

An Analysis  
of the  
Economic Impact  
of  
Guam's Political Status Options

Final Draft

Presented to the  
Guam Commission on Decolonization  
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## **Executive Summary**

This analysis is intended to advance the understanding of the probable economic outcomes of a transition in Guam's political status. The options under consideration are statehood, free association and independence. Because of the prospective nature of the status change, a number of assumptions are made about the resulting economic environment in Guam. The economic effects of potential changes in Guam's relationship with the United States and other nations are also considered.

An extensive, detailed description of recent economic conditions in Guam is provided as a basis for comparison with prospective conditions under each of the three status options. This description also serves to focus on those elements of Guam's current status that are viewed as constraints that might be remedied by a status change.

A brief account of Guam's political and economic history serves as a point of reference for the options being considered. This, along with the experiences of other places that have undergone similar status changes, lays the foundation for a depiction of what Guam can expect under each option.

The prospects for Guam under each status option are then described, with particular reference to the assumptions that are made about the results of negotiations with the U.S. government. Each of the major characteristics of Guam's economy is discussed in detail for each prospective status. The relative certainty of the results of the statehood option is put into perspective with the intermediate ground of free association and the ultimate liberation of independence, and the respective levels of risk are reflected in the ranges of prospective outcomes which could result. In essence, though, the crucial components of Guam's economic future revolve around the impacts of each status option on U.S. federal funding, external investment and tourist spending. These funds flows and their status-oriented characteristics will define the primary aspects of Guam's post-transition economy.

Finally, a quantitative model of Guam's economy is presented to indicate the prospective outcome of each of the status options one year and five years after the transition occurs. It is based upon in- and out-flows of funds from the economy, and is tested against the *status quo* for reliability. The results of the model indicate low, expected and high outcomes for each time frame, and also reflect the level of uncertainty about the ultimate outcomes of the three status changes under consideration. For most segments of the community, sufficient detail is provided to assess how each would be affected by a combination of changes in various expenditure categories. The model is original, developed specifically for this study, but may form the basis for economic forecasts in Guam regardless of the status option that is selected by the island's eligible voters.

As the report shows, there are advantages and disadvantages to each of the status options. It is up to the eligible voters of Guam to decide which option would be most desirable, and the economic dimension will be only one factor in that decision. However, this is an attempt to help to refine the definitions of statehood, free association and independence, and to describe potential economic conditions under each.

While the quantitative model indicates that the economy would perform better under statehood than under free association or independence within the first five years, there are other, non-economic factors that must be considered; those are beyond the scope of this report.

Clearly, independence provides the greatest freedom and latitude for Guam to pursue its goals, while statehood provides the highest level of security among the possible outcomes. Statehood would increase Guam's Gross Island Product because of increased U.S. federal government agency presence, the fortification of the island's defenses, and the political influence of two voting Senators in Washington. Free association could bring some of these benefits, while also mitigating some of the current constraints on Guam's economy. Independence would significantly loosen the ties between Guam and the United States, but would provide the greatest latitude to the people of Guam in defining and pursuing their own destiny, with the greatest economic opportunities accompanying the highest level of risk among the three options.

In any event, Guam's economic prospects beyond the five-year time frame presented in this report may be far different than the early impacts. It is left to the public to decide if the risks associated with each status option in the early years are adequately compensated by potentially improved economic conditions for future generations.

## **Introduction**

This report was prepared under contract for Guam's Commission on Decolonization. It is intended to analyze the prospective economic conditions under each of three status options being considered in a plebiscite to be held in Guam. Those options are to seek a change from the island's current status as an unincorporated territory of the United States to either a State within the U.S., a nation in free association with the U.S., or an independent nation. Whichever option is selected, it is anticipated to lead to negotiations with the United States toward the realization of the political status aspirations of the Chamorro people of Guam, those persons who are descendents of people who resided in Guam upon the signing of the Treaty of Paris in 1898.

Because this report provides an economic analysis of prospective future economic conditions in Guam, it is necessary that it first establish a benchmark with which comparisons can be made. Thus, the report begins with a detailed description of the *status quo*, the economic conditions in Guam today. Wherever possible, these conditions are explained in terms of the legal and political framework under which they prevail. In many areas, this requires an analysis of parameters that are not strictly economic in nature, yet which have an impact upon the structure and performance of the economy. Other parameters that affect the overall well-being and economic opportunities of the people of Guam are also discussed.

Since the early days of the U.S. colonization of Guam, efforts have been made to improve the island's political status. Some of these efforts were initiated by the U.S. and its representatives, while most were initiated by Guam's civic leaders. These efforts have met with more or less success over the past century, but there is a continuing sense of dissatisfaction with the current status among many members of the community. Just as it is necessary in this report to provide a description of the current condition of the economy as a benchmark against which prospective conditions can be compared, it is also useful to provide an outline of the history of Guam's political status efforts to provide perspective relative to the current initiative. Both the progress that has been made and the setbacks that have been encountered serve to illustrate Guam's evolving objectives and the constraints that exist in modifying its relationship with the U.S. government.

There is an enormous amount of uncertainty associated with Guam's political status initiative, and this uncertainty derives from several sources. Since the status plebiscite has not yet been conducted, it is not known which option will be selected. Once an option is selected, the people of Guam (presumably through their leaders) will have to develop a timeline and strategy for achieving their objectives, but neither has yet been developed. Priorities among the multitude of characteristics in the island's political relationship with the U.S. will also have to be established. Then, negotiations with the U.S. government can begin, but the negotiating position of the U.S. will not be known until that time. As a result of these negotiations, Guam's new political status will be defined, but it is impossible to know ahead of time what that definition will be. By necessity, then, this report lays out a detailed set of assumptions for each of the status options, based upon extensive research and the collective experience of the consultant and his associates. However, these assumptions may or may not accurately reflect the eventual status reality that Guam will experience.

Compounding the uncertainty is the fact that Guam is almost entirely dependent upon external factors in the performance of its economy. Primary among these factors are spending in

Guam by the U.S. government, investment expenditures which are predominantly from the outside, and the flow of tourists and their purchasing power into the island. Each of these could be affected in various ways under any of the status options, based upon both external economic conditions and reactions to internal conditions within Guam. Further, how they are affected will potentially change over time. Because of this, a range of possible outcomes for each status option is described in this report.

The final aspect of uncertainty about the economic outcome of whichever political status option is selected relates to the internal actions of Guam and its leaders. This is particularly true with regard to free association and independence, but also applies in the case of statehood. For instance, the rate of economic growth in Guam will depend upon the level of outside investment, which will itself depend upon the structure of taxes in Guam, the range and attractiveness of investment incentive programs, the degree of aggressiveness with which the island promotes itself internationally as an investment destination, and numerous other factors. There is no way of knowing in advance how well Guam will perform in implementing an optimum investment climate, so gauging the level of prospective investment is subject to substantial error. The same type of uncertainty applies in several other dimensions of Guam's post-status change economic environment, yet it is these factors that will prove to be most important in determining the island's economic destiny.

This report attempts to minimize the uncertainty described above through a number of means. The history of Guam's political relationship with the United States and the progress in securing improvements in that relationship provide meaningful guidance as to what can reasonably be expected. Coupling this with the recent experience of other jurisdictions in changing their respective relationships with the U.S. serves to temper the uncertainty even further. Reference to status changes in non-U.S. jurisdictions also helps to define what classes of change can be made, and how those changes might be accommodated.

Similarly, although several assumptions must be made, the history of Guam's economic performance in response to federal, investment and tourist expenditures helps to support the measurement of the prospective impacts of each status option. The assumptions interpret how the various external forces would most likely respond to political change in formulating their economic decisions, and the impacts of those decisions are relatively easily translated into economic terms.

In much the same way, the experience of other jurisdictions, including those affiliated with the U.S. and those aligned with other nations, helps to establish a set of reasonable expectations about Guam's economic prospects under the various status options. While none of these other jurisdictions are strictly comparable with Guam, the nature of the changes that they have undergone provides guidance in the preparation of this report.

Despite the efforts of this report to minimize uncertainty about Guam's future under the three alternative status options, a substantial amount remains. There are simply too many parameters, each with too many possible outcomes, for it to be otherwise. Therefore, regardless of how specific this report may appear to be with regard to some aspects of the island's economic future, it should be recognized that, at best, it provides only a general description of what may result.

This *caveat* also applies to the economic model that is presented at the conclusion of the report. The consultant attempted to apply two existing models of Guam's economy in

forecasting the impacts of the political status change, but encountered intractable difficulties with both. Neither model was designed for this type of application in the first place, and some of the data necessary to drive the models are no longer available. Therefore, it became necessary to develop a new model of the economy that would simultaneously rely only on available data and provide the kind of comparability that would be most useful to the public in assessing the impacts of the status change.

Essentially, the principal changes that can be expected to affect Guam's economy in the wake of a status change will be transmitted through cross-border flows of funds into and out of the island. This is not to say that there will not be changes internal to Guam, merely that the impacts of those changes will primarily be based upon how they affect the flow of funds. Since Guam must import the vast majority of the goods it consumes, strictly internal flows take on relatively minor importance in comparison.

How changes in the cross-border flows of funds will affect Guam's "Gross Island Product" (commonly referred to as "Gross *Domestic* Product") is analyzed by the application of various multipliers to different types of funds flows. These multipliers have been used in innumerable other contexts and have been found to be reasonably reliable. Further, they have been tested in relation to Guam's economy and determined to provide sound estimates. By applying these multipliers to the changes in funds flows anticipated to result from the alternative status options, a reasonable set of estimates of the economic outcomes of each status change is derived.

It is emphasized, though, that the model presented in this report is new to Guam, and is subject to an indeterminate amount of error. This is inevitable, and would be true of any model applied to such significant changes in any complex system. Nevertheless, it is important to recognize that the estimates presented here are not perfectly reliable, and should only be taken as guidelines as to how the economy might behave under the conditions that are expected.

It is hoped that this report receives wide and general circulation. While it is acknowledged that it is lengthy, complicated and sometimes tedious, it includes a wealth of information that should be quite useful in helping Guam's eligible voters assess the options with which they are to be presented in the plebiscite. It should also be of value in the future in that it develops a new model of the economy which can have wide application in economic analysis and forecasting.

# Guam's Economy – The *Status Quo*

## Physical Geography

### Location

Upon initial assessment, it would appear that Guam's physical location would be disadvantageous in terms of its economic prospects. Far from any substantial land mass, the island is figuratively "out in the middle of nowhere." However, Guam's location in the western Pacific places it in a location that has regularly been described as "strategic" from a military perspective; it has also proven to be strategic from an economic perspective, particularly given some of its other physical characteristics. Location, along with some of those other characteristics, placed the island at the center of pre-contact regional trading activities, and later allowed Guam to begin developing a modern economy long before its neighboring islands.

The Spanish Empire used Guam as a re-provisioning stop between the Philippines and Mexico, and brought metals and other useful items with them for trade with the resident population. Although the availability of fresh water on the island was critical to the Spanish in these exchanges, no stops would have been made here if Guam were not along the trade route.

The German whaling fleets used Guam as a port of call for much the same purpose, but also used other places as seasonal migrations occurred. Nevertheless, if Guam had not been along established trade routes, the islands residents would have not have been able to trade what they had for what the whalers brought.

Ceded to the United States under the Treaty of Peace between the United States and Spain,<sup>1</sup> signed at Paris, December 10, 1898, and proclaimed April 11, 1899, as ". . . the Island of Guam in the Marianas or Ladrones."

Although the island was initially used predominantly by the U.S. Navy as a coaling station, Guam's strategic location was in close proximity to U.S. activities and interests in the Southeast Asian theater of operations. This eventually led to the formation of significant infrastructure by the U.S. military, which incidentally accelerated the economic development of the civilian community, as well. Had Guam been located much further east or to the south, such infrastructure development may have occurred differently.

Guam's location has also made it an attractive destination for Asian tourists, as well. The relatively short air travel distance from Japan and other Asian countries to Guam has allowed the island to effectively compete with other locations, such as Hawaii, during the last thirty years. Guam is three hours flying time from Tokyo and five hours or less from all the other major Asian population centers. Recent improvements to the airport infrastructure and facilities make the island well-positioned to take advantage of the long-pending release to the local government of the adjacent military lands, infrastructure and facilities.

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<sup>1</sup> This Treaty of Peace is commonly referred to as the "Treaty of Paris" because of the location in which it was signed, and will be referred to as such throughout the rest of this document.

Guam's location is, nonetheless, remote by most standards. This has been an obstacle to development because of the relatively high costs involved in the shipment of everything from consumer goods to construction materials to finished products to and from the island. Even with the emerging Internet and transportation technologies, location has also inhibited the mobility of the people of Guam in pursuing alternative employment, thus affecting incomes and standards of living.

Guam's remoteness, though, is less relevant in an information and connectivity sense in this age of advanced telecommunications technology and the Internet. Guam is well connected to the rest of the world by start-of-the-art communications systems, including private, trans-oceanic fiber-optics and sophisticated military systems. It is part of the North American Numbering Plan and has access to 1-800 dialing,

## **Land**

One of the primary constraints on Guam's economic development is its limited land area. At approximately 212 square miles,<sup>2</sup> by any evaluation the island of Guam is a relatively small land mass. This limitation affects the availability of land for agricultural development, for commerce and industry, and for housing, thus placing upper boundaries on population and the potential for enterprise. Limitations on population, in turn, affect potential productivity by reducing opportunities for the specialization and division of labor, as well as total output, income and tax revenues.

In terms of agricultural pursuits, Guam's soils are poor to moderate in their support for agricultural development. Most of the island is characterized by clay, limestone and other soils that are marginal, at best, in their support of agricultural activity. Add to that the frequency of tropical cyclone activity and the abundance of plant pests that thrive in the tropical climate, and agricultural activity is severely limited.

Although the ratios have changed in recent years, it is still useful to think of Guam land as being roughly evenly divided among private, local government and U.S. federal ownership and control. Most privately held land in Guam is utilized fairly intensely, with the corridor stretching from Apra Harbor in west-central Guam to Anderson Air Force Base in the north being particularly heavily developed for commercial and residential purposes. Being on the leeward side of the island, these properties are better protected from tropical cyclones and are level enough to lend themselves to simpler, less costly construction techniques. There is also a band of development across the central part of the island that is primarily devoted to residential use.

The "best" land in Guam for development purposes is in the northern half of the island, but a substantial portion of this land is held by the U.S. federal government, and therefore unavailable for civilian economic use. Further, much of the land owned by the U.S. Air Force in the northern half of the island is left idle, including that which restricts access to the prime private beach areas of Urunao. The sprawling air base also covers much of the Northern Aquifer, and ground water pollution from military activities there have forced the closing of several wells in recent years. In this regard, a substantial portion of Guam's most economically valuable land goes unused because of land tenure restrictions. It was estimated in 1992 that the

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<sup>2</sup> United States Department of Agriculture, Soil Conservation Service, "Soil Survey of Territory of Guam," p. 1, May 1988 (54,908 hectares).

holdings of idle land by the federal government in Guam cost the local government as much as \$69 million annually in foregone government revenues alone.<sup>3</sup> In addition to the northern U.S. Air Force landholdings, U.S. military lands in Guam include the former political and economic capital of Sumay, which is part of the extensive southern holdings by the U.S. Navy. The contribution that excess land held by the U.S. military would make to Guam's Gross Island Product (Gross Domestic Product) in 2000 is estimated to be \$1.1 billion annually, if it were available for civilian use.<sup>4</sup> This is more than one third of Guam's GIP.

## Geology and Topography

The island of Guam is the peak of a seamount rising some 30,000 feet from the surrounding seabed. Because of its proximity to the margin between the Philippine Plate and the larger Pacific Plate, the island is subject to periodic and moderate to severe seismic activity.<sup>5</sup> Relatively frequent earthquakes strike the island, but damage is typically minor due to a rigorous building code. This code, though, places such stringent requirements on structural design and construction. Coupled with the fact that almost all of the construction material and labor is imported, this makes Guam's building costs among the highest in the world.<sup>6</sup>

The Mariana Islands (of which Guam is the southernmost) are an extension of the Honshu Ridge, and were formed through volcanic activity along the edge of the Philippine Plate. Guam is generally believed to have been formed from two volcanoes, with the northern one having been submerged some 400 feet below sea level for millennia. Recent studies have concluded that the northern and southern portions of the island are of approximately the same geological age, but they are quite different on the surface. This can be seen in the differences between the northern and southern halves of the island: the North has a coral substrata originally formed atop a submerged volcano, and later uplifted when it rose from the depths some 10,000 years ago; the South characteristically has a shallow layer of soil covering basalt.

The northern plateau is relatively level, rising from near sea level just south of Hagåtña to some 600 feet at the northern cliff line. The southern half is more mountainous, and the dividing line across the island from Adelup to Pago Bay is clearly visible to the casual observer. The coral substrata in the north contains Guam's aquifer, a water lens that provides most of the fresh water to the island's population, while water drains to the ocean in free flowing rivers in the southern half.

The poor substructure and steep slopes of the southern half of Guam make it less suitable to construction and more prone to landslides than the northern half. Arable land in the South is the richest in Guam, but only in the river valleys and narrow alluvial plains. As a consequence, there is considerably less agricultural development in the southern than in the northern half. Therefore, a much smaller proportion of the South is suitable to the support of economic activity. With the notable exception of Naval Activities Guam (formerly Naval Station, Apra Housing,

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<sup>3</sup> Barakat & Chamberlin, "*Analysis of the Impact of the U.S. Military Presence on Guam*," (Draft, 8-18-92), Exhibit 35.

<sup>4</sup> Op cit. The Barakat & Chamberlin figure for foregone tax revenues in 2000 is adjusted by Guam's average 1993 – 1997 tax burden to derive this estimation.

<sup>5</sup> The "Great Quake" of August 8, 1993, measured 8.1 on the open-ended Richter scale.

<sup>6</sup> According to the Chief Engineer, Guam Department of Public Works, Mr. Mark Gagarin.

Naval Magazine and other, smaller facilities, which collectively much of the best land in the west-central part of the island), Guam's South has been left almost entirely to civilian control.

Geologic and topographical conditions in Guam serve as inhibitors to economic activities in many ways. In comparison to other places, the effects are slight to moderate, but they are nevertheless significant.

## **Natural Resources**

Guam is surrounded by vast ocean resources. However, it is not endowed with substantial natural resources, other than its people and the beautiful beaches and scenery. Mining (other than for coral to use as aggregate in roadways and concrete) is non-existent. Forestry has not been widely practiced (except in harvesting firewood) since before World War II, when sizeable areas of Guam's hardwood forests were destroyed by the shelling and accompanying fires preparatory to reoccupation by U.S. forces. Development has crowded out large undomesticated animals, with the exception of a number of deer, wild boar, carabao and dogs. Although fish are reasonably abundant in Guam's coastal waters, the cold temperatures of the waters around the island are relatively barren in comparison to waters just a few hundred miles to the south. The more popular pelagic species are concentrated there, as is commercial fishing activity. There are no rivers large enough to provide significant hydropower. There is a natural large, deepwater harbor that is protected from the frequent typhoons. It is located on the central leeward side of the island, in reasonably close proximity to the business district. The harbor area is very advanced relative to other infrastructure in Guam, having been improved and extended over the years by both the military and civilian governments.

