michael Ralles is pursuing a Masters of International Relations with a concentration in Development Finance at the John's Hopkins School of Advanced International Studies (SAIS) and a Masters of Business Administration from the Robert Emmett McDonough School of Business at Georgetown University, both in Washington, D.C. He also holds a Bachelor's Degree in Economics and International Studies from Northwestern University in Evanston, IL. Prior to graduate school, he worked as a management consultant for the Zyman Group and Inforte Corporation. In 2004, Mike served as a consultant in Mozambique to ACDI/VOCA, a U.S. NGO funded by the U.S. Agency for International Development.

Krystal-Lee K. Tabangcura is a joint J.D./M.B.A. candidate at the University of Hawaii William S. Richardson School of Law and the College of Business Administration. She graduated from the University of Miami with a B.B.A . in Business Management and Organization.

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# I. Forward

This report is designed to be helpful to the policymakers of the U.S. Virgin Islands who are looking for ways to make their islands more hospitable for private sector economic development. We don't pretend to have all of the answers; we're just trying to make a constructive contribution to the conversation. This report analyzes policy from the perspective of impact on the business climate. We realize that policymakers don't have the luxury of examining policy from that perspective alone, and that social and political factors also have to be taken into account. We believe that it would be presumptuous of us to try to evaluate local policies from a social or political perspective, and respect the prerogative of local leaders to perform that analysis.

We would like the readers of this report to keep a couple of important things in mind. First, this report is designed to focus on areas where the business climate might be improved. The report may therefore appear to present a more negative picture of the business climate in the territory than is warranted. While the U.S. territories are not perfect, their business climates are arguably much better than those in the many developing economies that routinely attract outside investment. All of the territories benefit from the protection of the U.S. flag and the U.S. legal system, duty-free access to the U.S. market, safety (including U.S. military protection), U.S. financial support, use of the U.S. dollar, an English-speaking workforce that is well trained by the standards of the developing world and infrastructure that is good by the standards of the developing world. Each of the territories has its own particular competitive advantages as well.

The reader should also keep in mind that this report is based upon conditions as we found them in the summer of 2006. It is always possible that subsequent events could have a significant impact on how one might analyze the business climates of the territories.

This report was created by two MBA students and reviewed and edited by the staff of the Office of Insular Affairs. We therefore consider the report to be a product of OIA. It is offered with the greatest humility out of the desire to be of service. We recognize that the future of the territory belongs to the people of the islands, and that the role of the Federal Government is to provide our best information and analysis to help island leaders make informed decisions about their future. We hope that this report will be put to good use, and will help the people of the islands navigate their way to a strong, prosperous future.

*David B. Cohen*
*Deputy Assistant Secretary of the Interior*
*Washington, D.C.*
*December 2006*

# II. Introduction and Methodology

## A. General Background[1]

The U. S. Virgin Islands (USVI), an unincorporated territory of the United States, was purchased from Denmark by the U.S. in 1917 for US$2.5 million. Located between the Caribbean Sea and the North Atlantic Ocean, the territory is in close proximity to the continental U.S. and the eastern region of Puerto Rico. The Virgin Islands *(68 cays and islands)* is comprised of three main islands: St. Thomas, St. John, and St. Croix. Each island is geographically and economically distinct. Collectively, the Virgin Islands measures approximately 136 square miles with St. Thomas and St. John located 3 miles apart and St. Croix situated 40 miles to the South of St. Thomas. Some of the world's best ecological and historical sites are found in the Virgin Islands, and the islands are rich in colonial history and Caribbean cultures.


Source: https://www.cia.gov/cia/publications/factbook/geos/vq.html

### *1. St. Thomas*

St. Thomas, an island of 32 square miles in area, is home to the territory's capital, Charlotte Amalie, and an estimated population of 52,838 persons. Historically, St. Thomas thrived as a trading post for European ships passing through the Caribbean. The island has one of the best natural deepwater harbors in the Caribbean and is strategically located along the Anegada Passage, a key route for ships bound for the Panama Canal. During the 1960s St. Thomas became a popular tourist destination for U.S. mainlanders and Europeans; today, St. Thomas still remains the center of tourism for the Virgin Islands, with a reported 818 cruise ship calls in 2005. In 2005, visitor arrivals totaled 2,605,100, of which, a majority 1,912,500 were cruise tourists.[2]

### *2. St. John[3]*

Home to an estimated 4,333 people, St. John is a small island measuring 20 square miles in area. Two-thirds of St. John is covered by a national park, and boasts developed underwater and eco-tourism industries. St. John's economy is predominantly dependent on tourism. With St. Thomas only three miles away, St. John attracts day excursionist as well as high-end vacationers with luxury hotels and vacation homes. Due to its relative

[1] Wedderburn, Monique. (2005). United States Virgin Islands Business Opportunities Report. Office of Insular Affaris, U.S. Department of the Interior, Washington, DC.
[2] USVI Bureau of Economic Research 2005 Annual Economic Indicators
[3] Chow, Emily. (2003). *Investment Program Report for the U.S. Virgin Islands*. Office of Insular Affairs. U.S. Department of the Interior. Washington, DC.

size and proximity to St. Thomas, St. John is often aggregated with St. Thomas in promotions and policy matters.

#### *3. St. Croix*

St. Croix, an island of 84 square miles in area, is the largest of the three inhabited islands and home to an estimated 54,957 persons. Prior to the 1960's, St. Croix's economy depended solely upon sugar cane cultivation. In the 1960's the island economic structure diversified into manufacturing and tourism. Today, St. Croix's economy is predominantly manufacturing based, and largely dependent on petroleum and rum exports. Hovensa, the largest petroleum refinery in the western hemisphere, is a joint partnership between Amerada Hess and PDVSA, Venezuela's national oil company. In 2003, Hovensa employed over 1,600 workers and shipped US$4.8 billion of refined petroleum products to the United States. Virgin Islands Rum Industries Ltd., also located on St. Croix, is a top exporter of Cruzan, Old St. Croix and bulk rum to the mainland U.S.

#### *4. Government*

The Government of the U.S. Virgin Islands is comprised of three branches, executive, legislative and judicial branches. The executive branch is headed by an elected Governor, with a lieutenant governor and appointed department heads. The legislative branch encompasses a unicameral 15-member Legislature. The judicial branch is headed by the Superior Court of the Virgin Islands. The Federal Government maintains a U.S. District Court in the Virgin Islands and appeals of both federal and local courts are heard by the U.S. Court of Appeals for the Third Circuit in Philadelphia.[4]

The current governor, Charles W. Turnbull was elected in 1998. The term of office for the Governor of the Virgin Islands is four years; governors can serve up to two terms.

### B. Methodology

This analysis of the business climate in the U.S. Virgin Islands (USVI) was completed by two MBA students during the summer of 2006 and it is based on their interviews, research and observations. Initially, the Fellows trained with Dr. Paul Holden of the Enterprise Research Institute (ERI). Following their training, the Fellows employed the ERI methodology to assess the USVI private sector in eight specific areas:

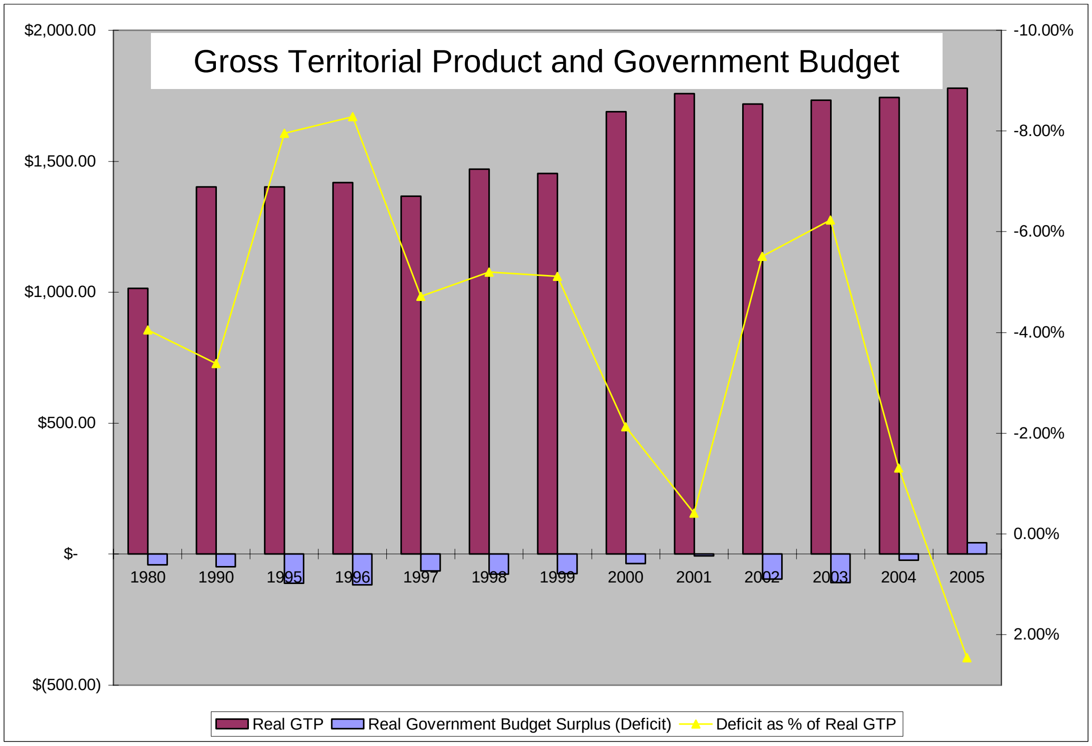
[4] Virgin Islands Public Finance Authority: Presentation to National Federation of Municipal Analysts, April 2005.

- Transparency
- Labor
- Taxation
- Legal system
- Infrastructure
- Land
- Business Practices
- Financial Infrastructure

The Fellows traveled to the USVI and met with over 45 leaders from the public, private and not for profit sectors on the islands of St. Thomas and St. Croix, focusing on government officials charged with creating a business-friendly environment and businesspeople operating in the USVI business environment on a daily basis. The Fellows gathered and reviewed information from primary sources as well as existing independent research into business practices in the USVI, to develop a cohesive view of the USVI economy and to identify some possible alternatives that could help drive future business growth.

After one month in the USVI, the Fellows returned to the Department of the Interior, Office of Insular Affairs in Washington, D.C. to review their research and complete a comprehensive assessment of the business climate in the USVI. The Fellows worked in conjunction with their counterparts in the program who had been following a similar process in the territories of American Samoa and Guam and the Commonwealth of the Northern Mariana Islands. For each of the eight subject areas outlined above, the Fellows developed relevant policy alternatives that the government of the USVI could explore as it continues to work to help spur business growth in the territory. The set of policy priorities were categorized according to relevance to the business climate in the USVI and feasibility. This document provides a detailed discussion of the policy alternatives which, in the view of the authors of this report, have the greatest potential for positive impact on the business climate in the USVI.

## C. Economic Background and Comparative Data




The economy of the USVI has been in the midst of a modest expansion for the past several years. In real terms, the Gross Territorial Product (GTP) has risen every year since 2002, and the territory has seen real GTP grow by 22% since 1999. Since 1980, the government of the USVI has consistently operated with a fiscal deficit, but in 2005, for the first time the government of the USVI realized a surplus. The improvement of the government budget system have been linked in large part to several specific efforts of the current USVI administration:

| Date | Action[5] |
|---|---|
| 1999 | **New cost cutting measures implemented, including:**<br>**• 5% reduction in payroll for FY 2000**<br>**• Hiring freeze**<br>**• 50% reduction in baseline overtime payroll costs** |
| 2000 | **Completed a Five Year Operating and Strategic Financial Plan** |
| 2001 | **Number of government employees reduced by 9%, with reductions maintained through 2004** |
| 2001 | **Entire balance of Hurricane Hugo Community Disaster Loan cancelled** |
| 2003 | **New hardware and software systems implemented to increase tax compliance** |
| 2004 | **Entire balance of Hurricane Marilyn Community Disaster Loan cancelled** |
| **2005** | **Government implemented an additional 2% reduction in personnel-related costs** |

These policies led to a reduction in the territorial budget deficit as a percentage of GDP until 2001. Following the September 11 attacks, the USVI experienced a downturn in

[5] Virgin Islands Public Finance Authority: Presentation to National Federation of Municipal Analysts, April 2005.

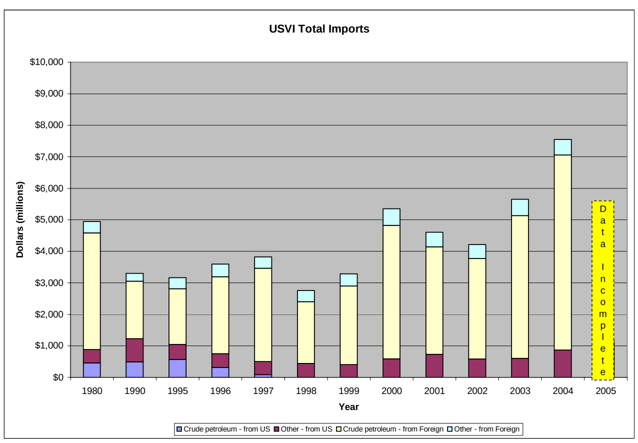
tourism which led to an increase in the budget deficit unrelated to expenditures, and since 2003 the fiscal position of the government has continued to improve, culminating in the surplus in 2005.

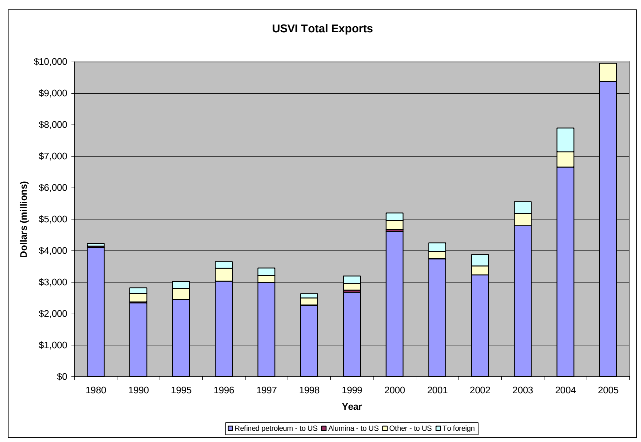
The economy of the USVI is largely concentrated in a handful of industries. Tourism is clearly the leading sector of the economy, representing 60 to 80 percent of GTP, depending on which specific industries are included in the definition of tourism. The next largest sector of the USVI economy is manufacturing, primarily refined petroleum products and rum from St. Croix. Watch-making, agriculture and construction also play a role in the USVI economy, but to a much smaller extent.[6]

While tourism is and will continue to be a very important component of the USVI economy, any movement to diversify the local economy would likely be favorable for the long-term economic health of the territory. Tourism is by its very nature subject to random external shocks that the recipient economy cannot control. Such events as hurricanes or the September 11 attacks tend to rapidly and demonstrably reduce the size of tourism revenues. This is not to say that the tourism industry should be neglected; rather, in addition to working to continue the long-term strength of that industry, exploring new, alternative industries to increase diversification in the economy may be beneficial. The USVI government has recognized this, and has been taking steps to diversify its economy into new areas.

A great deal of USVI economic activity revolves around importing raw petroleum from outside the U.S. and exporting refined petroleum to the U.S. With the Western Hemisphere's largest petroleum refinery in the territory, this activity is not surprising. For the year 2004, total exports to the U.S. represented over 90% of all USVI exports while imports from foreign countries represented 89% of total imports.

Source: USVI Bureau of Economic Research 2005 Annual Economic Indicators




Exports from the territory to countries other than the U.S. represent a very small proportion of total exports. Almost all foreign trade takes place within the region and is largely composed of refined petroleum. While the destination of petroleum within the

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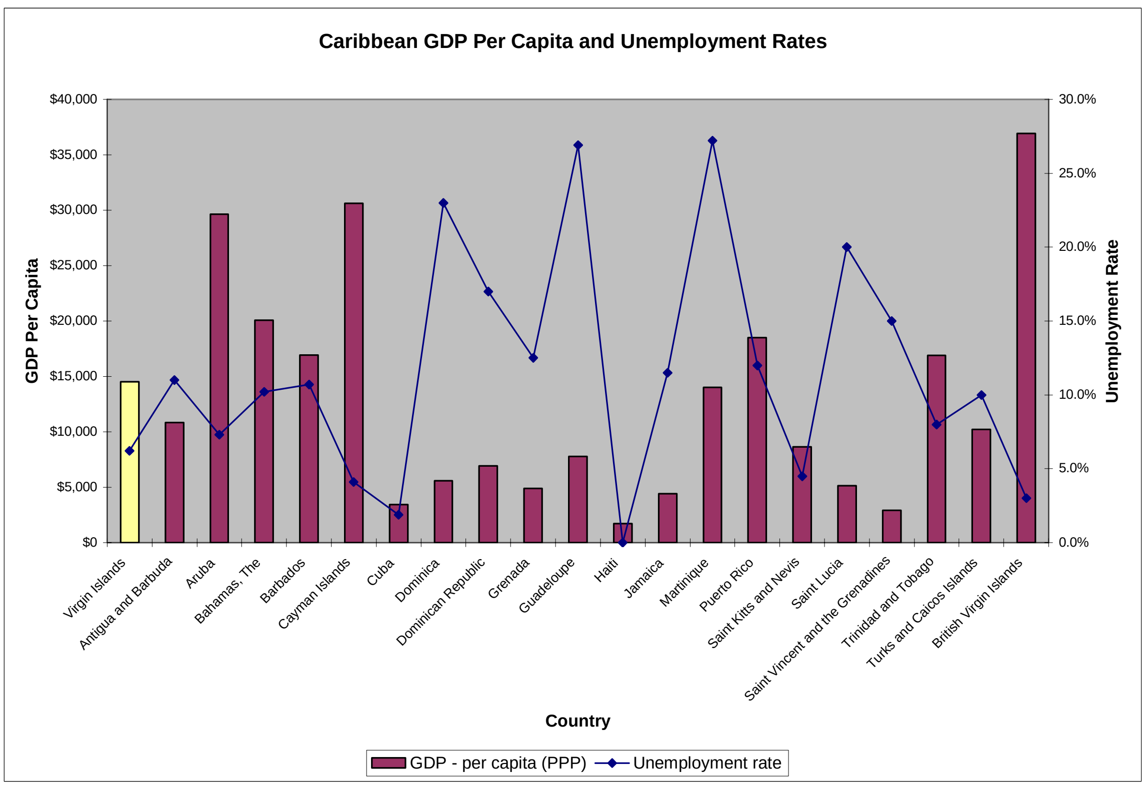
[6] Mills, Lauritz. U.S. Virgin Islands Economic Review and Industry Outlook. Bureau of Economic Research (BER): August 2005.