## **Special Characteristics**

Similar to the Spanish, the original American interest in Guam was based upon its strategic location as a coaling station in the days of steam-driven naval vessels. With the option of selecting "an island in the Marianas" under the Treaty of Paris, the U.S chose Guam because of its natural deep-water harbor. In contrast to the Spanish, though, the principal interest of the United States in Guam was its value for military purposes rather than to support commerce and trade.

The topography of Guam's northern plateau provides two advantages that are found on very few islands. First, the porous limestone substructure creates a natural aquifer, a "water lens" in which fresh water that percolates through from the surface floats atop saltwater that has infiltrated from the sides. This water lens provides most of the potable water consumed in Guam, and has an estimated capacity to produce some 57-to-60 million gallons per day. With proper management, this capacity could support a substantial increase in Guam's population and economic activity. Fena Reservoir provides a secondary source of fresh water for Guam, but presently lies within a military reservation. Both the Ugum and Ylig Rivers have been studied for their potential as additional fresh water sources (estimated to be as high as an additional 60 million gallons per day, varying seasonally), but have not been extensively developed.

The second advantage provided by the northern plateau is that it is large, relatively flat and uniform, providing an appropriate region for residential and commercial development, but also having sufficient areas already designated for airfields. Guam's remote location makes air

transport almost imperative in the support of meaningful economic development, and the characteristics of the land are well suited to this purpose.

The deep waters surrounding Guam may also be beneficial in the future. To the east of Guam, significant quantities of manganese have been discovered. At present, extraction of this resource is not commercially feasible, but is expected to be once ocean mining technology improves and current sources of the mineral are depleted.

Because of the cold temperature of the waters surrounding Guam, along with their depth, ocean thermal energy conversion (OTEC) holds the potential to provide an alternative source of energy to the island. Cost structures do not make OTEC commercially feasible today, but changes in technology and the decreased availability of fossil fuels in the future may allow Guam to take advantage of this characteristic.<sup>7</sup>

### **Population and Ethnicity**

The most recent census of Guam was conducted in 1990, and although sophisticated statistical projections of the population are available,<sup>8</sup> they are of dubious value because of irregular components affecting the island's population growth. Based upon growth patterns from 1980 to 1990, the population in Guam in 2000 was expected to reach 167,292.<sup>9</sup> However, because of changes in the economic growth rate reducing immigration and increasing emigration, along with significant reductions in the U.S. military mission, the true population may fall far short of the projection. The extent of the Micronesian population, which has reportedly grown substantially with the entry rights granted by the U.S. to the Freely Associated States, remains difficult to measure with accuracy, but a 2000 population of 150,000 to 155,000 is more likely. Although the economic differences between the 1980s and 1990s would not be expected to affect the distribution of age or gender in the 2000 population, military downsizing has, increasing the median age and bringing the genders more closely into balance.

Guam has a rather unique population in terms of its ethnic composition, due to generations of migration into and from the island. Although the ethnic distribution in Guam is still dominated by Chamorros, they had fallen below half (to 43.3%) of the population by 1990. Those of Asian descent made up the second largest group in 1990, at 29.5%, and this group was dominated by those of Filipino heritage (22.6%). Caucasians came in a distant third, comprising 14.4% of the population.<sup>10</sup> However, this distribution will likely change significantly under current U.S. immigration policies as time passes. As evidence of this, according to a formal

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<sup>7</sup> Information from Mr. Charles Crisostomo, former Administrator of the Guam Economic Development Authority, indicates that OTEC will not become commercially feasible for Guam until the prices of fossil fuels increase well beyond their current levels.

<sup>8</sup> Based upon 1980 – 1990 intercensal changes.

<sup>9</sup> 1997-1998 Guam Annual Economic Review, Guam Department of Commerce, Table PO2, Census and Population Division, Department of Commerce, Government of Guam.

<sup>10</sup> 1997-1998 Guam Annual Economic Review, Guam Department of Commerce, Table PO3, Census and Population Division, Department of Commerce, Government of Guam.

survey conducted in 1998,<sup>11</sup> the ethnic distribution between Chamorros and Filipinos was equal, with 32% of the population comprised of each group at that time.

## **Gender and Age Distribution**

In part because of the military presence and in part because of the significant number of transient construction workers in Guam in 1990, the population was skewed in favor of males. There were some 11,952 active duty military personnel in Guam at the time of the 1990 Census,<sup>12</sup> along with some 3,298 temporary alien laborers in the construction industry; both of these groups were predominantly male. Guam's relatively high birth rate and the young age of most military personnel combined to reduce the overall median age below developed nation standards.

In 1990, the median age of Guam's population was 25.0 years; the ratio of males in the population was 53.3%.<sup>13</sup>

### *Working Age Population*

The population of persons aged 15 years and older in 1990 was 93,200; of these, 54.3% were male.<sup>14</sup> This, though, reflects the dominance of transient males in the military and in the construction trades. As of June 1999, the estimated working age civilian population<sup>15</sup> in Guam was 105,270, of which 50.8% was female. Of the estimated labor force of 72,700 at the time, 44.7% were female, with a labor force participation rate of 60.8%; the labor force participation rate among males was 77.6%, and the overall rate was 69.1%.<sup>16</sup>

### *Trends*

Over the course of the past generation, Guam's labor force participation rate has increased fairly steadily, and labor force participation among females has increased most rapidly as traditional roles within the household have changed. Thus, the labor force has been growing more rapidly than the population (averaging a 3.5% compounded annual rate versus approximately 2.2% from June 1979 through June 1999). The industrial composition of the labor force has changed, as well, as shown in the benchmark comparisons below:

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<sup>11</sup> From a survey designed by the Gannett Corporate Research Department and conducted by Schulman, Ronca and Bucuvalas, Inc. of New York. Schulman, Ronca and Bucuvalas is independent of Gannett's corporate offices and the Pacific Daily News. The sampling error of the survey is reported to be +/- 3.5% with a confidence level of 95%.

<sup>12</sup> U.S. Bureau of the Census 1990 CPH-6-G, "Social, Economic and Housing Characteristics: Guam."

<sup>13</sup> U.S. Bureau of the Census 1990 CPH-6-G, "Social, Economic and Housing Characteristics: Guam."

<sup>14</sup> U.S. Bureau of the Census 1990 CPH-6-G, "Social, Economic and Housing Characteristics: Guam."

<sup>15</sup> Defined as being sixteen years of age or older.

<sup>16</sup> Current Labor Force Survey, Bureau of Labor Statistics, Guam Department of Labor, June 1999.

## Payroll Employment Statistics

	March 1979	March 1999
Total Payroll Employment	33,800 (100.0%)	63,460 (100.0%)
Total Private Employment	17,600 (52.1%)	44,600 (70.3%)
Agriculture	100 (0.3%)	330 (0.5%)
Construction	4,900 (14.5%)	6,500 (10.2%)
Manufacturing	1,200 (3.6%)	1,830 (2.9%)
Transportation & Public Utilities	2,700 (8.0%)	4,830 (7.6%)
Trade	6,800 (20.1%)	14,140 (22.3%)
Finance, Insurance & Real Estate	1,200 (3.6%)	2,690 (4.2%)
Services	8,400 (24.9%)	14,280 (22.5%)
Total Public Employment	16,200 (47.9%)	18,860 (29.7%)
Federal Government	6,600 (19.5%)	4,800 (7.6%)
Government of Guam	9,600 (28.4%)	14,060 (22.2%)

Source: Bureau of Labor Statistics, Guam Department of Labor

## Education and Training

### *Public Education*

Public education has been prevalent in Guam for nearly 100 years. Through its extensive public school system, Guam provides free or relatively inexpensive education at the primary, secondary and tertiary levels. Most schools are primarily modeled after the U.S. system, with a few schools based more on the Asian system. Tertiary schools, though, are accredited under U.S. standards. The system in general is inadequately funded, is deficient in advanced instructional technology, and has difficulty attracting and retaining sufficient numbers of qualified teachers. As a result, standardized test scores for Guam's students fall into the lower percentiles when benchmarked against US standards. Although the tests may be culturally biased, there is also some concern that the public education system, for whatever reason, is not adequately preparing Guam's youth for the challenges they will face as adults in the global economy.

### *Government of Guam*

The government of Guam supports a public education program for students ranging from pre-school through post-graduate college studies. Based upon the U.S. educational system, a liberal selection of courses is taught in the English language; credits are generally transferable to other schools throughout the U.S. During the 1998 – 1999 school year:

There were 27 public elementary schools in Guam, with 16,102 students and 762 teachers.

There were 7 public middle schools on the island, with 7,205 students and 521 teachers.

The government of Guam operated 4 high schools, with 8,364 students and 458 teachers.

### *Department of Defense*

In 1996, the U.S. Department of Defense determined that enrolling the children of its personnel in the Guam public school system was not in its best interests, and developed its own school system in Guam for the pre-school grades through high school. The final results of this segregation of the children of federal employees from their civilian counterparts for educational purposes have not been determined, but the action removed some \$12.4 million of funding from the civilian public school system annually.

In the 1999-2000 school year, Guam's Department of Defense Education Agency (DODEA) schools employed some 200 teachers and enrolled some 2,400 students from grade school through high school.

### *Private Education*

There are 29 private schools in Guam. Two of these are commercially operated enterprises offering remedial and accelerated learning programs. Another three of these are devoted to specialized training in well-defined skill areas. The remaining 23 are traditional schools operated by church affiliated organizations, including 4 schools that provide a full educational program from pre-school through high school.

The Catholic School System operates 15 schools from K-12 with 3,801 students and 270 teachers/aides.

There are 14 additional private schools of various denominations with 2,916 students and 210 teachers.

### *Vocational Education*

In addition to the three private specialized training enterprises, vocational training is provided by the Guam Community College, which offers Associate degrees and Certificates of Completion in several areas that are relevant to Guam's principal industries. There is a conscious effort to continually adapt the programs offered by the College to the realities of the labor market. Fourteen percent (14%) of the College's \$13 million annual budget is funded by the federal government.

### *The University of Guam*

The University of Guam is a land grant college originally founded as the College of Guam in 1952. It was re-chartered under its present name on August 12, 1968. First accredited by the Western Association of Schools and Colleges in 1963, it offers a variety of academic and professional programs, and has an enrollment of 3,577 students for the Spring semester of 2000. Included in the curriculum are courses in Business Administration, Nursing, Education and Public Administration terminating in the Masters Degree. Twenty-three percent (23%) of the University's \$34,317,050 overall budget is provided through grants and scholarships funded by the U.S. government.

## **General Legal Environment**

As in any community, the primary function of government is to protect its citizens from outside aggression. In Guam, the U.S. federal government generally performs this function. A secondary, essential function of government is to maintain order, establishing and enforcing the rules under which human interaction takes place. This includes laws defining and controlling criminal activity, but also encompasses the entire set of laws and regulations governing economic relationships. This function is generally performed by the local government in Guam, within a framework provided by the U.S. Constitution and laws.

Under different systems, the process for the formulation of laws and regulation, the methods of enforcement and the mechanisms for adjudication vary substantially. In Guam, the government is generally patterned after what has been called the American system of government, with laws that are adaptable to changing situations, but which are compatible with and subordinate to a constitution that can only be changed through rigorous efforts. It is this structure that lends stability and durability to the American system of government.

### **Structure of Government**

Under the American democratic system, as it is applied in Guam, there is an attempt to attain a balance of powers within the government. A separation of authorities is intended to serve as an inhibitor against the abuse of governmental authority. This is the system of “checks and balances” that is often cited as the foundation of justice within many democracies. Generally conceived in the ancient Roman empire, this system of government was modernized by the French political philosopher, Voltaire.<sup>17</sup>

As a colony of the United States, the laws and regulations of the U.S. government, *as applicable in Guam*, carry overriding authority in Guam’s legal system. However, there are many U.S. laws that are *not* applicable in Guam, either because they expressly exclude Guam from their application or they fail to include Guam in their enumeration of where they apply; in many other cases, it is unclear whether specific laws apply until they are the subject of adjudication.

The basic law of Guam is the Organic Act of Guam,<sup>18</sup> as amended. The Organic Act was first passed by the U.S. Congress in 1950, granting the island’s people a limited measure of self-government by authorizing an elected Legislature with the power to pass laws governing the internal affairs of the island. The Organic Act also provided for the first civilian government in Guam since the time of Spanish colonization, although the Chief Executive, the Governor, was appointed by the President of the United States rather than elected by the people of Guam. Further, this Governor had absolute veto authority over all Bills duly passed by the Legislature. Thus, the Legislature only had those powers that were allowed to it by the Governor.

The Organic Act also established a judiciary in Guam for adjudication of matters brought under local law.

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<sup>17</sup> A pseudonym used by François-Marie Arouet in his classic writings on political philosophy.

<sup>18</sup> USC Title 48, Chapter 8A, §1421 et. seq.

In 1970, the U.S. Congress passed the Elective Governor Act, providing for an elected Chief Executive for Guam. This helped to complete the structure of government of Guam in alignment with the American system. However, it fell short of providing internal self-government for Guam, since each law duly passed by the Legislature and approved by the Governor of Guam remained subject to unilateral repeal by the U.S. Congress.

### *Legislative Branch*

Guam has a unicameral Legislature, originally consisting of 21 members elected to two-year terms. In 1999, this number was reduced to 15 Senators. Elections to the Guam Legislature are “at large,” meaning that each Senator represents the population of the entire island, rather than only those within a specific voting district.

Upon inauguration, the members of the legislature internally elect their own leadership, which is usually favorable to the Senators from whichever political party holds the majority of seats. Committee assignments (chairmanship and membership) are also determined in this way. Each Committee, which oversees a fairly narrowly defined area of responsibility, includes at least one member from the minority party.

Each Senator has the right to introduce legislation for consideration by the Legislature, and the Governor may also introduce Bills through the Offices of the Speaker of the Legislature. The Chairman of the Committee on Rules assigns Bills to one or more Committees for consideration. At the discretion of the Chairman of the assigned Committee, a Bill may be scheduled for a public hearing, during which comments from other interested parties in the government and the public at large are solicited. The Committee may then modify the Bill, based upon the comments received and their own assessments, and prepares a report for presentation to the entire legislative body if it feels that the Bill is of merit. Generally, a Bill will not go forward to the entire Legislature without the benefit of a public hearing, but there have been exceptions.

Once a Bill is passed by a majority vote of the Legislature acting in Session, it is forwarded to the Governor for approval or veto. If the Governor signs a Bill as “vetoed,” it is returned to the Legislature for their further consideration, and may be passed into law over the Governor’s veto with an affirmative vote of no less than two-thirds majority. If the Governor signs a bill as “passed,” or if the Governor takes no action for a period of ten consecutive days (excluding Sundays and legal holidays), it becomes law immediately.

### *Executive Branch*

A Governor of Guam is selected by general election every four years, and campaigns for office with a Lieutenant Governor who holds the same term. An individual may not serve longer than two consecutive terms as Governor, but may hold an additional term in office after being absent from the post for a period of four years. The Governor has administrative control over a Cabinet comprised of the Directors and Administrators of some 65 departments and agencies of the government of Guam. Upon inauguration, the Governor appoints these Directors and Administrators to their posts, but such appointments must be approved by the Legislature; such approval is rarely withheld.

Through this structure, the Governor of Guam has administrative control over all executive actions by the government, and oversees the work of the government in providing services to the population.

The Governor is also responsible for preparing and proposing an annual budget for the government for the approval of the Legislature. This budget is based upon the expected revenues of the government, from whatever sources, and is allocated among the agencies and programs of the government in line with the policies of the Governor. However, there are some restrictions on the latitude of the Governor in preparing the budget, as some sources of revenue are designated for specific uses; there are also concerns regarding the distribution of personnel and skills among government agencies.

In order to supplement the revenues of the government and to amortize the costs of major infrastructure projects, the Governor is also authorized to incur debt on behalf of the government, with the advice and consent of the Legislature. However, this authority is limited in the Organic Act to be no more than ten percent of the appraised value of real property in Guam.

### *Judicial Branch*

Matters of U.S. federal law are decided in Guam by the U.S. District Court of Guam. The lone Judge in the District Court is appointed by the President of the United States and approved by the U.S. Senate. The position is held in perpetuity unless the Judge accepts an appointment in another Court, retires, resigns or is impeached. Decisions of the District Court of Guam may be appealed through the U.S. Court system to the Ninth Circuit Court of Appeals, and further, to the U.S. Supreme Court.

The local Court system in Guam is comprised of a lower and an upper Court. The lower Court, the Superior Court of Guam, is the Court of original jurisdiction for all matters arising under the laws of Guam. It is comprised of seven (7) Judges, each appointed by the Governor and approved by the Legislature. Once their appointment and performance on the Bench is affirmed by the electorate in the first general election after a seven-year term, they are entitled to retain the position in perpetuity.

The upper court, the Supreme Court of Guam, was just recently formed. It serves as the first Court of appeals for decisions rendered by the Superior Court. If it were a State Court, subsequent appeals would go directly to the U.S. Supreme Court. However, in authorizing the Supreme Court of Guam, the U.S. Congress saw fit to provide a period of 15 years during which such appeals would first be presented to the Ninth Circuit Court of Appeals. The three (3) Justices of the Supreme Court of Guam are also appointed by the Governor of Guam with the consent of the Legislature.

### **Rule of Law**

In accordance with the American system of government and the limited protections accorded to the people of Guam by the U.S. Constitution, all actions of the government of Guam toward the people are governed by the rule of law. In essence, no individual may be deprived of life, liberty or property without the due process of law. No capricious action or frivolous prosecution against an individual is permitted, except as in accordance with existing statute.

The rule of law helps to control the actions of the government with regard to its citizens. It also allows those citizens to be expressly aware of their roles, rights and responsibilities within the community so that they can adhere to the pursuit of their own interests without conflicting with the common good.

The rule of law, therefore, provides a level of certainty regarding governmental response to individual actions. This certainty supports stability and continuity within the economy and the community.

## **Strictures**

Ultimately, all actions taken by the government of Guam are subject to oversight and control by the U.S. federal government. The laws duly passed by the Guam Legislature are subject to unilateral repeal by the U.S. Congress. The decisions of the Guam Judiciary may be appealed to the U.S. Court system. Ultimately, both the U.S. Courts and the U.S. Congress have the authority to override decisions made by the Governor of Guam. Thus, Guam's internal self-government is limited by being subject to U.S. federal government consent.

Further, the rights accorded to the people of Guam as individuals are limited by the narrow application of the U.S. Constitution to Guam. Many of those rights extended to U.S. citizens in the States are not extended to U.S. citizens residing in Guam. Without discussion of the distinction between the statutory citizenship granted to the inhabitants of Guam and their descendents by the Organic Act and the constitutional citizenship awarded to individuals born in any of the 50 States, some rights are not available simply by the fact of residing in Guam. Perhaps the most evident of these is the right to vote in presidential elections. Regardless of whether one is a statutory or constitutional citizen, that right is not available to Guam residents. There are a number of other rights that are similarly withheld.

## **Industry**

The physical, demographic and legal characteristics of Guam combine to form a unique economic environment that is quite different from both developed nations and most less-developed places. In contrast to the United States, for instance, Guam has a relatively small, resource-poor, unindustrialized and open economy, whereas the United States boasts a large, resource-rich, industrialized and relatively closed economy.<sup>19</sup> As a result, most of the standard models of economic behavior and performance do not accurately describe the island's environment. The history of the island's economic development has also played a role in this, if for no other reason than that Guam moved from an agrarian society that was largely based upon barter before World War II to a service-oriented economy shortly after the War. There was no intervening industrial revolution.

## **Public Sector**

As is common throughout the U.S. territories, the emphasis of those administering Guam has been upon the development of a compatible political and governmental system to accommodate the U.S. military presence, rather than to build a viable economy for the people of Guam. As a result, there has been a concentration in building a strong and elaborate governmental bureaucracy at the expense of a productive private sector. Indeed, during the first

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<sup>19</sup> With reference to "open" and "closed" economies, most of Guam's economy is extremely dependent upon cross-border trade ("open"), whereas the U.S. is far less dependent ("closed").

part of the 1980s, government employment accounted for more than half of the total number of civilian jobs filled in Guam.<sup>20</sup>

Within the public sector, U.S. federal employment declined sharply as the Vietnam War ended, but the government of Guam provided more than half of the public sector jobs even before that time. With the base closures pursuant to BRAC '93 and '95,<sup>21</sup> U.S. federal employment resumed its decline, and will continue under the so-called "A-76" privatization of many civilian roles in support of military activities in Guam.

While U.S. federal employment has gradually declined over the past 25 years, government of Guam employment has continued to increase. From the fourth quarter of 1983, around the time of the end of Guam's previous recession, the local government added an average of approximately 360 jobs annually to its payrolls, with a spurious peak of 16,980 during the second quarter of 1998 in the wake of Super typhoon Paka. (Government of Guam payrolls have since returned to 13,540 as of the fourth quarter of 1999, and are expected to fall significantly below that level because of the early retirement and "buyout" programs at the end of that quarter.)

In any case, this dedication of a substantial portion of the island's scarce human resources to public administration functions has hampered the formation of a strong system of private enterprise, and to some extent continues to do so by diverting labor from private employment. Even more significant, though, in terms of the deployment of the island's resources is the relatively small amount of civilian employment now provided on the relatively large amounts of land held by the U.S. federal government.

As of December 1999, the U.S. federal government employed civilians in some 4,530 job positions.<sup>22</sup> Although the Department of Defense was the principal provider of these jobs, there are a number of other federal agencies present, and offices of all three branches of the government. The Executive Branch agencies (other than Defense) engage primarily in regulatory, social welfare and law enforcement activities.

Also as of December 1999, the government of Guam had some 13,540 job positions filled.<sup>23</sup> Although this represents a high proportion of total civilian payroll employment (22.4%), the government of Guam plays several roles that are typically distributed among several layers of government elsewhere in the United States. It handles several functions that are typically reserved to the federal government, such as Customs services; it acts predominantly as the equivalent of a State government, but also handles the tasks usually relegated to counties, municipalities and even school districts. In addition to the industrial pursuits of most other governments, such as education, police and fire protection, health and social services, etc., it also operates Guam's civilian hospital, the power system, water and wastewater systems, and local telephone service. There are, though, many within the community who believe that many of the

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<sup>20</sup> Guam Department of Labor, Bureau of Labor Statistics, various editions of the Current Employment Report.

<sup>21</sup> The set of decisions regarding the disposition of U.S. military facilities rendered by the Base Realignment and Closure Commission.

<sup>22</sup> Current Employment Report, December 1999, Bureau of Labor Statistics, Guam Department of Labor.

<sup>23</sup> Ibid.

services provided by government would be more efficiently and effectively provided by the private sector.

## **Private Sector**

Prior to World War II, Guam's private sector was predominantly engaged in subsistence activities. After the War, and largely due to the destruction or condemnation of much of Guam's land resources by the U.S. government, civilian employment was transformed quickly into public administration jobs. The enormous buildup of the military establishment in Guam demanded the services of large numbers of non-military support personnel, and jobs were offered at wage rates that were attractive relative to what was available in the private sector. There were, though, several enterprising individuals who started small scale businesses to meet the needs of off-duty military personnel and civilians alike, primarily operating grocery stores, barber shops, restaurants, laundries and saloons. There were several other businesses, as well, but government employment dominated Guam's economy until the late 1960s.

Simultaneous with the lifting of security clearance requirements for travel into and out of Guam in 1962, the massive base construction projects ended and a Chamorro civilian Governor was appointed for the first time. Employment and military spending in the local civilian community decreased rapidly, and a serious recession was eminent when Typhoon Karen struck the island. Federal assistance in recovering from the devastation of the storm renewed some of the injection of funds that had been previously lost and gave the island's civilian government time to prepare the way for private economic development. The military action in Vietnam brought a return of military spending and some additional civilian employment during the late 1960s and on into the 1970s, but tourism had become an important source of income for Guam by 1972. Many attempts to establish light manufacturing industries failed between the late 1960s and late 1970s, though, in part because of changes in the application of Customs regulations by the United States, where Guam's finished products were to be sold.

The rapid growth of tourism suddenly slowed because of the international oil crisis in the early 1970s, and the island economy was heavily impacted by the resulting worldwide inflationary recession by 1975. The end of hostilities in Vietnam and the resulting decline in federal spending compounded the effects on Guam's civilian community.

In 1976, Typhoon Pamela hit the island. Just as had happened after Typhoon Karen, U.S. federal relief funds again flowed into Guam, helping the community to recover from the storm. These funds also helped to create jobs and provide a source of external earnings to pay for the importation of goods and materials. Once recovery from Pamela was complete, though, the Guam economy entered a prolonged and serious recession that lasted until the mid-1980s. During the latter part of this period, government employment dominated the economy, with more than fifty percent of the jobs once again provided by the public sector.

Three events combined in the mid-1980s to suddenly accelerate Guam's economic growth to an impressive rate:

1. The price inflation in the United States and correspondingly high Dollar-based interest rates that plagued the country during the late 1970s and early '80s had been overcome.

2. Growing alarm in the United States regarding a large and rising trade deficit with Japan led to official U.S. admonitions for Japan to modify its trade practices in order to support a more equitable balance.
3. An agreement among the United States, West Germany and Japan led to the revaluation of the Yen. Although the target exchange rate was ¥180 per Dollar, the conversion factor went from ¥245 per Dollar to ¥120 per Dollar in a relatively short time.

Although these three events are related in several ways, they impacted Guam simultaneously in distinctly different ways. With regard to the first event, the stabilization of the value of the Dollar precipitously lowered the risk of investing in Dollar-valued assets; the uncertainty of runaway inflation was gone. The confidence of businesses and consumers alike was raised, and the resulting optimism about the future returned to the U.S. as a whole, including Guam.

The second event forced Japan into action, but in an unexpected way. In addition to taking a number of dubious steps to liberalize trade with the U.S., Japan took another, more controversial step, as well. In the mid-1980s, there was a sudden and enormous surge of Japanese overseas investment into the United States. With Dollar-based interest rates at low levels, Dollar-based investment became quite attractive. Guam was an unlikely beneficiary of these funds, but with a growing reputation as a tourism Mecca for young, suddenly “Dollar-affluent” Japanese travelers, the island became a virtual magnet for substantial investment from Japanese corporations. In the late 1980s, Guam had the distinction of being third on the list of jurisdictions into which Japanese investments were being made, behind California and Hawaii.

The third event, the revaluation of the Yen, had an immediate and profound effect on Guam’s economy. The tourists in Guam’s target market were suddenly spending more than twice as many Dollars on the island during a typical three-day and four-night stay. Dollar-based prices seemed an incredible bargain to Guam’s Yen-oriented visitors. Adding to the economic frenzy was the fact that the number of visitor arrivals was increasing at a compound rate approaching twenty percent in the late 1980s.

The culmination of these three events was a huge economic boon to Guam, with rapid increases in *per capita* income and employment, soaring wealth and property values, and stunning improvements in general standards of living and the public infrastructure. All of this occurred in an environment of relatively stable prices, so that real rates of growth in the economy (by almost any measure) approached and exceeded 20% *per annum* by 1990. Over the period from 1984 to 1991, standards of living in Guam more than doubled, rising above those of several States in the U.S. for the first time.

With the expansion of economic activity and corresponding income in the latter 1980s came a surge of growth in Guam’s private sector. As of the fourth quarter of 1983, there were a total of 15,680 jobs filled in Guam’s private sector, just 49.49% of the total Payroll Employment of 31, 680. By the end of 1991, just eight years later, Guam’s private sector provided 47,160 jobs, 70.51% of total Payroll Employment and more than three times the 1983 level. Business income, profits and taxes rose at similar rates during the period. In the span of thirty years, since the beginning of the 1960s, Guam’s private sector had grown from being virtually nonexistent, in terms of its contribution to the overall economy, to being unquestionably dominant.

Then, the speculative “bubble” in Japan’s securities and real estate markets collapsed in 1990. When the Nikkei stock average and land values in Tokyo fell precipitously, the flow of investment funds into Guam was suddenly cut off. Several ongoing investment projects were scaled back severely; others were simply abandoned. The economic boom that the people of Guam had enjoyed during the late 1980s came to a halt in a matter of a few months. Although there has been some investment into Guam since that time, most notably in retail facilities and in non-hotel tourist facilities, much of the funding has come from the U.S. and South Korea rather than Japan. In any event, the level of investment has been much lower than it was during the boom years.

Fortunately, Guam’s economic boom in the 1980s was primarily based upon investment in physical structures that formed the foundation for permanent jobs. From 1991 through 1997, payroll employment and the level of income remained relatively flat, not growing, but not declining appreciably, either. Rather than a recession, Guam experienced economic stagnation, and the private sector remained relatively healthy. That has changed in recent years, though, as the economy in Japan has deteriorated further. Visitor numbers fell off somewhat, but visitor spending fell faster; many marginal businesses simply could not survive.

Other factors were important, as well. The May 11, 1995, opening of K-Mart, a huge discount store, near Guam’s tourism district proved to be more competition than many smaller existing firms could survive, and many went out of business. For a while, an expanding number of visitors from South Korea helped to offset the declines in both passengers and spending from Japan, but the controversy surrounding the August 6, 1997, crash of a Korean Airlines jet brought an abrupt end to that relief. The unemployment rate, which had been rising gradually since 1991, started to rise more quickly, and the level of payroll employment began to fall.

In December 1997, Super typhoon Paka struck Guam with incredibly powerful sustained winds. Recovery from the devastation took months, and the island received a temporary reprieve from growing recessionary pressures as several thousand jobs were created by the inflow of disaster relief funding. The situation was remarkably similar to the events following Typhoon Karen in 1962 and Typhoon Pamela in 1976. In the wake of the storm, the government of Guam added approximately 2,400 jobs to its payroll, causing a surge in payrolls overall that lasted for more than six months. The private sector, though, has experienced a decline in payroll employment consistently since the end of 1997, and jobs in the public sector have been decreasing since June 1998.

The relative size of Guam’s private sector has also decreased since Typhoon Paka, as private sector jobs have disappeared far more quickly than jobs in the government. The government of Guam provided only 18.93% of the jobs in Guam during the last quarter of 1991, at the very end of Guam’s long, strong economic expansion. Since then, at its peak in June 1998, the local government provided 24.92% of all civilian jobs on the island, and has averaged 22.92% of all jobs since Typhoon Paka. In contrast, the private sector hit a peak of 72.65% of all jobs during the second quarter of 1992, but closed 1999 at just 70.10% after having fallen to a low of 67.68% in the second quarter of 1998. If it were not for the fact that the U.S. federal government has been drastically reducing its civilian payrolls in Guam since mid-1993, the relative position of the private sector within the economy would appear even worse.

Overall, Guam has developed a very healthy private sector over the past twenty years, contributing virtually all of the growth that the economy has experienced. Despite the recent

recession, private activity remains at a level similar to 1990, which was considered a very good year. However, continuing growth in the population has led to a deterioration in standards of living since the early 1990s.

## **Gross Domestic Product**

Guam’s Gross Domestic Product (GDP), referred to locally as the “Gross Island Product” (GIP), is intended to measure the total value of all final productive output within the community during a given year. Unfortunately, the systematic collection of economic data within Guam is less than perfect, so this figure has to be estimated using a model of how the economy functions. Thus, the figure is subject to two primary sources of error: first, there is the potential for error in the model itself; second, there is the potential for error within the actual data measurements that the model relies on in making its estimate. As a result, the estimate can be assumed to be somewhat inaccurate.

Estimates of Guam’s GDP exist for the early 1970s and the mid-1990s. These segments of data are based upon different methodologies, but there is no reason to expect either method to be less reliable than the other in deriving a measure of this type. In the early 1970s, Guam’s GDP was in the neighborhood of \$500 million annually; in the latter half of the 1990s, it has hovered around \$3 billion. Roughly 40% of this output is now generated by the tourism industry and related activity, whereas far more than half of GDP was attributable to U.S. military activity in the early 1970s.

## **Employment and Unemployment**

### **Labor Force**

The composition of Guam’s civilian labor force is unique, largely because of the relatively free flow of inbound and outbound worker migration combined with the immigration environment of the island. The most recent ethnicity information available is derived from the 1990 Census of Population and Housing<sup>24</sup>; although this information is dated, it nonetheless provides a general image of the workforce in Guam. Of a total working age population of 90,990 measured by the census, 34.8% were Chamorro, 24.6% Filipino and 16.3% Caucasian; the remaining 24.3% were of other single or multiple ethnicities. The total labor force at the time (including military personnel) was 66,138 and included 30.6% Chamorros, 24.6% Filipinos and 19.5% Caucasians; the remaining 25.3% were of other ethnicities.

The age distribution of the labor force in 1990 was as follows:

16 to 19	20 to 24	25 to 34	35 to 44	45 to 54	55 to 64	65 and over
6.9%	17.7%	31.6%	23.1%	12.1%	6.7%	1.9%

Source: U.S. Bureau of the Census 1990 CPH-6-G, “Social, Economic and Housing Characteristics: Guam,” Table 42.

<sup>24</sup> U.S. Bureau of the Census 1990 CPH-6-G, “Social, Economic and Housing Characteristics: Guam,” Table 60.

On average, from June 1980 to June 1999,<sup>25</sup> Guam's labor force has grown at an average annual rate of approximately 3.89%, a rate higher than the civilian working age population, at 3.44%. Employment, on average, increased by 3.60% annually during the period. There have been changes in the composition of the labor force over time. A higher proportion of women has entered the working world (60.82% in June 1999 compared to 52.15% in June 1980). The average age of participation has increased by approximately 2.7 years (from approximately 36.19 years to 38.91). However, the labor force participation rate declined for males in all age groups during the period, whereas it rose for females in all but the 16 – 17 year age group. Overall, Guam's labor force participation rate is high by U.S. standards, measured at 69.1% in June 1999 compared to the U.S. total of 67.7%, even as the U.S. economy is booming and Guam's economy is in recession.

Guam's civilian labor force in June 1999 consisted of 72,700 people, 61,640 of whom were employed, for an unemployment rate of 15.2%. Unemployment among men was higher (15.8%) than among women (14.5%). Teenagers aged 16 to 19 years old had the highest unemployment rate of any age category, at 47.8% (males: 48.6%; females: 46.9%). The lowest unemployment rate was among workers 35 years of age and older (11.4%).

## Industries and Occupations

The 1990 Census of Population and Housing provides the most recent reliable information regarding the breakdown of both the employed and unemployed labor force by industry and occupation, and also allows general conclusions regarding the match between the skills of the labor force and the demands of industry. Overall, even during a period of high employment (as in 1990), Guam's labor force was well matched to its industry. Of those 2,042 within the civilian labor force of 54,186 who were unemployed, 552 (27.0%) had recently entered or reentered the labor force after an absence of more than five years; the unemployment rate among the recently employed was just approximately 2.75%.

By industry, the breakdown of employment was as follows:

<b>Industry</b>	<b>Civilian Labor Force</b>	<b>Employed</b>	<b>Unemployed</b>	<b>Percent Unemployed</b>
Agriculture	450	436	14	3.11%
Forestry & fishing	78	77	1	1.28%
Mining	57	55	2	3.51%
Construction	8,196	8,023	173	2.11%
Manufacturing	2,383	2,302	81	3.40%
Transportation, communication & public utilities	5,700	5,603	97	1.70%
Wholesale trade	1,632	1,584	48	2.94%

<sup>25</sup> This period is used for comparison because the two endpoints were during similar phases of the business cycle.

Retail trade	10,420	9,959	461	4.42%
Finance, insurance & real estate	2,836	2,767	69	2.43%
Business services	1,232	1,176	56	4.55%
Repair services	868	834	34	3.92%
Personal services	3,952	3,829	123	3.11%
Entertainment & recreation	1,168	1,124	44	3.77%
Professional & related services	8,866	8,677	189	2.13%
Public administration	5,776	5,698	78	1.35%

Source: U.S. Bureau of the Census 1990 CPH-6-G, "Social, Economic and Housing Characteristics: Guam," Table 77.

Similarly, the breakdown of the civilian labor force and employment by occupation shows that, in general, Guam's workforce was reasonably well matched to the demand for skills within the community. It is clear, though, that unemployment was highest among those occupations requiring less formal skills training.

The occupational breakdown from the 1990 Census is summarized below:

<b><u>Occupation</u></b>	Civilian Labor Force	Employed	Unemployed	Percent Unemployed
Managerial & professional	12,282	12,108	174	1.42%
Technical, sales & administrative support	16,844	16,341	503	2.99%
Service	8,592	8,255	337	3.92%
Farming, forestry & fishing	643	610	33	5.13%
Precision production, craft & repair	8,984	8,831	153	1.70%
Operators, fabricators & laborers	6,287	5,999	288	4.58%

Source: U.S. Bureau of the Census 1990 CPH-6-G, "Social, Economic and Housing Characteristics: Guam," Table 76.

As the economy has receded during the 1990s, it is likely that the match between Guam's labor force and the available jobs, both by occupation and industry, has become less appropriate. However, in the absence of reliable information regarding this match, it can only be assumed that the skills and occupations supporting those industries that have remained most stable maintain a correct match, while those supporting industries that have suffered most from the recession have experienced the highest rates of unemployment. There is, though, one exception to this general rule: because Guam's construction industry relies on temporary alien laborer under the U.S.

Immigration and Naturalization Service's "H-2" visa category, unemployment in the occupational categories that support that industry should not parallel the decline of total payroll employment in the industry. As employment in the construction industry declines, it is generally the H-2 workers who are laid off first, and they return to their homelands without contributing to Guam's unemployment. Their departure does, though, reflect a decline in Guam's GDP, and reduces incomes through the multiplier effect as applied to declining payrolls.

## **Trends**

Over the years, Guam has adopted industries that tend to be service-oriented. From early attempts in the 1960s and 1970s to develop light manufacturing through the formation of a successful tourism industry, more and more of Guam's economic attention has been concentrated on the services, as broadly defined.

As noted, there has been a trend toward a higher labor force participation rate, and an even stronger trend among women to join the mainstream working world. The average age of the workforce has increased, as has the average age of employment. There is a greater emphasis on labor skills than ever before. As time progresses, it is likely that these trends will continue, but that they will eventually stabilize in a new structure of employment within the economy.