regions does vary by year, the trend towards exporting principally within the region remains. The ten largest non-U.S. trading partners in 2005 were:

| Rank | Country | 2002 $M | 2003 $M | 2004 $M | 2005 $M[7] |
|---|---|---|---|---|---|
| 1 | United Kingdom (including British Virgin Islands) | 0 | 0 | 3 | 114 |
| 2 | Netherlands Antilles | 60 | 49 | 77 | 104 |
| 3 | Canada | 6 | 0 | 1 | 63 |
| 4 | Korea, South | 11 | 35 | 98 | 60 |
| 5 | Bahamas | 38 | 36 | 9 | 36 |
| 6 | St. Lucia | 12 | 15 | 21 | 30 |
| 7 | Venezuela | 9 | 10 | 8 | 26 |
| 8 | Netherlands | 2 | 12 | 2 | 22 |
| 9 | Dominican Republic | 6 | 9 | 18 | 21 |
| 10 | Bermuda | 8 | 6 | 7 | 7 |

In comparison to other nations in the Caribbean, the USVI exhibits roughly average per capita GDP and unemployment rates. Additional comparative data across the Caribbean can be found in Appendix 1: Select Caribbean Comparative Data.




Compared with other U.S. territories, the USVI has already done much to enable growth and provide a stable, open business environment. The Fellows did identify some possible alternatives that the USVI government could consider as it continues its efforts

[7] U.S. Census Bureau. Foreign Trade Statistics. "State Exports for Virgin Islands." Last modified: 28 February 2006

to improve the local business environment, particularly in transparency of certain procedures, labor and tax policies. These three areas seemed to offer the greatest number of alternatives that could be considered to further enhance the USVI's growing economy.

# III. Transparency

Government expenditure represents one of the single largest areas of the economy in the USVI. From 2000 to 2005, the territorial operating budget consumed an average of twenty-two percent of gross territorial product.[8] There remains some uncertainty about the processes governing the expenditure of these funds; in certain extreme instances, some businesspeople believe it may not always in the best interests of the community at large. These perceptions, true or not, can be quite damaging the the USVI's image as a favorable location for doing business, and the USVI government may want to consider alternatives that would increase the level of transparency in government administration, which would help neutralize these perceptions.

## A. Procurement Process Transparency

The USVI has made significant and recognized strides in making the government procurement process more transparent over recent years, but perceptions that it is still too politicized persist in too many cases. The lack of a clear, universally applied procurement process tends to reinforce the perception that dishonest government officials may be able to channel contracts to their associates, rather than the lowest cost, most qualified provider.

In 1999, the government recognized the need to develop a "major policy for implementing competitive procurement to the maximum extent possible for its requirements for goods and services"; the same report recommended that "there is a need for strengthening the capacity of the Department of Property and Procurement (DP&P)."[9] At this time of this Assessment, however, some of the basic tools that are used to ensure the transparency of these processes were not available; the web page for DP&P was unavailable, and almost all senate bills and publications relating to the administration of this agency were also down. A search for the DP&P web page does indicate that a page did once exist, on the usvi.org domain, but is no longer available. As of August 4, 2006 the DP&P reported only one open request for proposal (RFP), and had no capability for listing RFPs on the internet. DP&P also refers potential bidders to the local USVI newspapers, where several additional invitations for bids are listed, but there does not seem to be a clear process for posting and taking down public notices.

The perceptions of a lack of transparency in the local procurement process have not been helped by information coming out of a recent court case in the territory. A scheme to create false companies, fraudulently receive government contracts, perform little or no work, and pay cash kickbacks to government officials was exposed by the local newspaper, and prosecuted in the local courts.[10] While this is an extreme example and is in no way representative of the day to day practices of the USVI government, it does reinforce outside perceptions of these practices.

Currently in the USVI, the procurement process is principally a manual process managed by the DP&P offline. Chapter 23, Title 31 of the USVI Code provides:

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[8] USVI Bureau of Economic Research 2005 Annual Economic Indicators
[9] 1999 USVI Five Year Operating and Strategic Financial Plan
[10] Fields, Tim and Megan Poinski. "Contracts rife with corruption, federal investigators allege." Virgin Islands Daily News 6/22/06: A1.

> The Commissioner of Property and Procurement shall solicit sealed bids from all responsible prospective suppliers or purchasers who have requested their names to be added to the bidders' list, by sending them such notices as will acquaint them with the proposed purchase or sale. All pending purchases or sales shall also be advertised by a notice posted on a public bulletin board in the Department of Property and Procurement.[11]

#### 1. Option for Consideration: Update Virgin Islands Code to stress the importance of transparent, online procurement procedures.

The National Association of State Purchasing Officials has recommended that states adopt a system of electronic bidding via the internet to reach a larger pool of bidders and thus increase competition for high-quality goods and services. The state of Oregon has been utilizing an online bidding system since 1992, and estimates savings of $1.3 million in paper and personnel costs on top of roughly $33 million in direct cost savings due to increased competition from bidders.[12] Since the code of the USVI neither mandates nor advocates this type of online procurement system, there is little mandate for the DP&P to pursue such advancements. The USVI could consider pursuing an update of the code to mandate the use of an online procurement process, or explore options within the administration for making such changes through executive action..

#### 2. Option for Consideration: Increase funding for DP&P process improvements and monitor results to quantify potential costs or savings.

As was recognized in 1999, DP&P will likely need additional resources to effectively implement an improved procurement system. The USVI does not necessarily need to implement an expensive online system all at once; a staged conversion process has also been used elsewhere, beginning with (for example) the posting of bidding procedures online, and setting a website that is updated frequently with all open government RFPs. Incremental improvement of the DP&P system could be mapped against a recognized best-in-class procurement system, and steady progress towards implementation of this system could be maintained. Such systems do exist, so there are several proven options that the USVI could consider, further reducing potential costs.

### B. Policy Transparency

The Fellows discovered a perception that the public availability of government information in the USVI was sporadic, with some agencies offering a great deal of information and others offering very little. Relatively few government agencies maintain an active internet presence. The government primarily operates websites under two domains, “usvi.org” and “gov.vi.” Currently, many (but not all) of the sites under the gov.vi domain are available, but all websites under the USVI.org domain are out of service. A simple internet search yielded countless cached government documents (i.e., documents which were once published and made available online but which are no longer posted on government websites), policies, and administrative departments which can no longer be accessed online.

If a significant proportion of information normally sought by business and the general public is either not available at all or not easily accessible, this can create some

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[11] 31 VIC § 236

[12] National Association of State Purchasing Officials whitepaper: Buying Smart: State Procurement Saves Million. http://www.naspo.org/whitepapers/buyingsmart.cfm

inefficiencies in the local business climate.. This leads users of government services to experience significant delays in completing transactions with the government, or researching government effectiveness, which creates an opportunity cost in time lost researching necessary information prior to investment, to say nothing of the potential public interest concerns.

***1. Option for Consideration: Develop a comprehensive information technology strategy which enables the timely distribution of government publications and policy documents.***

The USVI established a Bureau of Information Technology (BIT) in 2003. Recently, the Legislature created and filled the position of director and tasked the agency with developing a five year technology plan for the territory. There are many issues for this new agency to consider when developing this plan; the policy implications of its recommendations would be significant, particularly if it included a cohesive web presence strategy for the USVI government, or recommendations regarding active web delivery of all government content. While many of the BIT priorities currently lie in the area of back-end systems connecting various government agencies and emergency preparedness, the agency could go a long way towards fulfilling its mandate if it also worked to develop content delivery vehicles via the internet. These tools, by making information available and easily accessible, would also help neutralize perceptions regarding any lack of transparency in government operations.

While the BIT is over three years old, there are still some issues outstanding over its structure. Many of its employees are listed as "exempt" rather than "classified," which may reduce the flexibility of the Director to control staffing. This flexibility can be critical in the implementation of a mandate as complex as that assigned to the BIT, and as such the USVI may also want to explore options to increase the flexibility allowed to BIT.

## C. Comprehensive Economic Planning

Economic planning currently takes place across several government agencies in the USVI, which necessarily makes coordination important. There were reported instances of government investment-development initiatives that ran directly counter to one another, particularly on St. Croix. Coordination of interagency effort is hardly a challenge limited to the USVI, and is always a targeted area for improvement all the way up to the Federal level. Any lack of coordination may lead to different government departments working towards divergent policy objectives, and ultimately to inefficient uses of existing resources, which can be felt most acutely in smaller communities like the territories. Private sector activity is often influenced by government policy, and thus a cohesive economic development planning function is always important to allow government agencies to work together to drive a unified policy.