This raises a crucial point with regard to the future of Guam's economy as the impact of communications technology causes revolutionary changes in the world economy. Geographically, Guam is in a position to exploit enormous advantages in the "new economy," but without the availability of jobs in the information industry, there is little motivation for the island's youth and workers to accumulate the necessary skills. Without a base of skilled workers, though, it will be difficult for Guam to attract the investment required to take advantage of its location. While the island has sufficient technical workers to provide for its internal needs and support some trade in communications services, additional skilled members of the labor force will be required to meet potential future demands.

## **Income and Prices**

### **Income**

Direct measurements of income in Guam's economy are not available. The best available estimate is derived from a model assembled by the KPMG Peat Marwick Policy Economics Group in 1994. It uses a fairly simple estimation technique based upon fundamental principles of economics, and has had mixed success in short-term forecasting. In terms of data that would be useful in income measurement, the Guam Department of Revenue and Taxation has the best available information, but does not regularly use those data for that purpose, and so does not compile them in the necessary format.

There was a study conducted in 1989 at the Department of Revenue and Taxation by Mr. John D. Gilliam to estimate the level of "Gross Territorial Income" for 1988. It concluded that the total income generated by economic activity in Guam was some \$2.55 billion in 1988, distributed as follows:

Income Retained by Guam Military Commands	\$310,155,913
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Income Earned by Guam Civilian Hosts of U.S. Military	494,880,564
Other (than federal) Income Earned by Guam Individuals	562,761,367
Other (than federal) Income Earned by Guam Business Corporations	448,790,667
Income Earned from Guam by Rest of the World	<u>730,938,234</u>
<b>GROSS TERRITORIAL INCOME</b>	<b><u>\$2,547,526,745</u></b>

Source: John D. Gilliam, "Gross Territorial Income (GTI): Guam, 1988," Agaña, Guam, 1989.

While the accuracy of the figures in the report is open to debate, the estimate of total GTI is reasonably similar to the estimates derived from the KPMG model a few years later.

Mr. Gilliam, in his role as Senior Economist at the Department of Revenue and Taxation, also conducted research into the distribution of personal income in Guam for tax years 1989 and 1990, based upon income tax filing data. The unpublished results of his research indicate a fairly wide and growing disparity between the incomes of high and low earners; this subject has been a topic of discussion in some segments of the community in recent years, as have disparities in the distribution of wealth.<sup>26</sup> Unfortunately, the research is dated and has not been replicated in recent years, so there is no current detailed analysis of Guam's distribution of income and wealth available. Other data are available from the Bureau of Labor Statistics of the Guam Department of Labor, but broad and variable income categories make time series comparisons inconclusive.<sup>27</sup> However, casual observation and deductions that can be drawn indirectly from other sources of information indicate that the trend toward an increasingly unbalanced distribution of income continues.

## Prices

There is one word commonly used to describe prices in Guam: "high;" if two words are used, they are "very high." Although direct comparisons of the overall cost of living on the island with other places are somewhat arbitrary, comparison item for item places that cost somewhere near Honolulu, Hawaii, or Washington, D.C., among the highest-cost U.S. jurisdictions.<sup>28</sup> The principal reason for high prices in Guam is that the majority of the goods consumed must be imported, either aboard ships or aircraft. Not only does the transportation cost add to the cost of goods sold in Guam, the additional handling at the ports at both the exporting and the importing ends contributes to the landed cost. Further, Guam's remote location necessitates higher levels of inventories to accommodate transportation delays. This

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<sup>26</sup> This conclusion is supported by the 1980 and 1990 Censuses of Population and Housing, which actually showed the median *per capita* level of income declining from \$14,015 in 1980 to \$13,895 in 1990, while the mean *per capita* level of income increased from \$16,642 to \$18,007. The "median" represents the middle of the distribution, with half of the population below and half above; the "mean" represents the arithmetic average, the sum of all individuals' income, divided by the number of individuals. The declining median figure indicates that more people are concentrating in low income groups, while the simultaneously rising mean indicates that the incomes of those with higher levels of income are advancing inordinately rapidly.

<sup>27</sup> "Per Capita and Household Income on Guam [various years]", Bureau of Labor Statistics, Guam Department of Labor.

<sup>28</sup> [Get U.S. federal COLA data for this.](#)

leads to substantial additional warehousing and storage facilities, with their associated costs of rental, insurance, utilities, handling and the inevitable spoilage or obsolescence.

With some 155,000 people, Guam is a relatively small community, so goods are imported in fairly small lots; volume discounts, while available, are not as sizeable as in larger communities. Costs of goods shipped from the United States may also be artificially inflated by high freight rates aboard U.S. flag vessels, since Guam is considered to be within the “coastwise trade” of the States.<sup>29</sup>

As an isolated community, Guam also requires internal redundancy that would not be necessary in larger geographic locations. For instance, Guam must have all of the excess capacity in power generation needed to continue meeting load demand in the event of a generator failure; other U.S. jurisdictions have the luxury of being able to tap into the generating capacity of surrounding communities through a power grid. Because of Guam’s redundant systems, infrastructure costs are inordinately high.

As mentioned earlier, construction costs (and therefore building purchases and rentals) are higher in Guam than most other locales because of the frequency and force of earthquakes and tropical cyclones. In addition, though, there are other environmental factors that affect living costs in Guam. Termites and other destructive pests reduce the useful life of wood products and make local production of food crops more difficult and costly; the salt borne by moisture in the air causes iron products to rust more quickly; intense ultraviolet rays from the tropical sun affects the durability of paints and plastics. Mortgage lenders’ requirements that borrowers provide typhoon and earthquake insurance add to recurring costs. Guam’s pleasant climate does have its drawbacks, and living in this “tropical paradise” has its price.

Added to the foregoing elements is the fact that, operating in a small community, there is less business competition in Guam than in larger communities, particularly in the retail, wholesale, energy and transportation industries. While there are only a very few unregulated monopolies on the island, many businesses are able to command a premium price in the market for their products because there are limited alternatives. Therefore, profits tend to be higher than in other, larger communities, and this feeds a cycle in which efficiency is reduced. This may be a factor in the rising disparities in income and wealth mentioned in the previous section.

Guam’s Department of Commerce has generated a Consumer Price Index (based upon U.S. Department of Labor methodology) quarterly since 1972. The underlying data series was updated in 1978, but then allowed to continue without updating until the mid-1990s before it was revised to reflect further changes in consumption patterns. Although Guam has a U.S. Dollar-based economy, unpublished research by the author has detected no significant short- to intermediate-term correlation between inflation in Guam and in the United States. This is undoubtedly due to the combination of Guam’s high reliance upon imports from foreign nations,

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<sup>29</sup> The so-called “Jones Act” is a part of U.S. maritime law that requires that cargo, passengers and baggage transported between two successive U.S. ports must be carried aboard U.S.-registered vessels. These vessels, in turn, must be U.S.-hulled in order to gain U.S. registry, meaning that they are built in U.S. shipyards by costly U.S. labor. Historically, there has also been an issue surrounding the “Guam Rate Agreement” (No. 8454) under which the Federal Maritime Commission effectively allowed U.S. carriers to fix rates in the U.S.-Guam trade without justification or regulatory oversight. It has been alleged that this Agreement was abused, and that the U.S. carriers subsidized rates on their international routes at the expense of the people of Guam through higher shipping charges. There is substantial data and research to support this allegation.

shifting among sources of products and fluctuations in exchange rates over time. It is certain, though, that the rate of inflation in Guam and fluctuations in that rate have historically been of greater magnitude than it has been in the States.

On average, since the early 1970s, the level of consumer prices in Guam has roughly doubled every eight years. Then, suddenly, in the mid-1990s (coincident with the introduction of a revised Consumer Price Index), prices stabilized. Whether this is due to the ongoing recession, the establishment in Guam of high-volume retail outlets, the low rate of inflation in the United States, or these in combination with other factors is unclear. However, over the course of the past four years, inflation in Guam (as measured by the revised CPI) has been virtually non-existent.

## **Transportation**

### **Land**

Guam has a system of some 607 linear miles of public roadways of various types. These include 61 miles of main arteries, 68 miles of secondary arteries, 41 miles of collector roads and 437 miles of village streets.<sup>30</sup> Most of these roadways are well-traveled by the 100,000-plus licensed motor vehicles on the island,<sup>31</sup> and they provide transportation in Guam's population centers and around the perimeter of the island, as well as across the center part of the island. The condition of the roadways is generally moderate to excellent, although maintenance could be improved. On average over the past ten years, Guam has received \$14 million annually from the federal government for their expansion and improvement. These funds add to the average \$21 collected under the liquid fuels tax, which are dedicated to roadway construction and maintenance.

The government of Guam provides a public transportation system under the auspices of the Guam Mass Transit Authority. The GMTA receives approximately \$400 thousand annually in federal funding to help support its operations.

U.S. Federal Motor Vehicle Safety Standards, as adopted by the local government, apply to vehicles imported into Guam. However, the FMVSS and U.S. National Highway Traffic Safety Standards are not fully enforced in Guam during the annual vehicle safety inspection process.

### **Sea**

Guam's excellent deep-water seaport at Apra Harbor provides a cargo lifeline for the community. It is also a transit point for shipments to the other islands of the Marianas and the Federated States of Micronesia, and for fish from the FSM destined for Asia. Cargo arrives in Guam primarily aboard containerized vessels, although there is some breakbulk traffic into the island and motor vehicles typically arrive on roll-on, roll-off craft. The civilian port also has the capacity to handle bulk liquid fuel shipments. The Port Authority of Guam is a self-sufficient,

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<sup>30</sup> Guam Department of Public Works, Office of Highway Planning.

<sup>31</sup> Guam Department of Revenue and Taxation, Division of Motor Vehicles. Data for 1997, as published in the Guam Department of Commerce "Guam Annual Economic Review – 1997-1998," Table PT1.

autonomous agency, and receives no funding from the government of Guam or the federal government.

Vessels arriving in Guam are subject to the U.S. Coast Guard standards of safety and US environmental and OPA90 standards (because Guam is the only port in region requiring these latter standards, the availability and cost of charter transport into Guam are adversely affected). The result of applying these stringent controls is that only more costly vessels from Asia that meet the standards are allowed into Guam's port, marginally increasing landed costs. More significant are the costs associated with the Jones Act, mentioned previously, that results in most shipments into Guam from U.S. sources carrying a disproportionately high freight charge. Nevertheless, Guam benefits in several ways from the federal regulation of shipping, primarily in terms of safety. In addition to the enforcement of safety regulations in the waters surrounding Guam, the Coast Guard provides emergency assistance to vessels (including small craft) and helps to protect Guam's shorelines from being compromised.

## **Air**

Air transportation is a fundamental requirement of a remote population center the size of Guam, particularly in light of the dominance of tourism in the island's private sector. The primary civilian air field, operated by the Guam Airport Authority at Tiyan, has a well-maintained 10,000 ft. runway to accommodate all but the heaviest aircraft. This airfield, formerly Brewer Field of Naval Air Station - Guam, was returned to civilian control in the mid-1990s as part of the U.S. military's realignment proceedings. Because of environmental provisions and other concerns, the transfer of the airfield and its attendant properties is an ongoing process, so there are still several constraints on the use of the surrounding properties for commercial purposes.

With the exception of air traffic control, which is conducted by the Federal Aviation Administration (FAA), all facilities at the civilian airport are operated by the local government. The federal government provides no funding in support of the airport's operations, but the U.S. Department of Agriculture controls plant and pest quarantine activities at the airport. However, the new air terminal was built in anticipation of continuing rapid growth in Guam's tourism industry, and until that materializes, the costs of operating the airport on a per-passenger basis are quite high. Some of these costs are passed on directly to passengers through a users fee, but most are covered by charges to the airlines serving the island.

The FAA controls all air traffic in Guam, whether civilian or military, through an arrangement with a civilian subcontractor. This activity is funded by the federal government. None of these costs are recouped by the FAA, and the services are provided to Guam free of charge.

## *Passengers*

The Guam International Air Terminal processes some 3.1 million in- and out-bound passengers each year. Approximately 77% of these passengers are tourists, while the other 23% are Guam residents, business travelers or transit passengers.<sup>32</sup>

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<sup>32</sup> Source: Guam International Airport Authority and Guam Visitors Bureau.

Each departing passenger on international flights is subjected to security screening by the airlines, as required by U.S. federal regulation. Each arriving passenger is inspected by the Immigration and Naturalization Service of the U.S. Department of Justice, as well as by officers of the Guam Department of Customs and Quarantine. This latter agency receives intermittent funding from various U.S. federal government programs, including a share of funds generated by seizures of property in cooperation with the U.S. Drug Enforcement Administration, but no recurring federal support.

### *Freight*

Air freight into and out of Guam has become a significant secondary source of revenues for the Guam Airport Authority. High-value, low-bulk shipments arrive in Guam daily, and fresh/frozen fish are shipped frequently to markets in Japan. Gross local and U.S. federal funding for the operations of the airport also helps to support this cargo movement.

## **Communications**

### **Telecommunications**

Voice and data communications in Guam are primarily conducted in the form of broadcast and telephonic communications. The Federal Communications Commission regulates these two categories of telecommunications. A single, unregulated cable television network also serves the island.

#### *Broadcast*

Guam is served by 3 commercial AM radio stations and 5 commercial FM stations, two FM stations sponsored by religious affiliations and one non-profit public radio station. The island has two broadcast television stations.

#### *Cable*

The only cable television network in Guam has some 42,000 subscribers, and operates as one of the island's few unregulated monopolies following the uncontested purchase of its sole competitor.

#### *Telephone*

#### *Local*

Local landline telephone service is provided by an autonomous agency of the government of Guam. It provided 27,300 lines to households, 45,200 to businesses and 9,350 to local and federal government offices on the island as of Feb. 2000.<sup>33</sup> The hardware for the system has been modestly subsidized by low-interest loans from the U.S. Rural Electrification Administration, but the debt owed by the Guam Telephone Authority to the REA has inhibited reinvestment and complicated efforts toward privatization.

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<sup>33</sup> According to the Guam Telephone Authority.

There are also 3 companies providing cellular telephone service in Guam along with the Government owned, Guam Telephone Authority. These are also regulated by the FCC.

### *Long-Distance*

Guam recently became a part of the North American telephone system, adopting Feature Group D and falling under the U.S. domestic (rather than foreign) rate structure. This action has substantially reduced the cost of long-distance telephone service for the island's residents. There are 6 long-distance service providers in Guam.<sup>34</sup> Long-distance service into Guam is regulated by the FCC.

### *Other*

Both the U.S. military and the Department of State operate communications facilities in Guam. These are unavailable for civilian use, except in times of emergency.

### **Postal Service**

The U.S. Postal Service operates as the primary postal carrier in Guam. Postage rates charged are standard U.S. rates, providing a significant subsidy to the actual cost of such services in a remote location. However, mailing times from the U.S. to Guam are almost four times as long as mainland delivery times. Mail from Guam to Asia is also delayed, due to processing in Hawaii. The cost of this service is controlled, in part, by limitations on "home delivery" of the mail, and most residents and businesses have a "P.O. Box" or "General Delivery" address.<sup>35</sup>

There are also several, small, private postal services that operate on the island, but their volume of business is inconsequential in comparison to that of the USPS.

### **Courier Services**

Courier Services are provided to Guam by four major outfits (United Parcel Service, Federal Express, DHL and TNT). Courier services are also provided by Brinks for currency and other high-value commodities. These services are considered to be "common carriers" under U.S. law, and are regulated as such.

### **Trade**

#### **Internal Environment**

Internally, Guam operates under the general system of U.S. laws governing trade and commerce. The island has adopted the model Uniform Commercial Code (with minor modifications). The enforcement of contracts, the corporate structure of business establishments and a typical code of business "ethics" are virtually indistinguishable from their counterparts in and among the several States.

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<sup>34</sup> They are MCI, ITE, TNI, GuamCell (GTE), Access Telecom & Startec/PCI.

<sup>35</sup> According to the Guam Postmaster, some 40% of the island's residences and businesses enjoy carrier delivery, while the remaining 60% receive their mail through a Post Office box or general delivery.

The structure of the commercial sector of Guam's economy is also similar to that of the U.S., with tiers of wholesalers and retailers operating to distribute final goods to the consuming public. Whereas prior to World War II Guam had a significant level of barter in its trade structure, that transformed rapidly into a cash economy during the 1950s and has continued in that mode ever since. In the process, the economy has evolved from one based upon trade in physical goods to one that is far more concentrated on services.

## Offshore Trade

As a remote island jurisdiction with few native resources and little internal manufacturing capacity, Guam is dependent upon external trade in order to meet the demands of a modern, western economy. Most of the goods consumed in Guam are imported from the outside, with the majority coming from Asia, followed by the United States and the rest of the world.<sup>36</sup> Unfortunately, Guam does not have reliable data concerning the volume or value of trade with the rest of the world. Export data, where available, is mostly indicative of through-trade, with goods being brought into Guam and then transshipped to other islands. The collection of import data is an overwhelming task (given the resources devoted to this process), despite the fact that the United States has adopted the Harmonized System of commodity classification. Although the Guam Department of Commerce adopted rules and regulations nearly a decade ago to require that import documents be properly coded for data collection under the Harmonized System, resistance from the local business community has forestalled the implementation of these regulations. Thus, the collection of reliable trade statistics remains an indefinite goal.

### *Trade with the United States*

As a U.S. jurisdiction, there are a multitude of regulations and requirements governing the types and quality of goods that can be imported into Guam. As a broad example, there are strict provisions applied to food and foodstuffs. As a result, several classes of products must be acquired from the United States exclusively. Whereas these requirements may add to the overall cost of consumption in Guam, they also help to support the health and well-being of the community.

Guam is a beneficiary under General Headnote 3(a) of the Harmonized Tariff Schedules of the United State. This provision allows goods that are *bona fide* products of the island (i.e., having more than 50% of their FOB value added in Guam and foreign imports "substantially transformed" into items of a different nature or character) to enter the U.S. free of duties or tariffs. Although this appears to be an attractive incentive to the formation of light manufacturing firms in Guam, the result has been less than successful in most instances. For instance, although the goods may be *tariff-free*, some are still subject to *quotas*; modification of these quotas can result in the same effect on trade volumes as would tariffs. Further, there were instances in the 1970s when Guam's products languished on the docks in U.S. ports while U.S. Customs agents attempted to determine whether they met the requirements to be eligible for entry under the trade preference provided by Headnote 3(a).

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<sup>36</sup> According to a general assessment conducted by the Guam Department of Commerce.

## *Trade with Other Nations*

Many of the manufactured goods consumed in Guam are imported from Asia and other places. Ironically, a significant proportion of these goods is imported from Asia by way of U.S. ports because of transportation issues. However, most are imported directly into Guam.

A number of countries have treated Guam as a “less-developed place” (LDP) under the Generalized System of Preferences (GSP), a part of the General Agreement on Tariffs and Trade (GATT). This designation would allow preferential tariff and quota treatment of Guam’s *bona fide* products when imported into those places. In reality, though, there is little manufacturing in Guam (aside from fabrications for local consumption), so the economy of the island has realized few benefits from its status under the GSP.

## **Investment Climate**

Historically, the growth path of Guam’s economy closely follows the pattern of outside investment into the island. The economy boomed during the 1950s when the U.S. military was engaged in the extensive development of base facilities, then quickly went into a recession when that buildup was completed in the early 1960s. The first wave of tourism industry investment in the late 1960s and early 1970s supported rapid economic growth, followed by a deep recession in the late 1970s and early 1980s. The overwhelming wave of Japanese investment in the latter half of the 1980s, fed by several factors including Japan’s speculative “bubble,” generated unprecedented sustained growth in the economy for some seven years. The end of that investment in the early 1990s, though, left Guam stagnant, devolving into the recession that it is experiencing today. Acknowledging this pattern, Guam has created an environment that is quite accommodative of outside investment. There are some elements that could be further improved, but overall, Guam has an excellent investment climate.

## **Stability**

In general, Guam’s investment climate is quite stable. This is partially due to the clear resolve of the island’s leadership to maintain consistent rules over time, but it is also due to factors that are entirely exogenous to the island. As a U.S. possession, Guam is subject to a broad range of U.S. laws. These are well-known and widely respected by prospective investors around the globe, who appreciate the mitigation of risks associated with the established rule of law. They have little concern about the possibility of changes in the local business environment undermining the value of their investments, since there are clearly defined procedures for recourse through the Courts.

Guam’s economy is also based upon the U.S. Dollar, the *de facto* standard currency for international trade. This status is derived from the sheer volume of U.S. international trade, as well as the sophisticated monetary policies of the U.S. that are designed to maintain international trade balances in addition to the domestic economic control that is the overriding goal of most national monetary authorities.

Guam’s income tax structure, a mirror of that of the United States, is also familiar to many international investors, and changes slowly enough to add a degree of certainty to investment decisions.

As a U.S. possession, Guam is also defended from foreign aggression by the U.S. military, generally respected as the dominant fighting force throughout the world. This level of security brings with it the perception that Guam is a very safe destination for investment funding.

## **Incentives**

There are innumerable investment incentives offered by the government of Guam in the process of influencing the investment decisions of outside firms that are contemplating overseas investment opportunities and investigating multiple jurisdictions. Beginning with expeditious treatment of prospective investors in providing information about the business climate, through the availability of technical assistance related to financing, to the availability of low-interest loans and substantial tax preferences, Guam does more than most other jurisdictions in support of the investment decision.

The Guam Economic Development Authority (GEDA) was first formed in 1965 with a mission of bringing outside investment to the island. GEDA's principal tool in attracting outside investment is the Qualifying Certificate, a negotiated contractual obligation between the government of Guam and the investor, specifying the type, extent and character of the investment to be made and the tax advantages to be provided in reciprocation by the government. Although all income taxes must be paid by the investor's project in order to be in compliance with the mirror tax code provisions of the Organic Act, up to 75% of these taxes can be rebated by the government for a period of up to 20 years. Property taxes can be entirely abated for a period of up to 10 years, and there is even the possibility of a rebate of up to 75% of taxes on dividend income derived from the project for a period of up to five years during the life of the Master QC.

In addition to the investment incentives provided under the several programs offered by GEDA, some types of investment projects can also take advantage of various types of incentives offered under U.S. federal tax and financing laws, including the issuance of triple tax-exempt debt (i.e., U.S., state and municipal). This provides an incentive, particularly to U.S. investors, though it has not recently been effectively exploited by Guam.

The U.S. Small Business Administration also offers several programs to support new formation and the expansion of existing small businesses. These programs include direct loans, loan guarantees and business development programs.

## **Effectiveness**

In its early efforts to stimulate development in Guam, the U.S. federal and local governments pursued a number of different, nonintegrated paths. From agriculture to light manufacturing to entertainment, anything that could be reasonably conceived to provide a prosperous future was worth exploring. Industries grew and collapsed trying to take advantage of Headnote 3(a). Firms were formed that ultimately had no market for their products. There were many successes, but most were only temporary.

Despite a series of misunderstandings and some controversy over the years, GEDA's programs, and most especially the QC program, have been very successful in attracting investment into the local economy. Given early experience in the tourism industry, it is safe to assume that Guam would not have its current hotel room inventory without tax incentives to help buffer the risks that were involved. Without those hotel rooms, Guam's tourism industry would

not have the stature in the community that it has earned. Without the tourism industry, it is almost inconceivable that the people of Guam would have the relatively high standards of living that they enjoy today.

## **Fiscal Conditions**

The government of Guam has taxing authority in Guam and the ability to raise revenues through fees, fines and levies, as well as other charges for services. Although never used, it also has the implied authority to establish import tariffs on goods arriving from outside the United States.

The government also raises funds for long-term projects, primarily infrastructure development, through its access to the U.S. municipal bond market. Because the interest payments made on these bonds are exempt from U.S. federal income taxes, this debt is typically offered at interest rates that are preferential to the government.

U.S. federal grants and other financial assistance provide another source of funding for local government operations, but these monies are usually earmarked for specific projects or purposes. This source of funding is, however, significant in the government of Guam's annual budget.

Because of the nature of Guam's economy and the magnitude of shifts in the level of activities over the course of the business cycle, the sources of government funding tend to be relatively unstable. Because of the structure of the government's budget, dominated by personnel expenditures and other relatively fixed costs,<sup>37</sup> expenses tend to be much more stable. The mismatch between revenues and expenditures over time has resulted in growing budgetary and accumulated deficits over the course of the stagnation and recession of the 1990s.

## **Tax Structure**

The two principal sources of tax revenues for the government of Guam are the income tax and business privilege taxes. Guam's income tax, established under Section 31 of the Organic Act, currently "mirrors" the federal government's Internal Revenue Code. This is generally accomplished by, ". . . applying as the Guam Territorial income tax the income-tax laws in force in Guam pursuant to subsection (a) of this section [the income-tax laws in force in the United States of America], except where it is manifestly otherwise required, the applicable provisions of the Internal Revenue Codes of 1986 and 1939, shall be read so as to substitute "Guam" for "United States", "Governor or his delegate" for "Secretary or his delegate", "Governor or his delegate" for "Commissioner of Internal Revenue" and "Collector of Internal Revenue", "District Court of Guam" for "district court" . . ."<sup>38</sup> In addition to the funds collected under this tax, all U.S. federal taxes<sup>39</sup> paid into the U.S. federal government by inhabitants of Guam and members

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<sup>37</sup> Personnel expenditures are usually treated as a variable cost in economic models, but both the political aspects of government employment in a small community and the government of Guam Civil Service system cause these costs to be unusually persistent in Guam.

<sup>38</sup> From U.S.C. Title 48, Chapter 8, §1421i(e).

<sup>39</sup> With the exception of the taxes collected under the Federal Insurance Contributions Act (Social Security taxes, Self-Employment taxes and Medicare).

of the Armed Forces who are domiciled in Guam are also paid over to the treasury of Guam under Section 31 of the Organic Act.<sup>40</sup>

Guam's business privilege taxes are comprised of a collection of various excise and *ad valorem* ("value-added") taxes levied upon business activities and receipts. Principal among these is the Gross Receipts Tax (and its parallel on imported items for personal use, the Use Tax), equal to four percent (4%) of the value of retail sales by a firm in excess of \$50,000 annually. In addition, the government of Guam taxes receipts from rental property, insurance premiums, services and a number of other business revenues. There are business privilege taxes levied separately on admissions, hotel occupancy, tobacco and alcohol, liquid fuels and other specialized categories.

A final, minor source of tax revenue for the government of Guam is the real property tax, which generates just over 2%<sup>41</sup> of its annual revenues.

The proportional structure of taxes levied by the government of Guam is as follows:

	<b>1993</b>	<b>1994</b>	<b>1995</b>	<b>1996</b>	<b>1997</b>	<b>Average</b>
<b>Income Taxes</b>	55.68%	53.86%	54.55%	51.74%	52.91%	53.75%
<b>Gross Receipts Tax</b>	25.66%	26.10%	28.98%	29.47%	29.99%	28.04%
<b>Real Property Taxes</b>	1.65%	1.86%	1.98%	3.41%	2.75%	2.33%
<b>Tourist Attractions</b>	2.77%	2.15%	3.25%	4.14%	4.59%	3.38%
<b>Business License</b>	0.43%	0.54%	0.45%	0.45%	0.03%	0.38%
<b>Territorial Highway</b>	4.80%	5.10%	2.41%	2.42%	3.02%	3.55%
<b>Other Taxes</b>	0.90%	0.81%	0.96%	0.78%	0.83%	0.86%
<b>"Section 30"</b>	<u>8.11%</u>	<u>9.58%</u>	<u>7.42%</u>	<u>7.58%</u>	<u>5.88%</u>	<u>7.71%</u>
<b>Total</b>	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%

Because of the variability of business activity and earned income over the course of the business cycle in Guam, government revenues also rise and fall. Historically, the peak in these receipts was in 1997, with total revenues of \$613.8 million.

## **Expenditures**

Because of Guam's remote location and small size, the government of Guam takes on the responsibilities that would normally be distributed among municipal, county and state governments in the 50 States, and even fulfills many of the obligations normally reserved to the U.S. federal government there. There are several ways in which the expenditures necessary to support these activities can be classified, including appropriations by agency, expenditures by

<sup>40</sup> See U.S.C. Title 48, Chapter 8, §1421h.

<sup>41</sup> The average from 1993 through 1997 was 2.33%, as calculated from the Table on page 7 of *1994 – 1997 Annual Report*, Department of Revenue & Taxation, Government of Guam.

functional area of operations, and the division of government funds between payrolls, interest expenses, infrastructure investment, office rental and so forth. Each of these methods of classification would draw its own characterization of government activities and the prioritization of programs that public leaders have set, and provide some insight into the structure of governmental operations. However, information for recent years is difficult to present, since the accounting records are not consistently classified from source to source.

It should be noted that, over time, the funding of some agencies has been curtailed, while that of others has been expanded. There is a multitude of reasons for this, many of which are political and some of which are practical, with changes made in response to changing community needs.

Shifting circumstances have required that more resources be devoted to some areas of governmental activities to effectively meet the needs of society. As time has progressed, some programs have taken on greater importance, while others have successfully addressed their respective issues and are no longer given significant weight in the community's agenda.

Perhaps most telling in the pattern of expenditures by the government is the way in which these expenditures are divided into the kinds of resources, goods and services that they purchase. Payrolls have historically absorbed the overwhelming majority of government expenditures, often to the point where government employees lack the tools and/or materials that they need to successfully do their jobs. However, one of the beneficial results of the expenditure patterns of the government of Guam has been to provide stable, high paying employment for a substantial proportion of the workforce, helping to form a middle class that otherwise might have taken far longer to develop on the island.

### **Accumulated Deficit and Debt**

The government of Guam has historically incurred debt to fund long-term, durable projects, such as utility system expansion and roadway development. Typically, revenue bonds have been issued in U.S. financial markets and purchased by institutional investors such as insurance companies. These bonds have the advantage to the bondholder of being exempt from federal government taxation, and can therefore be sold with a lower yield than comparable private debt. The repayment of this type of debt is from revenues generated by activities and fees associated with the use of the funds (i.e., highway improvement bonds are repaid from the liquid fuels tax).

In recent years, it has become more common for the government of Guam to issue general obligation bonds, which are repaid from the general operating revenues of the government. The proceeds from this debt is often used to fund ongoing operations at a time when government revenues are insufficient to cover general expenditures.

The level of debt of the government of Guam is limited under the Organic Act to ten percent of the appraised value of real property in Guam. While the level of current debt is not reported here because of conflicting information from various sources, it is likely that the level of debt is approaching its statutory limit.

The accumulated deficit of the government of Guam is a less meaningful figure, since it represents funds that have been appropriated by the Legislature but not spent by the Executive branch. In a sense, these are outstanding obligations of the government, but they do not carry the

same weight as an outright debt. Again, the level of Guam's accumulated deficit is not reported here because of conflicting information from different sources, but it is generally believed to be substantial.

## **Federal Funding**

Details of federal funding of programs and operations in Guam are included in Appendix 1. Federal expenditures in the territory are substantial but variable, and under many programs Guam is not treated on a par with the several States. Nonetheless, federal expenditures generate a high level of income and economic activity.

Assessing the impact of federal expenditures is complicated because of the accounting provisions under which they are reported. This is particularly true of military expenditures, since the funds may actually be spent and generate economic activity elsewhere, with only the final product (such as a weapons system or an office desk) being assigned to Guam. In many cases, the economic impact is negligible. Similarly, the salaries of enlisted personnel do not support as much economic activity, since only a small portion circulates within the community, leaving instead to purchase imported items that are purchased on the bases.

Several of Guam's public assistance programs are operated under federal mandate, but are structured with a level of local matching funds that is higher than for the same programs in the States. More critical is the fact that many of these programs are also limited by an annual expenditure cap that is not sufficient to meet the federal share of program costs. Thus, although Guam is bound by federal law to administer the programs, a disproportionate financial burden is borne by Guam in covering program costs.

The variability of federal funding to Guam presents another complication. Although undoubtedly due to unrelated circumstances, there have been repeated instances when this funding rises during an expansionary period in the local economy and contracts during a recession, thus reinforcing the business cycle and making the level of economic activity less stable.

## **Status-Related Issues**

### **Immigration and Labor**

Guam falls within the Immigration Territory of the United States, and immigration into the island is controlled exclusively by the Immigration and Naturalization Service of the U.S. Department of Justice. The labor laws of the United States also apply in Guam, and are enforced by the U.S. Department of Labor; however, several of that agency's responsibilities in Guam have been delegated to or are performed in cooperation with the Guam Department of Labor.

Under Chapter XI, Article 73, of the United Nations Charter, to which the United States is a signatory, allowing immigration into non-self-governing places is discouraged. Nonetheless, the U.S. has allowed immigration into Guam over the past several decades at levels that have been inordinately high relative to the base population of the island. As recently as 1940, Chamorros comprised 93.2% of Guam's population, with the remainder split evenly between

Naval personnel and “Non-native others.”<sup>42</sup> By 1990, the Chamorro population of Guam had lost its clear majority, having fallen to just 43.3% of the total.<sup>43</sup>

While there have certainly been purely social and political impacts associated with immigration into Guam, the principal impacts have been economic. In many respects, the economic effects have been quite positive, as new immigrants have typically been of working age and industrious. The labor resources that they brought to the island have helped to accelerate Guam’s economic development (including the U.S. defense industry in Guam) and build a prosperous community.

At the same time, Guam and its people have borne substantial costs in assimilating these immigrants into a society with American standards, the English language and an economic system with which they were fundamentally unfamiliar. The education, training, housing, and social and physical infrastructure required to bring Guam’s newest residents into functional alignment with their adopted homeland has been costly, drawing community resources away from other potential uses. Compounding the issue is the fact that, once assimilated into the American system, these new immigrants often migrate to the States, taking Guam’s investment in their human resources with them and contributing their skills to other communities.<sup>44</sup> As a result, Guam has not always recovered its investment in the new U.S. citizens that it helped to prepare to be Americans. The current situation of relatively unrestricted immigration into Guam therefore constitutes a net cost to the island’s resident population, and is an economic issue (in addition to its social and political dimensions). The problems, economic or otherwise, derive from the fact that the immigration environment relates to the political agenda of the United States, and not to the needs of the people of Guam.

Many of the labor laws of the United States, as applied to Guam, are generally considered to be beneficial to the island and its people. For instance, few would argue that the regulations imposed under the Occupational Safety and Health Act of 1970 (as amended) are detrimental because of their establishment of safe working standards (although they may be unnecessarily costly, since the same objectives could be achieved more efficiently in some instances). Requirements that employers pay their employees for work performed are similarly uncontroversial. Limitations on the number of hours in a standard workweek, before overtime pay begins to accrue, begin to interfere with both business and (to a lesser extent) labor interests, though. Ultimately, given regional issues of competitiveness, it is the minimum wage that has been viewed as the most constraining labor law impeding Guam’s development during certain periods in the island’s history. Exacerbating the labor situation in Guam, the U.S. minimum wage laws act as an incentive for immigrants from low-wage countries, and limit the types of industry that the island is able to attract. Thus, the minimum wage supports expansion in Guam’s labor force while simultaneously constraining the availability of jobs. Ironically, though, there was a period during the mid-1980s when Guam had a locally enacted minimum wage requirement that was higher than that the U.S. federally-established minimum wage rate.

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<sup>42</sup> See “Guam and Its People” by Laura Thompson, 1941, pg. 32. The data cited are reported to be derived from various reports of the Governors of Guam.

<sup>43</sup> U.S. Bureau of the Census 1990 CPH-6-G, “Social, Economic and Housing Characteristics: Guam,” Table 11.

<sup>44</sup> See Bettis, Leland R., “Colonial Immigration in Guam. Displacement of the Chamorro People Under U.S. Governance”.

With the exceptions of Japan and possibly the Republic of China (Taiwan) and South Korea, the nations of the Asian Pacific Rim and the islands of the western Pacific are generally considered to be less-developed places. Wage rates are far lower than U.S. standards, and workers often accept work for any monetary compensation, since they have no alternative. Because other factors (i.e., location, available resources and productive capital) tend to be similar with those prevailing in Guam, the lower comparative wage rates place those nations at an advantage in attracting the types of investment that creates jobs. Guam's attempts to develop light manufacturing industries in the late 1960s through the late 1970s were inhibited by an inability to compete on the basis of labor costs. The minimum wage, therefore, was viewed as an obstacle to economic development. In some instances, it is still a competitive disadvantage today (particularly in the tourism industry, where competition from the Commonwealth of the Northern Mariana Islands, with its lower wage rates, has caused Guam to generally lag in the growth of visitor arrivals and lead in declines).

There is another aspect of wage rates, though, that imposes significant constraints on Guam's development. It has to do with the fact that the construction industry is the most volatile sector over the course of the business cycle, and Guam's small population base and labor force do not and cannot provide sufficient numbers of skilled construction workers to meet cyclical peak demands. During such periods, Guam "imports" construction workers from Asia under the INS' H-2 visa program as temporary alien laborers to perform the required work. In order to ensure that low-cost foreign workers do not displace U.S. citizens from jobs in the construction industry (or any other industry), the terms of employment of H-2 workers require that they be paid the "Prevailing Wage Rate," as defined by the U.S. federal government.

The Prevailing Wage Rate sets the minimum wage that construction workers in various skill categories must be paid, so that their availability for employment does not discourage employers from hiring U.S. workers in favor of foreign workers. It is determined according to a survey of employers of locally employed U.S. workers (including Guam residents) having similar skills. In Guam's case, though, the survey has included a significant number of civilian employees of the U.S. federal government (for instance, those working at the now-defunct Ship Repair Facility) who are paid according to U.S. mainland wage scales, adjusted upward to acknowledge Guam's higher cost of living. Although these workers were paid substantially more than their counterparts working in the private sector, their inclusion in the prevailing wage rate survey biased the results upward, forcing employers of H-2 workers to pay higher wages than the rate that actually prevailed in Guam's private sector. Adding to that the INS requirement that comparably employed resident workers of the same employer be paid at least as much as their temporary alien peers, the Prevailing Wage Rate raised construction wage rates, and thus the costs of construction, while forcing construction wages to gravitate toward U.S. federal civil service scales. This increase in costs tends to reduce the amount of investment in new structures in Guam, and consequently slows economic expansion.

In fairness, it should be noted that, despite the impact of the Prevailing Wage Rate on the rate of economic growth, the very existence of the H-2 category of temporary immigration allows a degree of stabilization in Guam's domestic economy that would not otherwise be possible. Even though construction wage rates may be higher than desirable during periods of expansion, the necessary workers are allowed to enter Guam at a far lower cost than would be the case if the required employees were recruited exclusively from the U.S. mainland. Just as importantly, when the level of construction activity declines, Guam has the luxury of "exporting"

its unemployment as H-2 workers return to their homelands, thus reducing the drag that their unemployment would otherwise cause on the island's scarce social resources.