***1. Option for Consideration: Designate a single government agency or interagency group for coordination of all economic planning activities and ensure that all other government agencies use the products of these activities as they formulate department-specific strategies.***

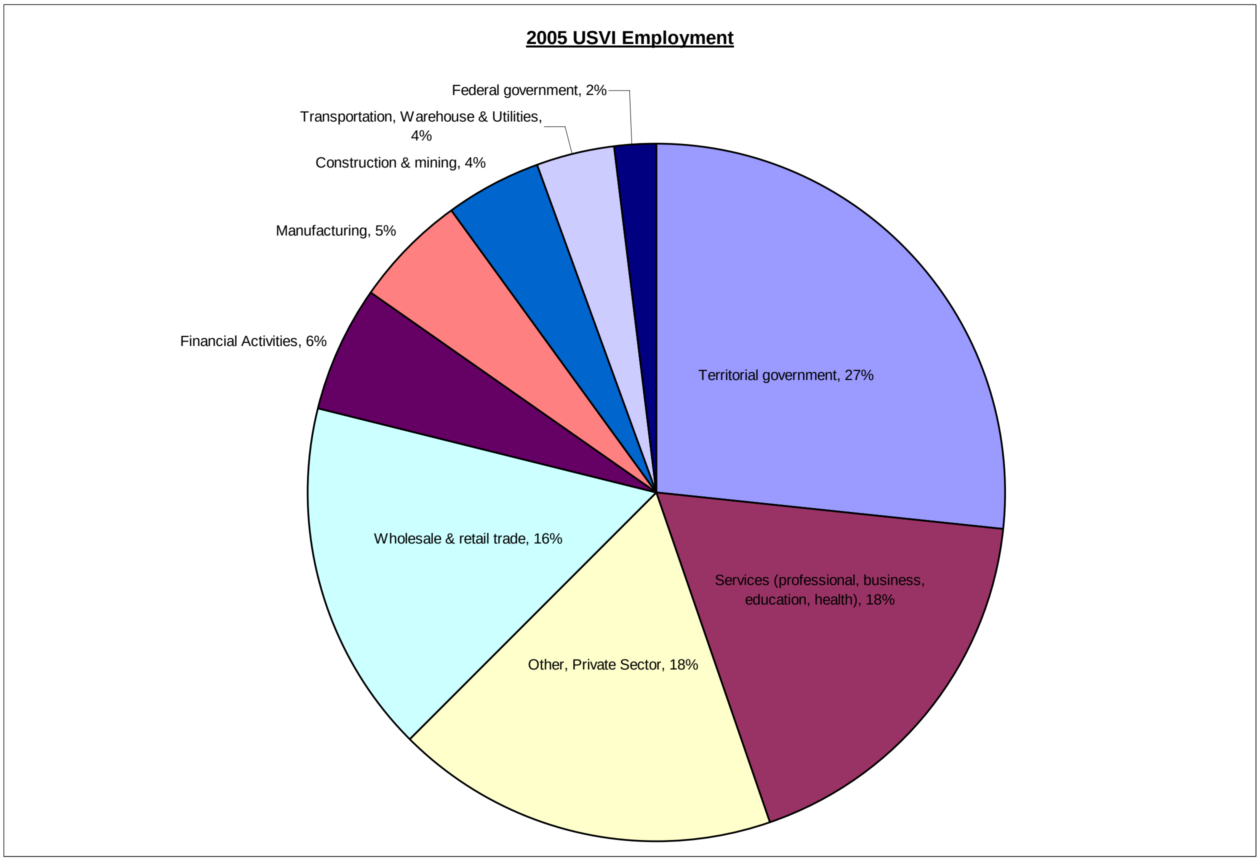
The USVI has been quite successful in its efforts to sustain an open, market-based economy that is flexible and responsive to changes in the local and global economic environment. It is exploring development opportunities to diversify its economy beyond the tourism industry into a number of high demand industries in which the USVI maintains a comparative advantage. Empirical research across the world has shown that the development of clusters – critical masses, in one place, of unusual competitive success in particular fields – can and do lead to greater economic prosperity.[13]

It is not necessarily the role of government to define up front the fields that will drive growth; rather, planning can center around establishing sensing and responding mechanisms to help cultivate growth through government policy in the industries where growth potential and comparative advantage are thought to be strongest. One especially potent tool for cultivating growth is the Economic Development Commission or EDC (see Taxation chapter). The government currently extends EDC benefits to particular industries, and may be able to enhance growth by explicitly aligning those targeted industries with strategic growth industries identified by its planning agencies; further coordination between those agencies could only improve the effectiveness and potency of that tool.

[13] Porter, Michael E. "Clusters and the new economics of competition." Harvard Business Review. Nov-Dec 1999: p. 77-90.

# IV. Labor

The USVI labor force included approximately 50,906 individuals in the year 2005 – roughly 45 percent of the total population of the territory. Of those in the labor force, 3,605 (7.1%) were unemployed, and 4,469 (8.8%) worked in agriculture. Non-agricultural public and private sector employment in 2005 was spread across a number of industries, as shown in the table below:




Discussions with private sector employers in the USVI brought to light a general belief that the territory suffers from a significant lack of labor suitable for employment across the private sector. Employers particularly mentioned that they are unable to source labor locally, for jobs ranging from basic customer service positions to high level professional employees. Although the unemployment rate in the USVI remains relatively high (6.8% to 9.4% over the years 2000 to 2005), many employers are reported importing employees to fill local positions.

According to 2000 census data, only 16.9% of USVI residents age 25 or older have attained a bachelor's degree or higher, compared with a U.S. national average of 26.5%. When comparing post-secondary attainment in the USVI with other Caribbean nations, the USVI scores relatively well, with only Puerto Rico showing a higher proportion of educational attainment (see chart). While these figures appear to be encouraging for the USVI, one must consider the economic development goals of each of these nations. Since the economy of most other Caribbean islands is focused on tourism, a highly educated workforce is not of critical importance – more important factors relate to customer service skills. However, as the USVI government continues to work to diversify the territory's economy and expand economic growth into other non tourism sectors, improvements in educational attainment – and thus, the technical and other skills of the local labor pool - will go a long way to improving the attractiveness of the USVI.

| Country | Post-Secondary Educational Attainment (% of pop over 25) [14] |
|---|---|
| Puerto Rico | 33.80% |
| U.S. Virgin Islands | 16.90% |
| Cuba | 11.50% |
| Dominican Republic | 11.40% |
| Barbados | 10.00% |
| Trinidad and Tobago | 4.00% |
| Jamaica | 3.70% |
| Haiti | 0.90% |

The need for labor importation or high up-front training costs can discourage investment, as employers tend to forego projects that would necessarily be labor-intensive. The cost of unemployment or underemployment is high for individuals in the USVI as their incomes fall and they are unable to maintain their standard of living.

Education of the USVI labor force therefore is a very important consideration, which the local government has emphasized. The pursuit of generic educational goals alone, however, does not guarantee that individual members of the workforce will develop the skills and training necessary for specific job opportunities. There are several alternatives that the USVI government could consider to both improve the current efficiency of labor allocation towards available positions and to develop a long-term ability to groom workers for high–demand, skill-specific areas, including development of a system of tracking and sharing information on available jobs.

### A. Vocational Information

The USVI Department of Labor currently operates a relatively basic job board to help facilitate connections between job searchers and employers. This service is of undeniable importance in the USVI, where unemployment levels are relatively high even though the demand for labor is high. The effectiveness of the system could be increased if more robust functionality were built into the system; increased publicity might also turn the site into a virtual central clearinghouse for job postings in the USVI. There is a variety of already proven systems, which will allow the Department of Labor to select a particularly cost-effective package with a variety of new functionalities, such as searching capabilities or the capacity to view job opportunities which have been posted and filled in the past.

#### *1. Option for Consideration: Develop a comprehensive job board, including statistics tracking over the long-term.*

The use of technology to enable better allocation of human capital to available job opportunities would likely serve to boost local employment and encourage business

[14] Higher Education in Developing Countries: Peril and Promise. A report of the Independent Task Force on Higher Education and Society. Published for the Task Force on Higher Education and Society by the World Bank in February 2000.

investment in the USVI through improved access to the labor pool. The key to successful long term implementation, however, would rest in aggregating data about specific jobs, skill requirements, salary ranges, etc. and using that data to inform local residents, particularly high school and college students about to enter the labor force, about the likely opportunities that will exist Over time, this would likely lead to a good alignment between job requirements and labor pool skills.

### B. Community links for repatriation

Another significant issue facing the labor force in the USVI is a "brain drain" in which workers with certain skill sets migrate out of the territory to pursue professional opportunities elsewhere. This phenomenon is a function of both the lack of suitable jobs in the territory as well as allocation failures (i.e., difficulties in appropriately matching employers and potential employees). As a result, the highest quality workers do not contribute directly to the VI economy, and businesses must invest significantly in labor development or importation, further reducing direct demand for local labor. This can become a self-perpetuating cycle, as more students choose to go to college on the mainland and do not return, and local firms in turn cannot find qualified employees in the territory and hence import employees from elsewhere.

#### *1. Option for Consideration: Develop an online system of community engagement for workers who have left the territory.*

Many of the individuals who have migrated out of the territory to pursue professional opportunities would likely be glad to return if they were aware of comparable job options at home. To help facilitate communication, the government of the USVI could consider building a comprehensive database of workers who have left and target those expatriates with information on high quality job opportunities that arise. This system could provide an incentive for workers who have left the territory to join the online community by enabling them to connect on a substantive basis with their friends and family who remain in the territory.

Initially, this service would facilitate communication and a greater sense of connection to the territory. All users would be required to register with their contact information, educational background, skills and industry experience. Once this data about workers has been captured, specific job opportunities could be channeled to the appropriate non-resident citizens in order to encourage a return to the territory. Such a shift would also likely increase investor confidence in the local labor pool, further improving the USVI's existing competitive advantages.

### C. Public Sector Retrenchment

As of 2005, territorial government employment accounted for roughly 22% of the total workforce (see chart below).[15] Compared with an average in Latin American and the Caribbean of 3.9%, or a global average of 4.7%, this is a very high proportion of the population employed in the public sector.[16] Even when compared against other

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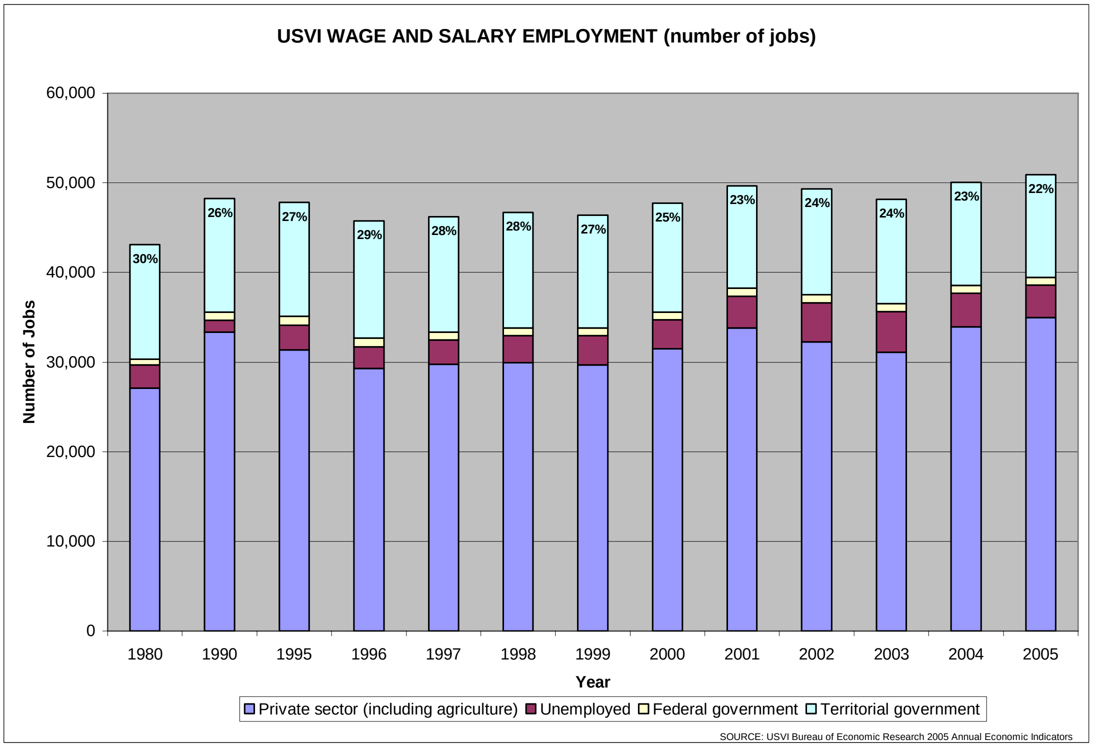
[15] USVI Bureau of Economic Research 2005 Annual Economic Indicators

[16] Schiavo-Campo, Salvatore, Giulio de Tommaso, and Amitabha Mukherjee. "Government Employment And Pay In Global Perspective." World Bank Public Sector Management and Information Technology Team

Caribbean areas, such as the Bahamas and Barbados (which have 6.4% and 6.7% of the workforce employed in public sector jobs, respectively), we see that the USVI maintains a very high ratio of public to private sector employment.[17] Even if we were to remove the Department of Education from the government employment figures, to be conservative and because educational improvement represent an important need in the USVI, we see that public sector employment still represents 14.6% of the territorial workforce.[18] This raises the possibility that government employment could be crowding skilled workers out of the private sector.




### 1. *Option for Consideration: Execute a public sector "rightsizing" initiative*

The government of the USVI could explore options and possibly develop a plan for further reducing unnecessary redundancy in the public sector, both to reduce the cost of governance and to free qualified workers for appropriate positions in the private sector. There are exiting models available, should the USVI choose to pursue this alternative; for example, the World Bank Group has developed a comprehensive set of tools that help governments identify "bloated" government agencies, classify employees based on value to the government and ability to obtain suitable employment outside the public sector, and implement change to minimize social and economic disturbance to individual workers. These tools are available "open-source," and can be found on their website via the attached link: Rightsizing Public Administrations.

Initially, the USVI government could benchmark current staff levels against those of other, comparably sized economies. The U.S. Department of Labor, Bureau of Labor

[17] United Nations Public Administration Program: Public Administration Country Profiles
[18] USVI Dept. of Labor, Bureau of Labor Statistics. 11/03/05 Presentation to EDC Annual Conference.

Statistics maintains data on public sector employees by department, as well as aggregated wage rate data (see table below). By reviewing in detail the public sector workforce of other territories, states or island nations, the USVI government could begin to formulate a plan targeting the agencies that appear to be the most oversized.

| Government Agency | Number of Employees | Percent of Gov't Employment |
|---|---|---|
| Dept of Education | 2,986 | 29.1% |
| Hospitals | 935 | 9.1% |
| Human Services | 934 | 9.1% |
| UVI | 768 | 7.5% |
| Police Department | 655 | 6.4% |
| WAPA | 617 | 6.0% |
| Dept of Health | 578 | 5.6% |
| Dept of Justice | 398 | 3.9% |
| Dept of Public Works | 363 | 3.5% |
| Port Authority | 322 | 3.1% |
| Territorial Court | 291 | 2.8% |
| Legislative Offices | 289 | 2.8% |
| Housing Authority | 269 | 2.6% |
| Fire Services | 243 | 2.4% |
| Dept of Labor | 235 | 2.3% |
| Housing, Parks and Rec | 150 | 1.5% |
| Dept of Finance | 123 | 1.2% |
| Dept of Property and Procurement | 117 | 1.1% |
| **TOTAL** | **10,273** | |

Source: USVI Dept. of Labor, Bureau of Labor Statistics. 11/03/05 Presentation to EDC Annual Conference.

# V. Taxation

The USVI tax code mirrors that of the Internal Revenue Service ("IRS"). The territory uses the same income tax rates, regulations, forms, and filing dates, and other administrative provisions as the IRS, with a few exceptions. The USVI has the independent authority under the U.S. Internal Revenue Code to reduce certain taxes, impose surtaxes no greater than ten percent, and levy non-discriminatory local income taxes—but only, in each case, to the extent authorized by the Internal Revenue Code. The following table details the taxes levied in the USVI and their individual contribution to the total tax revenue in 2005.

Source: USVI Bureau of Economic Research

| Category | Rate | Tax Revenue (2005) | % Total Tax Revenue | Description |
|---|---|---|---|---|
| Individual income taxes | 35% | $363,000,000 | 51% | Mirrors maximum rate under federal code. |
| Corporate income taxes | 35% | $117,000,000 | 17% | Mirrors maximum rate under federal code, with exceptions for 10% corporate surtax and special tax incentives. |
| Real property taxes | 1.25% | $37,900,000 | 5% | Levied on assessed value, which is 60% of actual value. |
| Trade and excise taxes | Varies | $21,400,000 | 3% | Levied on all persons and entities doing business in USVI for items manufactured or brought into the USVI for use in a business. |
| Gross receipts taxes | 4% | $125,000,000 | 18% | Levied on all receipts of business activity without deductions. |
| Hotel room taxes | 8% | $16,500,000 | 2% | Levied on guests of a hotel or other rental establishment. |
| U.S.Customs duties | 6% | $5,200,000 | 1% | Levied on items imported from U.S.but manufactured elsewhere, in amount that, when added back to amount already paid to federal government, equals 6%. |
| All other taxes | Varies | $20,900,000 | 3% | |
| TOTAL | -- | $706,900,000 | 100% | -- |

## A. The Economic Development Commission (EDC) Program

The USVI relies significantly on tax incentives to fuel economic growth in the territory. Its main incentive program, which stems from a Congressional legislation intended to encourage investment and spur economic growth in the territories, is issued by the USVI Economic Development Commission (EDC) and administered by the USVI Economic Development Authority (EDA). Businesses that qualify for the EDC Program receive substantial benefits, including a 90% rebate on income taxes paid to the USVI, exemption from gross receipts and property taxes, and special abatements for excise taxes and U.S. customs duties. In return, these companies must make a minimum capital investment of $100,000, hire at least 10 USVI residents at middle-management-salary positions, make charitable contributions to education and the local community, and be bona fide residents of the USVI. While there is a time limit on these benefits ranging from five to fifteen years (depending on the nature of a business and its location in the territory) benefits can be extended at the governor's discretion.

Overall, the EDC Program has had a positive effect on economic growth in the territory. As of August 2006, there were 101 companies listed as EDC beneficiaries and it is estimated that these businesses generate approximately 20% of the territory's annual revenues. An overwhelming majority of EDC businesses we surveyed emphasized that they would not be operating in the territory had it not been for the program's tax benefits and adamantly believe it is doing its job to promote private sector development and spur economic growth. In recent years, however, the EDC started being advertised as a tax haven,,which led to further Federal legislation (and subsequent U.S. Treasury Department regulations) aimed at tightening residency and income source rules.