## **Legal and Judicial Framework**

Guam's legal and judicial framework is established under U.S. federal law, with additional structure provided in local law and precedent. Until recently, the island's local court was comprised of the Superior Court of Guam, which adjudicated criminal and civil cases that arise under Guam's laws. Recently, a local Supreme Court was created to complete the island's judicial system. In contrast to the State Supreme Courts, though, appeals to decisions made by Guam's Supreme Court are referred to a federal Circuit Court of Appeals rather than directly to the U.S. Supreme Court; this is a transitional provision imposed by the U.S. Congress, which asserts that Guam's Supreme Court needs an opportunity to "mature."

Similarly, Guam's laws are promulgated within a system established by U.S. federal law, and closely reflects the U.S. system. Although Guam has a unicameral rather than a bicameral Legislature (Senate only, rather than Senate and House of Representatives), the process of a proposal becoming Law is essentially the same, with the submission of a Bill to the legislative body, solicitation of public comment, passage by a majority of legislators, and submission to the Executive branch for approval or veto. If vetoed, a Bill can still become Law by a two-thirds majority vote of the Legislature. One difference between Guam and the United States system in this is that the U.S. President vetoes a Bill by not acting upon it, whereas if Guam's Governor takes no action on a Bill, it automatically becomes Law (after a period of time).

### *Land Tenure*

One of the central issues in Guam's recent economic history has been the control of land and the rights thereto. A substantial portion of Guam's land was covered over into the federal estate in the years after World War II. U.S. federal powers of eminent domain were exercised in this process, and many feel that these powers were used without appropriate restraint. Several U.S. federal court cases have shown that just compensation was not made in some of the land takings, and there is a prevailing impression in Guam that more land was taken than has been efficiently used.

Most of the land acquired by the U.S. federal government in Guam has been designated for U.S. military use, yet much of that land has remained idle for decades. Nevertheless, the U.S. federal government retains these lands, and maintains its option to take more acreage at its discretion in the future under its continuing power of eminent domain.

### *Individual Rights*

Individual rights in Guam were initially only vaguely defined under U.S. federal law, and were gradually clarified by the U.S. Supreme Court through decisions affecting Guam and the other U.S. possessions. Specific reference to most of the rights guaranteed by the Amendments to the U.S. Constitution was only added in recent years. While there is still some ambiguity about the application in Guam of portions of the main body of the U.S. Constitution, application of the Amendments is now clear, and only a few of those rights applying strictly to the States and their inhabitants are denied to the people of Guam.

One of the fundamental rights denied to the people of Guam is the right to vote for the Chief Executive of the United States, the U.S. President; another is being represented by a voting member of the U.S. Congress. As a result, Guam's interests are not directly acknowledged by the U.S. federal government. This lack of democratic representation translates to a lack of meaningful influence in key political matters affecting the island and its people, and is one of the driving factors behind Guam's efforts to attain an improved political status.

## **Foreign Affairs and Defense**

The federal government exercises exclusive control over Guam's relationships with foreign nations and foreign governments. Virtually all official interaction that the island has with foreign nations is conducted through the Department of State, and even participation in non-political forums by Guam is strictly controlled and severely curtailed by the U.S. government.

There are a number of regional groups and associations founded by non-governmental organizations (NGOs) in which Guam has expressed a participatory interest, but involvement in most of these is prohibited by the federal government. One glaring example is the Asian-Pacific Economic Conference (APEC), organized to discuss and resolve mutual, regional economic concerns. Guam's participation, even as an observer, was initially prohibited by the Department of State, although the U.S. federal government's position on this later became more moderate.

Nevertheless, Guam does not have the authority to commit to any agreement or any action on its own behalf in relation to a foreign government. Several classes of agreements and other arrangements are prohibited to Guam, with the U.S. federal government substituting its own interests, the presumed "national interest," for that of the island and its people. In some instances, this is beneficial to Guam, since the United States government has the power to wield enormous influence in international affairs, a power that Guam simply does not have. However, the interests of the U.S., on a "macro" scale, are not necessarily aligned with the interests of Guam, given its particular circumstances within the Asian-Pacific region. At times, Guam's actions are constrained even when the 'macro' economic interests of Guam do not conflict with the U.S. national interests.

The United States has assumed all responsibility for the military defense of Guam against foreign aggressors. This is in line with the U.S. national policy of maintaining a forward line of defense to forestall any antagonistic intrusion by a foreign nation into any of the 50 States. However, the resolve of the U.S. to defend Guam itself has not been tested since the mid-1940s. Prior to that time, Guam was not fortified against foreign invasion, in compliance with the terms of the agreement reached between the U.S. and Japan in the Washington Conference of 1921, establishing a moratorium on the militarization of the Pacific islands. Since that time, though, the offensive posture of the U.S. military establishment in Guam has coincidentally served as an effective defense. As in other areas under U.S. jurisdiction, a local National Guard and Army and Air Force Reserve units supplement U.S. military forces in Guam to maintain the common defense.

## **Environmental Provisions**

In 1970, with the creation of the U.S. Environmental Protection Agency, all U.S. environmental laws were applied in Guam, and have served to improve environmental conditions on the island and in its surrounding waters. The Guam Environmental Protection Agency, which

receives an annual average of \$2.3 million in Federal grants, is the primary monitoring and enforcement agent for U.S. environmental laws in the areas of safe drinking water and hazardous waste. Guam EPA additionally enforces all local environmental laws dealing with air pollution, surface run-off, wetlands protection, groundwater, pesticide control and water pollution.

Guam is one of the few islands of the Pacific, outside of Hawaii, that has an integrated sewage disposal system with treatment plants, a well-developed safe drinking water program, and a detailed solid and hazardous waste disposal program. These improvements have generally been beneficial to the island in the maintenance of the quality of life for Guam's residents and visitors alike. However, the rigid standards have added to the development costs that investors and others have had to bear.

Similarly, laws and regulations protecting wildlife have also inhibited several promising development projects. In many situations in Guam, the rigorous protection of flora and fauna is considered by some to be detrimental, on net, to the human population, regardless of the intent of the regulations. As an example of this, an area of land in the northwestern quadrant of the island was released by the U.S. Navy in 1993. Rather than return this land to civilian control, it was given over to the Fish and Wildlife Service of the U.S. Department of the Interior and designated as a wildlife preserve. Ironically, the Fish and Wildlife Service has not been able to locate any of the wildlife on the preserve that it is intended to protect. The land in question is generally considered to be quite valuable for the future economic development of the tourism industry in the Guam, the mainstay of the island's private sector, yet its designated use will potentially withhold it from civilian development in perpetuity.

This in by no means to suggest that environmental regulations have not been beneficial to Guam. On the contrary, the Clean Water Act has helped to preserve significant sources of fresh water for the island and its population that might have otherwise been harmed by unrestricted development. Nonetheless, the application of these regulations without regard to Guam's particular circumstances and how they contrast with the U.S. mainland has served as an obstacle to several promising economic development projects.

## **Financial Sector**

As a possession of the United States, Guam's Dollar-based economy falls under the same processes and controls as apply in the States. The structure of interest rates is the same, the types of available financial assets are the same, and the level of regulation (for most intents and purposes) is the same.

The financial industry in Guam is comprised of banks, savings and loan associations and credit unions; securities agencies and brokerages; insurance agencies and brokerages; and, finance companies. With the exception of the latter two, they are all regulated by a variety of federal government agencies; insurance and finance companies are regulated by the local government. The financial industry plays such a central and critical role in any economy that government regulation is deemed essential for the protection and prosperity of society.

Under the *status quo*, Guam participates in U.S. federal financial clearing system, providing the community with an efficient, globally accepted payment mechanism. As a Dollar-based economy, the U.S. Federal Reserve Bank controls interest rates in Guam through its control of the money supply of the nation. The Office of the Controller of the Currency regulates nationally-chartered banks, while the Guam Banking Commission regulates locally-chartered

banks; however, as a matter of expediency, each of these is insured by the Federal Deposit Insurance Corporation, which serves as the proximate regulatory authority. Guam is also an eligible location for offshore banking<sup>45</sup> activity under U.S. law, which is regulated separately by the U.S. federal government. For all practical purposes, the FDIC also regulates Guam's savings and loan associations. Credit unions fall under the regulatory authority of the National Credit Union Administration.

The rules applied to banks, savings and loan associations, and credit unions are coordinated at the federal level by the Federal Financial Institutions Examination Council, composed of representatives from each of the major depository regulatory agencies. Because of the particular functions of depository institutions, and most especially their holding of the public's funds in fiduciary trust, regulation of each institution is essential to maintaining the public's trust in the industry and the nation's currency (and other forms of money). It ensures that financial institutions adhere to sound business practices and that the risk of loss to both depositors and shareholders is minimized. Confidence in the nation's money, in turn, allows enormous efficiencies in the economy to be exploited; without regulation, the use of money would become ineffectual, and the economy would cease to function efficiently. Insurance of depositors' accounts helps to strengthen this confidence even further.

The U.S. Securities and Exchange Commission regulates trade in stocks and bonds by securities agencies and brokerages, although much of this is accomplished by the relegation of oversight to the National Securities Dealers Association, an industry trade group.

Under federal law, the regulation of insurance is left to the several states (including the territories), except for the applicability of several antitrust provisions (Sherman Act, Clayton Act and Federal Trade Commission Act).<sup>46</sup> Consequently, insurance agencies in Guam are primarily regulated by the local government.<sup>47</sup>

## **Social Welfare Programs and Other Assistance**

There is a wide range of programs available in Guam to assist those members of society who, for whatever reason, are unable to adequately provide for themselves. These include the so-called "public assistance" programs of Old Age Assistance, Aid to the Blind, Aid to Families with Dependent Children, Aid to the Permanently and Totally Disabled, and General Assistance, providing cash assistance. The U.S. federal Food Stamp, School Lunch, and Women Infant and Children programs provide assistance in obtaining basic food and nutritional requirements. Subsidized housing is available under Section 8 of the Department of Housing and Urban Development Act of 1965. The Social Security, Medicare and Medicaid programs can also be considered to be social welfare programs.

Participation in these programs has been as follows:

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<sup>45</sup> "Offshore banking" allows foreign banks to operate in the United States for the purpose of financing international trade. Such banks are not allowed to accept domestic U.S. deposits unless they are associated with trade financing credit.

<sup>46</sup> See U.S.C. Title 15, Chapter 20, §1012.

<sup>47</sup> See 22 GCA, Chapter 18, for instance.

	June 1989		June 1999	
	Persons/ Households	\$ Amount	Persons/ Households	\$ Amount
Old Age Assistance*	651	\$53,393	501	\$126,265
Aid to the Blind*	2	\$120	1	\$151
Aid to Families with Dependent Children	4,009	\$236,843	10,006	\$1,582,943
Aid to the Permanently and Totally Disabled*	163	\$11,957	93	\$23,146
General Assistance	296	\$20,021	2,686	\$446,202
Food Stamp Program	11,901	\$1,120,724	20,464	\$2,707,485
School Lunch Program	N/A		N/A	\$2,834,881
Women and Infant Care	N/A		6,681	\$348,521
Section 8 Housing	1,271	\$14,000,000	1,271	\$14,000,000
Medicaid	N/A		5,546	\$2,638,132

\* These three programs were replaced by the fully federally funded Supplemental Security Income program in the States in 1972 under P.L. 92-603.

Source: Guam Department of Public Health and Social Services, Guam Housing and Urban Renewal Authority, and Guam Department of Administration.

Many of the above programs are administered by the government of Guam, which spends locally-generated revenues supplemented by U.S. federal matching funds. While the programs are all different, they typically have a 75% federal share of matching funds. However, the match is limited by a gross dollar expenditure cap, which has resulted in the percentage match being substantially below the percentage designated.

In addition to social welfare programs, there are other programs that apply to Guam and provide assistance during times of need. Principal among these are the disaster assistance programs administered by the Federal Emergency Management Agency and the U.S. Small Business Administration. Both agencies have been instrumental in assisting Guam in recovering from typhoons.

### **Other Factors in the *Status Quo***

After more than a century of U.S. federal administration of Guam (which has been primarily military rather than civilian, and was broken only by the Japanese occupation of the island during World War II), there are innumerable other federal laws and regulations that apply, either partially or in full. Many of the imposed provisions have proven to be beneficial to the island, while others have been onerous. All have been applied with little or no consultation with, nor acquiescence by, the people of Guam. The foregoing, though, are considered to be the most

important from an economic standpoint, as their effect on Guam's economic circumstances are the most frequently referenced in discussions of the island's relationship with the United States.

## **Status Options**

The people of Guam have been seeking to improve their economic and political status throughout their colonial history, and have taken a wide range of approaches to obtaining their goals. Under the colonial administration of the United States, the first attempt was the self-proclaimed ascension to Governor of Joaquin Perez in 1899. Several more moderate attempts have been made since, culminating in the Organic Act of 1950 and the Elective Governor Act of 1970.

More recently, Guam made a failed attempt to adopt a constitution in 1979. The island then held a plebiscite on status options in 1982 (followed by a runoff between statehood and commonwealth later in the year, since no single status received a majority of the vote in the first plebiscite). Guam's voters passed a draft Commonwealth Act in 1987 for consideration by the U.S. Congress. In Article 1, §102(a), of Guam's draft Commonwealth Act, the ultimate right to self-determination by the Chamorro people of Guam was to be recognized, and was to be exercised according to provisions to be contained in the Commonwealth's Constitution. This Constitution was to be adopted by a general referendum of all registered voters in Guam.

After years of unsuccessful efforts to gain passage of the Commonwealth Act, the Commission on Decolonization was created in 1997 under Guam P.L. 23-147. The Commission was established to accord those people in Guam who have not exercised their right to self-determination in modern times the opportunity to exercise that right by selecting the ultimate political status of the island. Under P.L. 23-147, those eligible to exercise this right are defined as, "All inhabitants of Guam in 1898 and their descendants who have taken no affirmative steps to preserve or acquire foreign nationality."<sup>48</sup>

Because the United States Congress has not explicitly acknowledged this right to self-determination with respect to the people of Guam, the eligible voters are to make their selection in a non-binding plebiscite in order to express their preference. It may be assumed that the government of Guam will then proceed in an effort to encourage the U.S. Congress to accommodate the expressed wishes of these people.

### **Options Under Consideration**

Public Law 23-147 provides for the consideration of three political status options: independence, free association and statehood. The Commission on Decolonization has established three Task Forces, one for each option, that are charged with conducting research into each of their respective options and helping to organize an educational campaign to inform eligible voters about the repercussions of their selection. This analysis is intended to support those educational campaigns.

### **Background**

According to historians and anthropologists, Guam has been inhabited by the Chamorro people since c. 1300 B.C. When Ferdinand Magellan "discovered" the island in 1521, the

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<sup>48</sup> This is the definition used in determining those persons who were to gain U.S. citizenship under the 1950 Organic Act of Guam.

Mariana Islands were populated by some 100,000 Chamorros, having a common language, a well-structured society and a self-sufficient agrarian economy. “Guahan,” the Chamorro name for Guam, literally means “we have,” and Guam engaged in periodic trade with the peoples of the Caroline Islands to the south and east. Maguel Lopez de Legazpi claimed Guam in the name of the Spanish crown in 1565, but formal colonization of the island did not begin until the first Spanish missionaries arrived to help administer the island and convert the Chamorros to Christianity in 1668. Primarily, though, the Spanish interest in Guam was limited to its usefulness as a source of fresh produce and potable water for sailing ships in their trans-Pacific trade, and as a port of refuge for the Manila galleons.

As Spain consolidated its empire, the administration became more methodical, with a permanent garrison of soldiers and a Captain who served in the role of Governor. Upon the insistence of the missionaries who also visited Guam, the Spanish army became involved in the process of religious conversion, enforcing the objectives of the Cross with the influential exercise of the sword. The “Chamorro Wars,” which lasted from 1672 through 1698, resulted in the decimation of the Chamorro population (along with European diseases against which the native inhabitants of Guam had no resistance) to less than 5,000.

## **Colonial Heritage**

After being claimed by Spain in the mid 16<sup>th</sup> century, the colonial administration of Guam took over 100 years to develop. Over the course of the next two and one-half centuries, the level of administrative oversight varied from almost non-existent to fairly stringent control. Overall, though, the Spanish interest in Guam was for the island’s convenient location and the staples provided by the island. After the reduction of the population by war and disease in the late 17<sup>th</sup> century, the Spanish began bringing in conscript labor from Mexico and the Philippines in significant numbers to supplement the native population in provisioning Spanish vessels. Over the course of the years, various attempts were made to educate and “civilize” the native population, with more or less success.

When Spain ceded Guam to the United States under the Treaty of Paris at the end of the Spanish American War, it took nearly two years for the U.S. to install a government on the island. From 1900 through 1941, the island was governed by a series of Navy captains. Some of these made important efforts to improve the public health, educate the island’s youth and form a civilian contingent within the local government, but most devoted their attentions to the military mission. The primary approach to economic development was to support agriculture, and it met with only sporadic success.

On December 8, 1941, the Japanese Army invaded Guam and held the island for some 31 months. Japan had held the Northern Marianas, Palau, and the other islands of Micronesia for some twenty years under a League of Nations mandate, and viewed Guam as completing its set of colonies in the region. However, the people of Guam were not easily subjugated, and the occupation was not cordial. The United States returned to Guam in force in July 1944, and has exercised sovereignty over the island ever since. The lives of the indigenous population were completely devastated by the harsh Japanese occupation, and enormous damage to the island’s infrastructure and development by the shelling and bombing that accompanied the effort to “liberate” Guam.

## **Political Aspirations and the History of Guam's Status Initiatives**

It did not take long for Guam's Chamorros to appreciate the American system of democracy, and to desire a greater degree of self-determination than was provided under Guam's early Naval government. In response to their expression of these desires, Governor (Captain Roy C.) Smith formed the First Guam Congress in 1917 as an advisory group, established to serve as a liaison between the Chamorro population and the military leaders. The First Guam Congress, though, was disbanded in 1931 when Governor (Captain Willis) Bradley concluded that the 34 members were not functioning as a representative body or in a manner to take full advantage of its possibilities.

The Second Guam Congress played much the same role as its predecessor, but was better organized. In 1936, it supported a long and arduous trip to Washington, D.C., by B.J. Bordallo and E.T. Calvo, whose purpose was to petition the Congress for U.S. citizenship and an improved political status for the people of the island. Little progress was made, and the efforts of the Chamorros were cut short by the Japanese occupation during World War II.

After the War, it took little time for the indigenous residents of Guam to resume their efforts toward greater internal political authority. Ironically, it was the federal government's desire to acquire land in Guam for its military operations that forced the issue of citizenship for the Chamorros, and a nation just recovering from its second anti-colonial war went further in establishing a civilian government with some meaningful, however limited, internal political power. The 1950 Organic Act of Guam was a major milestone in the political history of the Chamorro people, helping to define a modern political status for the island with a modest degree of internal authority.

The Organic Act has served as the basic law governing the political status of Guam for a half century. It defined a civilian government, with three branches, patterned after the U.S. system, but having a Governor appointed by the President. The Governor, though, had veto power over acts of the elected Guam Legislature that could not be overridden, except by the U.S. Congress. While the Organic Act represented a remarkable advance toward internal political authority for the civilian inhabitants of Guam, the people wanted more.

In 1962, President Kennedy appointed the first indigenous Governor of Guam. This was a meaningful, albeit token gesture, acknowledging Chamorro rights to the civilian governance of the island. In 1970, though, Congress set another milestone by passing the Elective Governor Act, providing the people of Guam the authority to elect their own executive leadership for the first time since Spanish colonization began some 300 years before.

During the 1960s, increasing affluence of the Chamorro people, by then U.S. citizens, allowed more of the island's youth to further their education in the States. It was a period of heightened political awareness on college campuses, in large part because of the civil rights movement, the war in Vietnam and the migratory farm workers' issues in California. Some of Guam's youth, returning to the island once their education was completed, brought sophisticated new attitudes with them. The "Brown Power" movement struggled in its infancy, but quickly spread throughout the island as many residents reassessed the basic concepts of democracy and self-determination as applied in Guam's context. Despite the progress that had been made since World War II, it was less than satisfying, and renewed interest in internal sovereignty stimulated further efforts toward self-determination. Guam's first Constitutional Convention was convened

in 1969 to draft a constitution for Guam, but the U.S. Congress never considered the product of its efforts.

In 1976, the U.S. bicentennial year, the people of Guam organized a second Constitutional Convention (with the consent of the U.S. Congress) to draft a formal constitution for the island. This time, congress approved the document. However, with the end of the war in Vietnam and a sudden deterioration in tourism because of the oil crises of that decade, economic issues quickly took precedence over political issues, and this second constitution was never ratified by the people of Guam.

Guam Public Law 15-128 established the Commission on Self-Determination in 1980. The second effort to form a constitution for Guam had failed, in part, because the relationship of Guam to the United States had not been clearly defined first. The Commission's initial responsibility was to remedy this situation by conducting a plebiscite to poll the population with regard to the political status that they desired. The first plebiscite was held on January 12, 1982, resulting in a plurality vote for commonwealth (49%) and statehood (26%), followed in rank order by *status quo* (10%), incorporated territory (5%), free association and independence (4% each) and "other" (2%). A runoff plebiscite was held on November 2, 1982, resulting in the selection of commonwealth status (73%) over statehood (27%) as the preferred political status of the people of Guam.<sup>49</sup>

Guam's leadership spent the next several years drafting and refining a legislative initiative for approval by the island's voters before submission to the U.S. Congress, and held a plebiscite on April 18, 1987, for its adoption. Articles 1 and 7, to govern the political relationship between Guam and the U.S., and immigration provisions for the Commonwealth, failed in the plebiscite, while all other provisions passed. Articles 1 and 7 were modified and offered for approval in another plebiscite that took place on August 8, 1987, in which both passed.

The "Guam Commonwealth Act" was introduced in the U.S. House of Representatives on February 17, 1988, and in the Senate on March 7 of that year. The first hearings on the Bill were held before the Subcommittee on Territorial and Insular Affairs of the Interior Committee of the House of Representatives in Honolulu, Hawaii, in December 1989. At the end of two days of hearings on the legislation, Subcommittee Chair Ron DeLugo of the U.S. Virgin Islands directed the Guam Commission on Self-Determination to gain the concurrence of the U.S. federal Executive Branch on the wording and provisions of the Commonwealth Act, and then to resubmit the resulting legislation to the Congress.

## **Recent Experience**

In 1990, President George Bush's administration organized a high-level Task Force to study and discuss the Commonwealth Act. Every second month, the Task Force and the Commission met face-to-face to attempt to agree upon mutually acceptable language and provisions for Guam's commonwealth status. After more than two years of intensive discussions, a common ground could not be achieved in several areas of discussion. The effort, while succeeding on many of the proposed legislation's subjects, was ultimately a failure. Although attempts to achieve Commonwealth status continue, there has been little hope of success after the end of discussions with the U.S. federal Executive Branch in February 1992.

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<sup>49</sup> "Guam's Draft Commonwealth Act," as presented to the United States Congress, February 1988, p.10.

Progress in improving Guam's economic conditions was the principal result of the Commonwealth effort. In the areas of immigration and telecommunications, substantive changes were made in U.S. law, as it applies to Guam, with improvements in the temporary alien labor program into the island and the extension of the North American Numbering Plan. Perhaps more importantly, several federal agencies acquired a better understanding of conditions in Guam, and have improved their programs to the benefit of the island's population.

However, the overall experience of the Commission on Self-Determination was one of frustration. The perceived objective of their U.S. federal counterparts was to undermine the process and interfere with any attempt to gain improved political and economic status for Guam. In many instances, the "good-faith" efforts were called into question, and some federal officials proved to be particularly obstinate in their discussions with the island's leadership.

### **Current Efforts**

Public Law 23-147 created a Commission on Decolonization for the Implementation and Exercise of Chamorro Self-Determination (the Commission on Decolonization). While the Commonwealth effort continues, a decision was made to move forward with a Chamorro-only vote to select the island's ultimate political status in relation to the United States, in accordance with the intent of Section 102(a) of the draft Guam Commonwealth Act.

Chapter 21, Section 21106 of the Guam Code Annotated, created by Public Law 23-147, establishes three Task Forces to study and advocate the options for Guam's prospective political status: the Independence Task Force, the Free Association Task Force, and the Statehood Task Force, corresponding to the three status options to be considered. Section 21110 of the same Chapter specifies the language of the ballot on which votes shall be cast, as follows:

"In recognition of your right to self-determination, which of the following political status options do you favor?" (Mark ONLY ONE):

1. Independence ( )
2. Free Association ( )
3. Statehood ( )

A plebiscite is scheduled to be held on November 7, 2000, to accord Guam's Chamorro population, a politically-defined group, the opportunity to exercise their right to self-determination. In order to better educate the voting public on the three political status options, the three Task Forces were formed with the objective, in part, of assisting in organizing and conducting a public education campaign on the three status options. This campaign is considered necessary in order to clarify the prospective conditions in Guam under each of the respective status options so that the eligible voters can make a more informed choice from among the three.

This study has been prepared to assist the Task Forces and the Commission in their educational efforts. It is intended to be an unbiased, balanced presentation and analysis of the political status options and their potential economic impacts.

## **Comparable Experience in Other Places**

It is quite difficult to anticipate all of the possible outcomes of a change in political status. In all of history, no such change has ever resulted in exactly the conditions that were anticipated. Further, the Task Forces have not yet prepared draft constitutions or other legal frameworks for their respective advocated option, nor have they yet established a clear set of the economic parameters that they expect to prevail after the transition in status has occurred. Therefore, this analysis resorts to a comparison of the *status quo* to the experience of other jurisdictions that have undergone similar status changes, tempered by adjustments to reflect Guam's unique, preexisting circumstances.

As a limitation of the study, this approach may not fully or accurately represent Guam's prospects under any of the proposed statuses, since the nature of the final result of the political transition and the consequent economic structure of Guam may ultimately be different than envisioned. However, the approach may make the study far more valuable to the people of Guam and to the transition process itself, since it will provide a baseline, alternative perspectives, and possibly guidance regarding how Guam's post-transition economy might be structured.

### **Basis for Comparability**

In order to describe the prospective economic conditions in Guam after a transition to statehood, free association or independence, it would be most useful to draw parallels with other places having similar characteristics to Guam prior to undergoing recent changes similar to those under consideration. Unfortunately, there are no cases that meet these requirements. Therefore, it will be necessary to draw comparisons with other jurisdictions that are moderately dissimilar to Guam, and to adjust those comparisons with reference to how differing prior circumstances might alter the outcomes in Guam's case.

#### *Small, Less-Developed, Remote Economies*

Because this is an analysis of prospective economic circumstances in Guam, it is critical that it be based upon locations having similar physical and developmental conditions prior to a political status change. Large economies typically have larger populations, more internally available resources and greater existing industrial capacity. Economies that are more developed have more refined transportation and distribution systems, and typically have greater accumulated wealth with which to make needful investments. Jurisdictions on or near large landmasses experience a freer cross-border flow of goods and a lower burden of transportation costs. Therefore, limiting comparisons to the experiences of small, less-developed, remote jurisdictions will be most useful in assessing Guam's economic circumstances subsequent to a transition.

#### *Colonial History*

Although most people view the relationship between colonial history and a status change as being strictly political in nature, there are a number of areas in which such a transition affects economic circumstances, as well. There are several ways in which a change from non-self-governing status to sovereignty can affect an economy's operation, particularly if the legal structure of economic interactions is not well defined when the political shift occurs. The

imposition of rules from the outside can have a profound effect on the internal operation of an economic system, and the absence of those rules has the potential to cause chaos unless the post-transition government has the experience and/or foresight to properly regulate economic interactions. Both the length of time and the intensity in application of the authority of the metropolitan power are therefore important to the results of this study.

### *Recent Status Transitions*

Virtually every fundamental characteristic of the world economy has changed substantially in the past several decades because of advances in technology and communications, and because of the social, political and diplomatic realities that those changes have engendered. Social perspectives have changed, as evidenced by the secular concentration on “human rights” in recent international diplomatic interactions. Most modern governments have only recently acknowledged the counterproductive nature of trade barriers, and global power alliances are shifting more frequently than ever before. In this environment, the impacts of political status changes that have taken place in the past are hardly representative of what might be expected today. Consequently, the results of more recent status changes are more relevant to the purposes of this study.<sup>50</sup>

### *Type of Status Change*

Each of the Task Forces has indicated that they anticipate a negotiated change in status subsequent to the decolonization plebiscite.<sup>51</sup> As a result, the change that Guam should expect would be reasonably moderate, as opposed to radical. This is in contrast to many of the more revolutionary separations from colonial powers that have occurred since World War II in that there is some degree of continuity in government and greater stability in the societies affected. This feature of Guam’s anticipated status change limits consideration of comparable transitions to those that have occurred under fairly amicable circumstances, more in an evolutionary rather than a revolutionary mode.

### *Affiliation with the United States*

A final feature of comparability relates to the colonial regime under which the jurisdiction in transition has existed. Under any colonial administration, there are a set of laws, regulations and standards that are imposed from the outside. Regardless of the metropolitan power, this framework becomes ingrained over time into the society, and often even into the culture of the colonial subjects. With this basis in familiarity, the post-transition structure of the jurisdiction often bears marked similarities to the pre-transition colonial structure for a period of at least several years. Given the prolonged administration of Guam by the United States and the degree to which the resident population has become accustomed to and assimilated into the “American”

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<sup>50</sup> It should be noted that the posture taken by the U.S. government in the political status negotiations with Pacific islands during the past quarter century provide insight into the current philosophy of the United States in these matters, and will therefore influence the conclusions drawn in this study. However, that philosophy continues to evolve, and cannot be relied upon to completely or accurately reflect the attitudes of the U.S. government today.

<sup>51</sup> It is possible, of course, that Guam could *declare* its independence from the United States, but the political and economic risks of such an extreme action are generally considered to be unacceptable to the majority of people in Guam.

system, it is likely that Guam will retain many of the attributes that have become routine since 1898. In this regard, those systems that are most comparable to Guam will be those that have experienced a similar history under U.S. administration.

## **Selected Economies**

### *Statehood Comparables*

#### *Hawaii*

A relatively remote island economy with a significant indigenous population and limited natural resources, Hawaiian history and status make it perhaps the best example of the transition from territory to statehood in comparison to what Guam may experience.

The fiftieth and last State in the United States attained statehood on August 21, 1959, some 59 years after it was established as a U.S. territory. The history of the Territory of Hawaii, both before and after annexation in 1898, is replete with examples of domination by outside interests, most notably commercial interests. The U.S. largely neglected the political and economic interests of the indigenous residents, and their economic status was not proportionately improved as the islands developed.

One major difference between Hawaii as a territory and Guam was the imposition of U.S. federal taxation prior to statehood. Although this “taxation without representation” (Hawaii had a non-voting delegate to the U.S. House of Representatives) contrasted with one of the primary reasons that the United States itself had sought independence from Britain, its existence before statehood helped to reduce the economic shock that transition entailed.

#### *Alaska*

The forty-ninth State endured 88 years of American colonialism and officially sanctioned commercial exploitation after its purchase by U.S. Secretary of State William Seward in 1867 before being admitted to the Union in 1959. There are a number of characteristics and conditions in Alaska throughout its colonial period that have no parallel in Guam, but there are enough similarities to warrant its mention.

Much of the value extracted from Alaska prior to statehood was in the form of minerals, furs and salmon, with each industry controlled by non-resident entrepreneurs, most notably those located in Washington State. As residents of a territory, the residents of Alaska also experienced artificially high prices on imported goods due to the imposition of the Jones Act in coastal trade.

Alaska was also “buffer zone” during the Cold War, serving as a forward position relative to the Soviet Union for military deployment; it had begun filling this role in the defense against Japan during World War II.

Like Hawaii, the federal income tax was imposed upon the people of Alaska prior to the transition to statehood. In contrast, though, Alaska has never had to implement a state income tax, deriving the bulk of its revenues from resource extraction royalties.

## *Free Association Comparables*

### *The Federated States of Micronesia*

As a former Trust Territory of the United States under a 1947 United Nations mandate, the Federated States of Micronesia serves as a recent example of the transition to free association by a U.S.-affiliated entity. The details of the Compact of Free Association and the economic aftermath of the transition are both relatively important examples of a transition to free association under a reasonably current set of U.S. provisions. Not only do they set precedents in Guam's prospective negotiations toward free association, they also provide a great deal of information about the philosophy of the U.S. in dealing with former protectorates.

Many students of the history of the FSM have concluded that a kind of "grand experiment" took place there during the Trusteeship, with Yap, Chuuk, Pohnpei and Kosrae each being treated differently in terms of economic development policies. Of the four states within the FSM, Pohnpei bears the closest similarities to Guam, and so will serve as the primary parallel to the free association status option. Pohnpei received the highest level of infrastructure funding and development, and private economic activity was encouraged there more so than in the other three States.

### *Palau*

The Republic of Palau (Belau) is also a part of the former Trust Territories, but had its transition to free association delayed by a specific provision in its Constitution. After a series of several votes to change the "nuclear free" constitutional clause in order to permit U.S. military entry into the nation in times of U.S. national emergency, the people of Belau were granted substantial, long-term benefits during and beyond their transition to free association.

The economy of Belau, tied to Taiwan more than to Japan (as are the other islands), has performed reasonably well during the 1990s. Further, the people of Belau have agreed among themselves to accept slower growth in their economic system in exchange for maintaining their pristine environment and protecting their principal resources from rapid deterioration.

Belau has made, perhaps, the most successful transition to free association in economic terms, and provides several insights into how the process can be optimized and how the U.S. Congress actually views the Pacific islands under its control.

### *Commonwealth of the Northern Mariana Islands*

The Commonwealth of the Northern Mariana Islands has not taken any of the political status options contemplated by Guam, but has made the transition from Trust Territory to commonwealth status within the past quarter century. Because its status is neither statehood, free association nor independence, it does not provide any direct comparability with Guam's status options. Nevertheless, it can provide insight into both the process of status change *vis-à-vis* the United States as well as some of the prevailing political philosophies exhibited by the United States during status negotiations. Further, the CNMI provides cautionary evidence of how a negotiated status might be perversely interpreted or unilaterally modified once it is in place.

### *Fiji*

Fiji was an unorganized group of islands, ruled by local chieftains until 1871, when local disorder prompted residents of European descent to form a national government. Continued disorder, though, led a group of chieftains to request British annexation. Fiji was then a British colony from 1874 until 1970, when it gained independence. From 1970 until 1987, it was a member of the British Commonwealth of Nations ( a freely-associated status), but was expelled following two coups in 1987, after which it was declared a republic.

Comprised of two principal islands (Viti Levu and Vanua Levu) and some 800 smaller islands (approximately 100 of which are inhabited), the economy is based upon sugar exports, tourism and subsistence farming. The population is divided, with approximately 50 percent native Fijians and some 45 percent are the descendants of Indians brought in by the British to work on plantations between 1879 and 1916. There is significant ethnic stress, due primarily to the nation's land being owned by native Fijians and most enterprise being operated by the minority Indians.

The two political coups in 1987 adversely affected Fiji's tourism industry, and the nation lost a significant number of its skilled and educated workers when many Indians left the country shortly thereafter. A new constitution, adopted in 1990, grants preferential treatment to ethnic Fijians. The constitution requires that the President and Prime Minister both be native Fijians, and that the appointed Senate and elected House of Representatives are filled with majorities of Fijians. However, all citizens of Fiji who are at least 21 years of age may vote.

### *Cook Islands*

The Cook Islands is a self-governing island group in free association with New Zealand. Most of the eight principal islands in the Southern Group are volcanic in origin, mountainous, and relatively fertile; several are coral islands. The Northern Group is composed of low-lying coral islands. The port of Avarua on the island of Rarotonga is the administrative center of the Cook Islands.

Tourism is the leading industry in the islands. Coconuts, citrus fruits, copra, pineapple, clothing, mother-of-pearl shells, and handicrafts are among the principal exports. Rarotonga has an international airport. The inhabitants of the Cook Islands are Polynesians, culturally and linguistically related to the Maori of New Zealand. Education is provided by government schools, and health care is free.

Spanish and Portuguese navigators reached the islands in the late 1500s and early 1600s, and the islands were sighted by the British explorer James Cook in 1773. In 1888 the Cook Islands were made a protectorate of Great Britain, and in 1901 they were annexed by New Zealand. Since 1965 the islands have had full internal self-government, while matters of defense and external affairs remain the responsibility of the New Zealand government.

### *Independence Comparables*

#### *Philippines*

The Republic of the Philippine Islands provides the only example of a negotiated independence from the United States. In a process that began shortly after the beginning of the

twentieth century, the Philippines was granted sovereignty, and the evolution to self-government occurred gradually over a period of nearly half a century.<sup>52</sup>

There are obviously huge differences between Guam and the Philippines in terms of population and natural resources, and the movement toward independence is quite remote in time from Guam's efforts. Therefore, the parallels to be drawn are not strong. However, there were a number of precedents set in the process that may also be applied by the United States to Guam.

### *Cuba*

Although Cuba was granted its independence under the Treaty of Paris, which ended the Spanish-American War in 1898, an American military government ruled the island until May 20, 1902, when the Cuban republic was formally instituted. However, the Cuban constitution, which had been adopted in 1901, incorporated the provisions of the Platt Amendment, U.S. legislation that established conditions for American intervention in Cuba. During the period of occupation, U.S. commercial interests invested heavily in Cuba, particularly in natural resources and the sugar-growing industry, which quickly fueled resentment and eventual insurrection. In response, American troops retook the island in September 1906, and maintained control until 1909. Another uprising in 1912 again brought U.S. military intervention.

Decades of economic difficulties followed, largely due to the dominance of U.S. firm's in Cuba's primary industries. These difficulties are blamed for political instability and repeated insurrections. The government of Cuba rapidly transformed into a dictatorship in the early 1930s, and economic difficulties mounted because of fluctuating world sugar prices. Following a military coup in 1952, an election was held in 1954 and constitutional rule was restored the following year. However, a general revolt in 1958 led to the establishment of a provisional government in 1959, followed by expropriation of U.S.-owned properties in 1960. Diplomatic relations between Cuba and the U.S. collapsed, and tensions mounted further after an unsuccessful U.S. sponsored attempt to invade the island in 1961. Tensions have remained high ever since.