**Impact of American Jobs Creation Act and Recent Treasury Regulations.** The American Jobs Creation Act of 2004 added Section 937 to the Internal Revenue Code, changing the residency requirements for the USVI and the other territories. Prior to this Act, residency was established by a test that evaluated the facts and circumstances applicable to the individual taxpayer. The new rule now explicitly requires that the person be present in the territory for at least 183 days during the tax year in question, although implementing regulations provide some limited exemptions and allow the test to be satisfied with an average of 183 days of presence in the territory over a rolling three-year period. Furthermore, the implementing regulations require that the person must not have a tax home anywhere else, nor must the person have a closer connection to the U.S. or a foreign country than to the territory.

The residency modification seems to have caused serious issues even for bona fide business owners currently under the program. There were many business entities in the territory whose owners and executives spend significant amounts of time traveling outside of the USVI conducting business related to enterprises in the islands.

Furthermore, Section 937 altered income source rules, which could significantly impact EDC services to businesses. The new rules establish that income from sources within the U.S. or sources "effectively connected" to a U.S. trade or business is not USVI-source income. This has hit the services industry in the USVI particularly hard, because to qualify for EDC benefits as a service business under Category IIA of approved industries, a company must provide services to clients outside the USVI. These services (including hedge funds and other investment or financial services) have accounted for nearly all the growth of the EDC Program since 1999, with 49 out of the 96 EDC companies in 2004 being service companies qualifying under Category IIA. With a significant amount of these service companies' clients residing in the U.S., the new regulations may effectively end EDC participation for these businesses.

The modification of the residency requirements and the uncertainty surrounding the income source rules for service businesses has had an adverse impact on the EDC Program, influencing some companies already there to pull out and discouraging new companies from entering.

Although uncertainties surrounding the rule modifications may have initially hurt the program, in the long run, the new requirements may actually serve to benefit the USVI economy. As one expert has put it, "[t]ax incentives cannot make up for the costs to business of…legal uncertainty."[19] Once the source rules are clarified, the uncertainty surrounding the investment climate will subside and investors will be able to invest in the islands with a higher degree of confidence.

**Refocusing the EDC Program.** While various academic studies denounce tax incentive programs as ineffective in increasing foreign direct investment ("FDI"), these studies acknowledge that there are some situations where tax incentives work. One such case is the country of Singapore. Singapore's tax incentive program aims not to increase the *level* of FDI, but to influence the *type* of FDI. The country is trying to attract certain types of activities to "influence the structure – not the total amount – of economic activity in the country" and has been overwhelmingly successful.[19]

Similarly, the USVI has implemented targeted tax incentives to develop its technology sector – again, the type, not the level. The USVI legislature enacted Title 17, Chapter 43 of the USVI code to:

> Provide for the creation of a protected cell corporation … to be owned by the University of the Virgin Islands Research and Technology Park Corporation, defined as the "Research and Technology Park Protected Cell Corporation," as a means to provide Hosting Services to Knowledge-Based Businesses, in the Research and Technology Park and to offer tax benefits to the Protected Cells of the Research and Technology Park Protected Cell Corporation.

The University of the Virgin Islands' Research and Technology Park on St. Croix is taking steps to attract technology companies to the islands for what is now being termed "nearshore services." Given the territory's technology infrastructure and convenient location right off the southeast coast of the U.S., the USVI could also consider refocusing the EDC Program to offer targeted tax incentives in the areas of technology and technology-related business services. St. Croix offers the second highest concentration of bandwidth in the world, thanks to the two fiber optic cables that land there. This is a largely untapped resource. Targeting its tax incentives to capitalize on this competitive advantage in technology is critical to the development of the territory's economy and gives the islands a prime opportunity to diversify beyond tourism. The USVI could perhaps ultimately become a technology and financial hub of the Caribbean. A notice issued by the U.S. Treasury Department in 2006 provides examples of technology and software activities for which the USVI would be authorized to provide tax incentives.

Since its inception, the EDC benefits have been the primary tool used by the USVI to attract outside investment. Much of the marketing of the territory to outside businesses and investors is focused on the ability to realize tax savings in the USVI. One example of this focus can be seen in the fact that the EDA is the primary investment promotion agency of the government and that a majority of EDA marketing activities are related to publicizing the EDC tax benefits. This focus on tax benefits may have inadvertently contributed to any exploitation of the EDC program which may have occurred.

[19] Bergsman, Joel. "Advice on Taxation and Tax Incentives for Foreign Direct Investment" May 1999. (Collaborative paper)

> ***Option for Consideration:*** Market the USVI to outside businesses and investors based on the entire strategic package the territory offers, reducing the emphasis on the tax savings which are possible.

The USVI has numerous assets which are attractive to investors beyond the tax benefits of the EDC. Examples of these other assets include its great broadband capacity, proximity to the U.S. mainland and protection of the U.S. flag, just to name a few. While tax benefits may be one of the most tangible benefits that can be highlighted to an external firm, the island does have other assets that companies will find attractive. By highlighting the entire package, the government of the USVI could target its outreach to companies that could prosper in the USVI even if tax incentives are eventually lost through changes in the law.

### B. Approval of EDC Applications

The procedures for approving EDC applications and extending benefits are broad and somewhat discretionary. The primary criteria involved in making an approval is whether or not the business is deemed to be in the best interest of the public in terms of promoting economic development in the territory. Currently, the Governor and the EDA board retain sole discretion over making this determination, and the Governor alone determines whether or not benefits for a particular business entity should be extended after the initial grant has expired. These officials have wide discretion in making approvals on applications. This might increase the government's flexibility to offer benefits, but it also causes uncertainty for potential investors and creates the potential for abuse. An arguably sounder approach would be to use objective criteria rather than the wide discretion that is currently enjoyed by the Governor and certain officials..

> ***Option for Consideration:*** The USVI might consider incorporating into the EDC code a detailed checklist of criteria for the Governor and EDA board to examine and respond to in the process of approving EDC applications.

An enumerated list of criteria for determining exactly what is in the best interest of the public in terms of promoting economic development would make the procedure for approving EDC applications straightforward and.

### C. Alternative to the Gross Receipts Tax (GRT)

The USVI currently has a GRT of four percent. With the exception of business entities with annual gross receipts of less than $150,000, who are exempt from tax on their first $5,000 per month of gross receipts, the GRT applies to all gross receipts with no exemptions or deductions. On top of the effective corporate tax rate of 38.5-percent, which accounts for the 10-percent corporate surtax, the GRT can be costly and burdensome on businesses not receiving EDC tax benefits.

> ***Option for Consideration:*** The USVI could consider replacing the GRT with a simple value-added tax (VAT) system.

An alternative to the GRT for the USVI could be to switch over to a VAT system. A VAT would potentially work better than the current system because it prevents taxes from "cascading" (that is, when the same proceeds are taxed multiple times), because it only taxes each party on the value that is added to the good or the service. An additional consequence is that high volume, low margin businesses are penalized to a much lesser extent under the VAT than under the GRT, because they are only taxed on the value-added, and not on their overall sales.

The VAT is also likely to be preferable to a sales tax as well, because compared to the sales tax, the VAT does not unduly pressure consumer-oriented activities. In addition, research indicates that the VAT is a relatively efficient revenue-generating instrument that tends to improve compliance, because companies have an incentive to register with the taxation authority in order to obtain refunds[20].

In addition, switching over to a VAT would be relatively straightforward in the USVI (as compared with switching over to a sales tax) because the mechanisms required to administer the VAT are fairly similar to what is already in place for the GRT. This would make the transition easier for both taxpayers and the tax collecting authority.

[20] Grandcolas, Christophe, "VAT in the Pacific Islands" Asia-Pacific Tax Bulletin, January/February 2004.

# VI. Legal system

As residents of an unincorporated territory of the U.S., USVI residents enjoy the fundamental privileges and protections of the U.S. Constitution. There are some occasions where federal laws may not apply, but for the most part, the territorial government operates similar to that of a U.S. state, with the Organic Act being roughly analogous to a state constitution.[21]

In terms of the business regulatory environment, the Virgin Islands Code includes comprehensive areas of law governing commercial transactions in the territory, including banking (Title 9); commerce, technology, and trade (Title 11); the Uniform Commercial Code (Title 11A); conservation and consumer protection (Titles 12 and 12A); and corporations and associations (Title 13 – Corporate Code). The commercial legal framework for ensuring a business-friendly regulatory environment is in place, but local businesses often cite the need for improvement in enforcement and efficiency, and there may be a need for further clarification of existing laws.

## A. Labor

The USVI is known for having some of the toughest labor laws in the Caribbean. In addition to U.S. fair labor laws and anti-discrimination provisions, the islands have incorporated several other regulations into their code to protect workers' rights. These provisions, from a business standpoint, have resulted in numerous labor disputes, and can substantially increase the cost of doing business. While the sensitivity of these issues is clearly recognized, it is nonetheless useful to examine the potential impact these regulations have on the local business climate as local labor conditions are taken heavily into consideration in investment decisions.

### *1. Provisions of Local Labor Law*

**Wrongful Discharge Act.** This Act enumerates nine categories of reasons for which an employer can terminate an employee. If the discharge of an employee does not fall within one of these nine categories, the employer can be held liable for wrongful discharge. In effect, the Act shifts the burden of proof from employees to employers to establish that the employee was *not* wrongfully discharged. This provision in the labor code has resulted in several lawsuits for discrimination against employers and is generally deemed by businesses to be burdensome and costly.

> ***Option for Consideration:*** The USVI might consider reforming its labor code to modify or eliminate the Wrongful Discharge Act and allow at-will employment.

At-will employment entails that an employment agreement may be terminated at will by either the employer or employee for any reason that is not contrary to law (such as anti-discrimination law). The USVI has in effect fair labor laws and anti-discrimination laws that can serve to sufficiently protect employees from being improperly discharged. Implementing at-will employment, combined with proper enforcement of worker

[21] The Organic Act is similar to a constitution in that it is the organizing document of the territorial government. Unlike a constitution, however, the Organic Act was not adopted by the body politic to whom it applies. Rather, the Organic Act is an act of the U.S. Congress, in which the USVI has no voting representation.

protections standard in the mainland, could reduce the amount of labor disputes and consequent costs to employers while protecting the local labor force from unfair labor practices.

**Pre-hire Arbitration Contracts.** While the USVI code contains provisions for mediation and arbitration agreements to deal with labor disputes, sources noted that the legislature does not look favorably on pre-hire arbitration clauses. These provisions generally require an employee to waive his or her right to court adjudication and submit any claims to a private arbitration system should a dispute arise. A business source in the islands implemented an alternative dispute resolution policy for settling labor disputes, but the USVI legislature deemed it unfair to force employees to sign pre-hire arbitration contracts and is currently considering legislation to make pre-hire arbitration clauses unenforceable. While some may consider such clauses to be overly favorable to employers, this concern could be weighed against the extensive costs and time of a court trial to both the public and private sector. .

Since the USVI court system is facing a backlog of cases, labor disputes take time to resolve and can be very expensive to both the business and the employee. To promote judicial efficiency and expedite the resolution of labor disputes, the USVI might examine ways in which the arbitration process in the USVI could be strengthened so that employees as well as employers would have more confidence in its ability to reasonably protect their rights. This effort might assuage the concerns that some have about pre-hire arbitration contracts, and encourage greater use of alternative dispute resolution. This, in turn, could take pressure off of the judicial system and enable it to operate more effectively. It could also reduce the amount of time and money businesses and employees spend on resolving disputes, without sacrificing reasonable worker protections.

# VII. Infrastructure

The physical infrastructure of the USVI can be difficult to develop and maintain due to the small size of the territory and the constant threat of hurricanes. The provision of public services such as electricity, roads, water and waste disposal services cannot rely to some degree on economies of scale to meet the aggregate demand for these services across the territory, a common issue in small communities like the USVI. To compensate for the small size and isolated nature, these services need to be managed effectively to drive increased quality and lower costs.

Generally speaking, infrastructure development can be provided directly by both the government or by the private sector. In areas such as communication infrastructure, where private sector entities are the primary provider of service to the public, the government could consider enacting policies that enable firms to meet the unique needs of the USVI. In other areas such as power, water, and waste disposal, which are currently provided for directly by the government, it may be beneficial to consider if private sector providers could provide these services more efficiently.

## A. WAPA Privatization

The Virgin Islands Water and Power Authority (WAPA) is charged with meeting the electricity and water needs of the territory. There has been a commonly-reported perception that WAPA is underfunded and struggles to provide adequate service. Privatization of the utility could lead to improved services at lower cost. Privatization of WAPA could also help the government to further shore up its financial situation by removing the perennial drain on government resources and providing an injection of cash through the sale of the current assets of the utility.

The government of the USVI has considered WAPA privatization as recently as 2000. At that time, an affiliate of Southern Energy, Inc. (SEI) offered the government of the USVI $380 million for an 80 percent stake in WAPA (the offer called for Southern Energy to pay $105.4 million in cash, assume $153.9 million in bonds and forgive $24 million that the government owes the authority).[22] The USVI Senate rejected Southern Energy's proposal, expressing "serious concerns regarding both the process and content of the SEI proposal"[23] citing a lack of transparency and a general feeling that the interests of the community were not considered. There was and continues to be a concern in the USVI that removing direct ownership of WAPA from the USVI community would "make WAPA beholden to interests that are not first and foremost concerned with the interests of the community."[23]

### *1. Option for Consideration: Undertake further efforts to privatize the Virgin Islands Water and Power Authority and develop an effective policy and regulatory framework for the utility in private hands.*

A 138-page report entitled "WAPA Ownership Alternatives Feasibility Study" was released in May 2005. The report outlines the significant issues related to a privatization of the utility and provides a number of alternatives to consider during the privatization

[22] "SOUTHERN CO. UNIT MAKES OFFER FOR VIRGIN ISLANDS UTILITY." The New York Times March 24, 2000.
[23] Final Report: WAPA Ownership Alternatives Feasibility Study. May 2, 2005

process. A detailed valuation was carried out based on comparable utlities to yield a combined (electricity and water) enterprise value of $256.94 to $288.69 million for the utility (See Appendix 2: Final Report on the Feasibility Study Regarding Altering the Utility Situation in the United States Virgin Islands).

The WAPA report was sponsored by a group of "concerned citizens," operating as the WAPA Buy Out Committee. The report outlines several criteria upon which to base a decision about the best means towards privatization of the utility, and suggests that an employee buyout would be the preferred means of privatization.

Privatization of WAPA will undoubtedly continue to be a sensitive issue. An earnest privatization scheme would require the government of the USVI to evaluate objectively the costs and benefits of all available options and move forward with a plan that will lead to the highest degree of economic welfare for the population as a whole.

As the sole USVI entity charged with electricity generation, electricity distribution and water distribution WAPA, necessarily operates as a public sector monopoly. Any privatization of the utility would have to explicitly acknowledge this fact and be accompanied by a regulatory framework that protects the interests of WAPA's consumers and creates an economically viable framework for privatization. According to a World Bank report, the sale of "an inefficient public sector monopoly to an unregulated private owner will almost certainly result in increased firm profitability…and greater returns to government, these gains can easily be outweighed by the welfare losses imposed on consumers and the economy as a whole from inadequate access to products and services, their suboptimal supply, or their excessively high price."[24] An effective regulatory framework can help to ensure that societal welfare is not diminished, and that the benefits of privatization are still realized. There are other models for the USVI to consider; Guam and the CNMI have already privatized segments of their power and telecommunications utilities, and are actively exploring options for privatizing the remaining segments.

[24] Kikeri, Sunita and John Nellis. "An Assessment of Privatization." The World Bank Research Observer vol. 19 no. 1 (2004): 87-118.

# VIII. Land Ownership

The USVI follows similar laws as the U.S. with regards to real property. Any person or business entity may hold title to land in the territory, but foreign persons and entities must meet certain registration requirements not required of USVI residents or U.S. citizens. Furthermore, given the territory's unique status as a group of islands, special regulations govern zoning and coastal area management. However, the parameters of these laws are not clearly defined, often making development in the islands burdensome and costly.

**Zoning and Subdivision Regulations.** Zoning and subdivision laws in the USVI have been criticized as being inflexible and inadequate, resulting according to some observers in "haphazard development and adverse environmental impacts."[25] There is currently no map or inventory of submerged and filled lands, nor is there a register establishing the economic value of such lands. Furthermore, there is no map detailing existing public access routes to the territory's beaches, even though USVI law makes all beaches accessible to the public via these customary access routes.

The territory manages coastal lands and waters through its Coastal Zone Management Act (CZMA). The coastal zone extends 50 feet inland from the low tide line and the CZMA applies to coastal waters, adjacent shore lands, and all property beneath them. Developers wishing to develop coastal properties must obtain a CZMA permit before proceeding. Aside from the CZMA, though, there is no all-encompassing plan that governs development throughout the territory.

> ***Option for Consideration:*** The USVI could consider expediting the implementation of a comprehensive land and water use plan, to provide clearly-defined zoning and subdivision provisions.

Discrepancies in current zoning and subdivision law have resulted in numerous land disputes between the government and developers, and private residents and developers. The USVI is currently looking into developing a Comprehensive Land and Water Use Plan that would overhaul the territory's current zoning and subdivision law, replace 18 zoning districts with 7 land-use zones and 5 water-use zones, and eliminate spot-zoning.[26]

> ***Option for Consideration:*** Provide clearly-defined and straightforward zoning and subdivision provisions to guide development.

Such regulations would help to reduce the amount of disputes, making the development process simpler and less costly. The USVI could also consider creating a more expedient process for accelerating the resolution of land disputes so as to reduce delays and costs to developers.

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[25] Plaskett, Dean. Senate Hearing. Senate Planning and Environmental Protection Committee. August 2004.
[26] Fields, Tim and Megan Poinski. "Contracts and Cronies." The Virgin Islands Daily News 14 January 2005: 14.

# IX. Business Practices

## A. Licenses and Permits

Starting a business in the USVI requires a business license and accompanying permits, depending on the type of activity involved. As an example, a company whose business activity entails a construction project would have to obtain a building permit; a person desiring to enter the taxi trade would have to register for a taxi operator's license. Professionals such as architects, electricians, or public accountants, among others, must be certified by their respective boards in order to practice in the USVI.

### *1. Business Licensing*

Business licenses issued in the USVI are typically valid for a term of one year and fees are specific to the particular activity, and set out by statute. Obtaining a business license in the territory involves a very straightforward set of procedures, including:

- filing an application with the Department of Licensing and Consumer Affairs (DLCA);
- obtaining a police record check and agency recommendations for zoning and fire code compliance;
- registering a trade name with the Lt. Governor's Office; and
- obtaining a tax clearance from the USVI Bureau of Internal Revenue (BIR).

The USVI has taken considerable strides in integrating technology into the public sector to improve efficiency and expedite the business licensing process by implementing an online procedure for submitting applications. There remains room for improvement in certain areas of the process, as discussed below:

**Technology.** The DLCA's online process was set up to improve efficiency and expedite the business licensing process, but business sources in the islands have reported that the online application form is not always operable and that they were unable to submit forms electronically. Others reported that extensive follow up with the agencies involved was necessary to ensure that applications were processed.

> ***Option for Consideration:*** Implement a management system to improve agency responsiveness to applicant inquiries and concerns, and to ensure that employees are kept abreast of relevant new technology.

The USVI could consider implementing a management system that focuses on agency responsiveness, including electronically logging applicant inquiries and follow-up responses to ensure promptness. The DLCA could also consider requiring mandatory technical training courses of all employees on an annual basis, to ensure that employees are kept abreast of new technologies currently in use. These are relatively small adjustments, but could have a potentially significant impact on the speed and efficiency of the licensing process.

**Coordination.** The DLCA's online One-Stop Licensing Program only handles the first two steps of the business licensing process – the application and agency recommendations – and leaves the trade name registration and tax clearance for the company to obtain separately. Businesses must therefore physically submit forms to each of these departments via mail or hand delivery to retrieve the necessary documents, adding to the time necessary to process the business license application. As a result, while it takes an average of seven to ten days to initially process a business license application, the entire process takes over two months.

There are alternative models that could be considered. For example, the state of Delaware's One Stop Business Registration and Licensing System incorporates one electronic application form for three different local agencies involved in the licensing process. Delaware's licensing system also conveniently provides links to the Delaware Division of Corporations and the Internal Revenue Service, so applicants can retrieve incorporation forms and apply for a Federal Employer Identification Number (FEIN).

> ***Option for Consideration:*** Automate the entire business licensing process to include electronic application forms for obtaining a trade name certificate and tax clearance as well as the initial license.

As the DLCA continues to consider technical improvements to its internal systems, the agency could also consider collaborating with the Lt. Governor's Office and the BIR to centralize the licensing process and make it completely electronic. This would entail implementing online mechanisms within the DLCA's current electronic application form that allow businesses to obtain the necessary trade name certificate and tax clearance electronically.

# X. Financial Infrastructure

No specific issues were raised with regard to financial infrastructure in the USVI. While access to capital is somewhat limited by the small number of financial institutions that have established operations in the USVI, funding opportunities for business development seemed to be generally available. Both private banks and government-backed lending programs are operational and generally work smoothly. The U.S. Small Business Administration and the University of the Virgin Islands operate a Small Business Development Center (SBDC). The SBDC is accessible to the general public in the USVI, and appears to be very helpful in facilitating relationships between businesses and lenders.

It is worth noting that the government of the USVI, in conjunction with the Public Finance Authority (PFA), has recently undertaken a successful campaign for a territory-wide investment-grade bond rating. Representatives of Moody's, Standard and Poor's and Fitch have visited the territory to assess creditworthiness. Two of the agencies have returned overall ratings that do indeed place the territory's general obligation credit at investment grade, making the USVI the only territory with an investment grade rating.

# XI. Conclusions

Despite the number of difficulties small island economies face, there is significant potential for private sector growth and development in the U.S. Virgin Islands. The authors of this report hope that the information and alternatives presented above will be helpful to decision-makers in the challenges they face each day. The authors would like to thank all those in the USVI, the Enterprise Research Institute, and the Office of Insular Affairs for their time and assistance on this project

# XII. Appendices

## A. Appendix 1: Select Caribbean Comparative Data

| Country | GDP (purchasing power parity) | Population | GDP - per capita (PPP) | Unemp-loyment Rate | Exports | Exports % of GDP | Imports | Imports % of GDP | Tel lines per person | Mobile Tel Lines per person | Internet hosts | % of population using internet |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Antigua and Barbuda | $750 million (2002 est.) | 69,108 | $10,853 | 11% | $214,000,000 | 29% | $735,000,000 | 98% | 0.550 | 0.781 | 2,143 | 29% |
| Aruba | $2.13 billion (2004 est.) | 71,891 | $29,628 | 7% | $80,000,000 | 4% | $875,000,000 | 41% | 0.516 | 0.737 | 5,420 | 33% |
| Bahamas, The | $6.098 billion (2005 est.) | 303,770 | $20,074 | 10% | $469,300,000 | 8% | $1,820,000,000 | 30% | 0.461 | 0.612 | 359 | 31% |
| Barbados | $4.745 billion (2005 est.) | 279,912 | $16,952 | 11% | $209,000,000 | 4% | $1,476,000,000 | 31% | 0.485 | 0.715 | 241 | 54% |
| Cayman Islands | $1.391 billion (2004 est.) | 45,436 | $30,614 | 4% | $1,200,000 | 0% | $457,400,000 | 33% | 0.836 | 0.374 | 5,069 | 22% |
| Cuba | $39.17 billion (2005 est.) | 11,382,820 | $3,441 | 2% | $2,388,000,000 | 6% | $6,916,000,000 | 18% | 0.067 | 0.007 | 1,918 | 1% |
| Dominica | $384 million (2003 est.) | 68,910 | $5,572 | 23% | $74,000,000 | 19% | $234,000,000 | 61% | 0.305 | 0.607 | 446 | 27% |
| Dominican Republic | $63.73 billion (2005 est.) | 9,183,984 | $6,939 | 17% | $5,818,000,000 | 9% | $9,747,000,000 | 15% | 0.102 | 0.276 | 81,598 | 9% |
| Grenada | $440 million (2002 est.) | 89,703 | $4,905 | 13% | $40,000,000 | 9% | $276,000,000 | 63% | 0.365 | 0.483 | 18 | 9% |
| Guadeloupe | $3.513 billion (2003 est.) | 452,776 | $7,759 | 27% | $147,800,000 | 4% | $1,766,000,000 | 50% | 0.464 | 0.714 | 418 | 17% |
| Haiti | $14.15 billion (2005 est.) | 8,308,504 | $1,703 | N/A | $390,700,000 | 3% | $1,471,000,000 | 10% | 0.017 | 0.048 | 3 | 6% |
| Jamaica | $12.17 billion (2005 est.) | 2,758,124 | $4,412 | 12% | $1,608,000,000 | 13% | $4,093,000,000 | 34% | 0.142 | 0.798 | 1,271 | 39% |
| Martinique | $6.117 billion (2003 est.) | 436,131 | $14,026 | 27% | $404,200,000 | 7% | $2,307,000,000 | 38% | 0.394 | 0.733 | 70 | 25% |
| Puerto Rico | $72.7 billion (2005 est.) | 3,927,188 | $18,512 | 12% | $46,900,000,000 | 65% | $29,100,000,000 | 40% | 0.283 | 0.683 | 132 | 25% |
| Saint Kitts and Nevis | $339 million (2002 est.) | 39,129 | $8,664 | 5% | $70,000,000 | 21% | $405,000,000 | 119% | 0.639 | 0.256 | 48 | 26% |
| Saint Lucia | $866 million (2002 est.) | 168,458 | $5,141 | 20% | $82,000,000 | 9% | $410,000,000 | 47% | 0.303 | 0.552 | 25 | 33% |

| Country | GDP (purchasing power parity) | Population | GDP - per capita (PPP) | Unemp-loyment Rate | Exports | Exports % of GDP | Imports | Imports % of GDP | Tel lines per person | Mobile Tel Lines per person | Internet hosts | % of population using internet |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Saint Vincent and the Grenadines | $342 million (2002 est.) | 117,848 | $2,902 | 15% | $37,000,000 | 11% | $225,000,000 | 66% | 0.161 | 0.484 | 21 | 7% |
| Trinidad and Tobago | $18.01 billion (2005 est.) | 1,065,842 | $16,897 | 8% | $9,161,000,000 | 51% | $6,011,000,000 | 33% | 0.301 | 0.611 | 17,171 | 15% |
| Turks and Caicos Islands | $216 million (2002 est.) | 21,152 | $10,212 | 10% | $169,200,000 | 78% | $175,600,000 | 81% | 0.269 | 0.080 | 1,488 | N/A |
| Virgin Islands | $1.577 billion (2004 est.) | 108,605 | $14,521 | 6% | $389,000,000 | 25% | N/A | N/A | 0.653 | 0.378 | 3,818 | 28% |
| British Virgin Islands | $853.4 million (2004 est.) | 23,098 | $36,947 | 3% | $25,300,000 | 3% | $187,000,000 | 22% | 0.507 | 0.346 | 480 | 17% |

Source: CIA Fact Book

## B. Appendix 2: Final Report on the Feasibility Study Regarding Altering the Utility Situation in the United States Virgin Islands

WAPA

Document imbedded or available at: http://www.house.gov/christian-christensen/WAPAFinalReport.pdf