In 1965, a brokered agreement between the U.S. and Cuba allowed some 260,000 Cuban nationals to emigrate to the U.S. until the airlift was ended in 1973. In 1980, when the Cuban government again temporarily lifted travel restrictions, another 125,000 Cubans fled to the United States.

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<sup>52</sup> After overcoming insurrection in the wake of the Spanish-American War, U.S. civil government replaced military authority in 1902 and a bicameral legislature was authorized. The first session of the Legislature opened on October 16<sup>th</sup>, 1907, with an elected lower house. In 1916, an elected upper house was instituted under the authority of U.S. law, and eventual independence was promised. However, a commission appointed by U.S. President Harding in 1921 concluded that immediate independence would be "a betrayal of the Philippine people," and progress toward sovereignty was stalled. A 1933 U.S. law proposed granting independence after 12 years, but reserved military bases for the United States in the Philippines and imposed tariffs and quotas on Philippine exports, and was rejected by the Filipinos. A year later, another U.S. law granted complete independence by 1946, and provided for an interim commonwealth supervised by the United States, but with an elected Philippine president and a constitution. The constitution, adopted in February 1935, was approved by President Roosevelt and ratified by plebiscite, and the commonwealth was formally established on November 15, 1935. The Republic of the Philippines was formally proclaimed on July 4, 1946.

Isolated in international trade with free nations since 1960, the Cuban economy continues to falter, and following the termination of subsidies from the Soviet Union when that nation was dissolved in the early 1990s, matters have become worse. Poverty is widespread, and political dissent and insurrection are again on the rise.

### *Jamaica*

Jamaica became a Spanish colony in 1509, but its economy was left largely undeveloped by Spain and languished. The native population died out because of harsh treatment and disease, and the demands for labor to work the island's plantations were met by the importation of African slaves. The island was captured by the English navy in 1655, and formally transferred to England in 1670. Shortly thereafter, accelerated colonization ensued.

Under the English system of colonialism, a large measure of self-government was instituted in the late 1600s. Slavery was abolished in 1838, leading to severe disruption of the economy and eventually to insurrection in 1865. The uprising was quickly quelled, and Jamaica was made a crown colony. Representative government was partly restored in 1884. The island gained its independence nearly 80 years later, in 1962, and government was established as a constitutional parliamentary system similar to Britain's. The nation has alternated between socialist and free-enterprise policies since that time.

Primarily an agricultural economy, with some mining and manufacturing, Jamaica is heavily dependent on foreign trade and tourism. During the mid-1990s, the annual gross domestic product of the nation's 2.5 million people was approximately \$1,640 *per capita*.

### *Other Comparables*

#### *Puerto Rico*

Although Puerto Rico is labeled as a "commonwealth," its political status is quite similar to that of Guam, except that it has a constitution. Like Guam, Puerto Rico is also in the process of attempting to improve its status relative to the United States. Puerto Rico was ceded by Spain to the U.S. at the same time as was Guam, but is a much larger island far closer to the U.S. mainland, with a substantially larger population and more available natural resources. Although the two U.S. possessions are in similar stages of economic development, *per capita* income in Guam is far higher than that in Puerto Rico.

Because Puerto Rico has not yet achieved a change in its political status, it does not provide a basis for post-transition comparisons to the statuses being contemplated in Guam. However, it has been engaged more intently in the process and has made far more progress than has Guam. The mood of the people of Puerto Rico keeps changing, though, and although statehood has retained about the same level of interest among the people there over the past decade, interest in independence has supplanted *status quo* as the second preferred option.

Because the efforts in Puerto Rico to change its political status in relation to the United States are contemporaneous to those in Guam, there are numerous examples from the Puerto Rican experience that can serve as useful lessons to Guam. However, there are several important differences between the two U.S. possessions that could make the ultimate results of similar political status choices quite different. Therefore, whereas the experience of Puerto Rico may be illustrative of some of what Guam can expect in its efforts to change status, neither the economic

results of a change nor the concessions granted by the U.S. Congress to the two dissimilar places will be comparable.

### **Common Assumptions**

A change in political status will have numerous impacts on political, social and economic conditions in Guam, yet exactly what the resulting conditions will be cannot be known until the final status is defined. One of the purposes of this report, though, is to assess economic conditions in Guam after the status change has occurred. Without foreknowledge of those conditions, it is necessary to make a variety of assumptions so that the prospects under each status option can be assessed. Further, the assumptions regarding each parameter impacting the economy must be both internally consistent within a particular status option and comparable across the three options.

For purposes of this report, the researcher reviewed 19 major parameters along with eight sub-parameters for the *status quo* and each of the three status options. Working with his associates, he developed descriptions (where appropriate) and assumptions about each. These are incorporated into this report as Appendix 2, which provides a matrix assessing each status for each parameter and sub-parameter.

## **Comparisons and Prospective Results**

### **Limitations on the Accuracy of the Comparisons and Prospective Results**

Each of the three political status options under consideration by the eligible voters of Guam would constitute a significant deviation from the status quo, and each would bring with it changes to the structure and operations of Guam's economy, with greater or lesser impacts in several areas. Some of these impacts would undeniably be beneficial to the people of Guam, while others could be detrimental. Thus, anticipating these impacts is a worthwhile exercise, and the primary purpose of this report.

However, it must be clear that there is rarely any certainty about the future, and in many circumstances, there is a great deal of uncertainty; this is one of those circumstances. There are several reasons for this situation. First, it is difficult enough to just define the *status quo* from which Guam proposes to depart. There is a lack of sufficient, timely socio-economic data available for the island, and the validity of much of those data is somewhat questionable. This would make it difficult to compare and contrast even a known future with the *status quo*, since the baseline is not perfectly clear.

Second, Guam is unique. Although there are several other places that have undergone changes in political status, whether to statehood, free association or independence, none of these places began the process from Guam's current circumstances. Indeed, among those that are cited as "comparable" in this report, none bear even a close resemblance to Guam. Their populations were larger, or smaller; they had more or fewer available natural resources; they were colonized for longer or shorter periods, many under metropolitan powers other than the United States; the level of economic development at the starting point was different. At best, review of the results of their status changes will only help to illustrate the types and, possibly, the magnitude of the changes that the people of Guam can expect. It should be understood, though, that there are too many differences between Guam and these other places prior to the respective status changes to draw any strong conclusions regarding Guam's prospects solely based upon the experience of other places.

Third, and perhaps most important, is that each of the three status changes being contemplated by Guam are to be negotiated. The eligible voters of Guam have not yet defined which status they will seek, let alone the conditions that they expect or the provisions that they hope to attain in whichever final option they choose. Even if Guam's leaders were able to clearly specify their objectives in every element of whatever status change is selected, and to precisely describe their desired outcomes, the opening position in any negotiation is rarely equivalent to its final result. There are two sides in every negotiation, and the interests of the other party are often not completely understood. As a result, some things that seem all but impossible are accomplished easily, while others that seem simple result in protracted disagreement. Only the process itself, and the determination of the U.S. Congress, will determine the final character of Guam's political status change.

Thus, this report portrays potential scenarios. These scenarios are based upon available data, research into comparable conditions in other jurisdictions, socio-economic and political fundamentals, and the authors' own skills and experiences in Guam and the region. It represents a great deal of study and analysis, but in the end, it only reports the researchers' most likely

scenarios about a very uncertain future. There are many variables involved and innumerable possible outcomes for each of those variables. Interactions among the variables in a practical sense merely make the ultimate results of a status change less certain. Nevertheless, it is important to engage in this scenario building because, otherwise, it would be impossible to rationally contemplate the choices at all. It is evident that Guam considers the *status quo* to be unsatisfactory, both in political and in economic terms; a change is desired, so decisions must be made to move the people of Guam forward in their aspirations toward self-determination. This report, then, is developed to provide a reasonable, albeit limited, basis for the economic aspects of those decisions.

### **Basic Assumptions for Time Frame Conformity of the Analysis**

Since each of the proposed status options is expected to be achieved through the process of negotiation, there will obviously be a period of time between Guam's plebiscite to select an option and the implementation of that option. It is quite possible that the time period will be protracted, and that Guam's economy and the conditions under which it operates will change in the interim. Nonetheless, one of the objectives of this study is to provide a comparison of each status option at two points in time: immediately upon full implementation of each option, and again five years after such implementation. Because it is impossible to predict how long the status negotiations will last for any of the options, Guam's current economic circumstances will be used as the baseline against which the prospects under each option will be assessed. This introduces an element of unreality into the study, but one that cannot reasonably be avoided.

There is a common presumption that the selected status option will be implemented once its provisions have been negotiated, but this is not necessarily the case. With particular reference to statehood, it is likely that the final status will follow a series of interim statuses, starting with incorporation. The Statehood Task Force anticipates that Guam will finally achieve statehood at a more distant point in the future, anywhere from 25 to 100 years after the status plebiscite is conducted. This introduces an even greater level of artificiality to the analysis, since it is impossible to predict what economic conditions in Guam would be so far into the future as a baseline against which to compare the transition to statehood. Further, even if such future-based analysis were possible, it would not constitute a reasonable comparison to the other two status options. Therefore, it must be assumed that the date of implementation for Guam's status change will be the same regardless of which option is selected in the plebiscite. Further, it is assumed that the date will be near enough in the future so that the *status quo* at that time is sufficiently similar to existing economic conditions that the comparisons below are reliable.

### **Preconditions to an Orderly Transition**

For purposes of this study, it is assumed that the transition to a new political status for Guam is the result of a collaborative effort with the U.S. federal government, and that the terms of the resulting status are mutually agreed. Therefore, it is anticipated that the transition will be amicable and that both Guam and the U.S. will assist one another in making the transition as orderly as possible.

There are two additional assumptions that must be made to adequately present an analysis of the transition from the *status quo* to Guam's new political status. The first of these is that Guam will draft and adopt a constitution that is appropriate for its new status prior to the transition. The second is that a set of statutes defining the legal and economic structure under the

new status will be adopted before the change and ready to implement immediately at the time of the transition.

Guam does not presently have a constitution, and relies on the Organic Act as its basic guiding law. While this is not necessarily optimal from a legal or a political standpoint, it is nonetheless functional. With a transition to a new political status, though, Guam will need its own constitution, and it is desirable that it be adopted prior to the status change. Indeed, in the case of a transition to statehood, it appears that it is a necessary requirement, and that the constitution provides for a republican form of government and complies with the U.S. Constitution. In any case, Guam is contemplating one or another form of sovereignty, and defining the powers and authority of government within that context is necessary. Further, once the eligible voters of Guam have selected their desired political status and form of sovereignty by way of plebiscite, it is expected that the referendum for adoption of the provisions of a constitution will be open to all voters in Guam.

Similarly, there is a set of U.S. federal laws that currently applies to Guam (in addition to the Organic Act), some of which may continue to apply, some of which may apply in a different way, and some of which will no longer apply after the status change. Unless Guam has a set of laws prepared in advance of the transition to accommodate the changed application or termination of application of existing laws, there will be a vacuum in some areas that may (at least temporarily) be chaotic. To avoid this situation, a comprehensive set of laws must be in place at the time of transition, including those that replace laws that suddenly are no longer in force.

The reason for these assumptions within the context of this study is expediency: without a constitution and a comprehensive set of laws, the period after transition could be chaotic as the people of Guam rush to establish a functional government. It would be a time of confusion and uncertainty, and the resulting economic effects would not accurately represent the conditions that Guam would enjoy once its new status stabilized. Making these assumptions helps to avoid a depiction of Guam under its new status that is unfair, incomplete and inaccurate. There are enough complexities involved in defining the prospects for Guam's economy under three different status options without introducing the complications that the absence of these assumptions would entail.

## **Statehood**

This is by far the best-defined of Guam's political status options. There are fifty working examples of States within the United States, so it would be a simple matter to define the legal structure of economic relationships under this status. Despite the fact that each State is somewhat different from the others, both in its internal economic structure and in its relationship with the U.S. federal government, there is an overall uniformity that makes these differences seem inconsequential. It is unlikely that Guam, as a State, would deviate very much from this uniformity, so assessing the prospects under statehood is easier than for the other two options.

## **Immigration**

There is little difference anticipated between the *status quo* and statehood with regard to immigration into Guam. Guam would continue to be an eligible point of entry into the United States for those seeking permanent residence or naturalization, and all other aspects of the

naturalization process, including the residency requirement, would continue to apply. There are, however, some changes that should be anticipated in terms of the numbers of such arrivals. As a State, the preference for immigration into Guam could increase because of the improvement in perceived prestige of Guam's political status. Thus, there may be a slight-to-moderate increase in the number of new immigrants entering Guam. Both the positive and the negative impacts of new immigrants to Guam's economy, including its labor conditions, its educational system and its infrastructure, would be changed accordingly. The increases in the costs of infrastructure and education should be substantially offset by the economic contributions to gross domestic product and the tax base by the increased influx of immigrant workers; the net effect, although impossible to determine *a priori*, should be significant and positive.

Similarly, habitual residents arriving from the Republic of Palau, the Federated States of Micronesia or the Republic of the Marshall Islands would continue to have their entry into Guam unrestricted for the purposes of education, work and residency. Again, the improvement in the perceived prestige of Guam's new status may increase the number of habitual residents entering Guam somewhat. Because of the greater difficulties in assimilating unrestricted immigrants into Guam's society and economy, it is likely that there will be more significant net costs than those associated with immigrants from Asia. However, it is likely that the enhancement of Guam's representation in Congress with two voting Senators and a voting Representative would help ensure that Guam is properly compensated for the full cost of accommodating these habitual residents under the provisions of the respective Compacts of Free Association. Thus, the net effect of the status change on this aspect of immigration should be neutral or somewhat positive in the near-term. Given the evidence of the longer-term contributions of immigrants to the entrepreneurial growth of the United States, the long-term impact (which is not addressed in this study) may be very positive.

It is likely that statehood would bring with it a more strict application of the requirements for recruiting temporary alien laborers under the provisions of the Immigration and Nationality Act<sup>53</sup> in two ways. First, it is likely that the certification of the need for workers and their unavailability in the United States would revert from the Governor of Guam back to the U.S. Secretary of Labor, extending the time required in the certification process. Second, it is likely that the required search for suitable unemployed U.S. workers would be expanded to the entire nation. The resulting delays in the recruiting process could interfere with the importation of needed labor resources into Guam, particularly in the construction industry, causing Guam to lose opportunities to attract some types of investment. The prospective opportunity costs involved are inestimable, but potentially large.

## **Individual Rights**

It is anticipated that the rights of the people of Guam will be strongly protected under statehood, just as they are in the 50 existing States. These rights will include the right to vote in national elections, and to be represented by voting members in the Senate and the House of Representatives. This influence on the decisions of the U.S. federal government has the potential to significantly improve economic conditions in Guam, albeit indirectly, as greater attention is paid to the economic issues and constraints facing the island. However, under statehood the

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<sup>53</sup> INA §101(a)(15)(H)(ii)(b).

rights of Guam's Chamorro population may become indistinguishable from those of the population at large.

### *Nationality*

Nationality under statehood would be tied to the United States, which may hold nominal economic benefits for the people of Guam when they travel, but should have little or no substantive effect in comparison with the *status quo*. It is anticipated, though, that both cultural and linguistic linkages between Guam and the U.S. would continue to increase over time. This may ultimately have positive economic benefits (offset by some negative social costs), but they would be small.

### *Citizenship*

Under statehood, the people of Guam would enjoy U.S. citizenship, with all of the attendant rights, privileges and responsibilities. Guam would share equal and uniform economic and political benefits with the other member States of the Union. There are, though, few economic benefits directly associated with U.S. citizenship that are not already enjoyed by U.S. citizens residing in Guam.

### *Culture*

There would continue to be a liberal acceptance of multicultural backgrounds in Guam under statehood. However, there would be an implicit understanding and acceptance of the assimilation and displacement of the dominance of the Chamorro culture on the island, as it is replaced with a more homogeneous American standard. There is the possibility of nominal grants in aid from the U.S. federal government for projects in "cultural preservation," but these are anticipated to be economically insignificant.

### *Travel*

No change is expected regarding the rights of Guam residents to travel before or after the transition from the *status quo* to statehood. Consequently, there would be no economic impact.

### *Affirmations*

Guam would enjoy strong "states' rights" under statehood, with its political and economic agendas more effectively expressed by its voting representatives in Congress. The powers of the U.S. federal government would be more clearly and strictly defined by the uniform application of the U.S. Constitution in Guam, and the effects of the exercise of those powers would be more certain and better controlled. The mutual consent provisions of the U.S. Constitution would have the same meaning in Guam as they presently have in the existing 50 States. More effective representation, less uncertainty and a measure of self-government at the national and local levels could collectively have a significant impact on the operations of the economy of Guam, particularly through the exercise of the power to affect legislation and regulation affecting the island.

## *Protection of Rights*

In addition to the protections and stability accorded by the U.S. Constitution being fully applied in Guam, there will also be a state constitution in force. All personal rights, as defined at both levels of constitutional authority, will be protected, and Guam's government will have the ability to call upon the U.S. federal government to control civil disorder should the need arise. The rights of the Chamorro people, with few exceptions, will be largely indistinguishable from those of the population at large, except that there may be certain rights attached to Chamorro ethnicity, as a native American trait, that will differ. No significant economic impact is anticipated from this element during or after the transition to statehood from the *status quo*, although these universal rights would have modified Guam's progress and development had they applied some fifty years ago.

## **Legal and Judicial Framework**

### *Legal Framework*

If statehood is chosen, the *status quo* will be enhanced by the adoption of the entire U.S. Constitution. The extension of presently inapplicable provisions of the Constitution would reinforce the protection of personal rights and freedoms. While this clearly would have value in a social and political sense, the economic benefits are much more obscure, and would be largely immaterial to the overall performance of Guam's economy.

### *Judicial Framework*

If Guam accepts statehood, it is unlikely there will be any major change in the current judicial structure of the island. If statehood is selected, there may be a slight change in the role that the Ninth Circuit Court of Appeals plays in relation to the Supreme Court of Guam. However, no major changes or economic impacts are anticipated.

Federal funding of the judiciary will undoubtedly depend on the status option the people of Guam choose. If statehood is selected, federal funding of the judiciary would continue unaltered, at both the District Court and the local court levels. Therefore, there should be no economic impact whatsoever associated with this parameter within Guam's change in political status to statehood.

## **Foreign Affairs**

As a state, official representation of Guam's interests in all international forums will be immediately discontinued. The U.S. State Department will represent U.S. interests abroad, as it does on behalf of all states. All information and activities relating to Guam will be funneled through U.S. Foreign Service organizations.

However, Guam's interests and agenda would take on more importance in formulating U.S. policy positions and in negotiations because of its greater influence in the Congress. This may help to influence tax, trade, military and other relationships with foreign nations to the benefit of Guam. As a result, a series of economic benefits could be gained that would help to lower the cost of living and increase commercial and industrial opportunities.

## Land

Culturally, socially, politically and economically, land, land ownership and land title are some of the most important issues in Guam. These are made especially prominent because of the island's relatively small size and the overwhelming proportion of land resources that have been reserved for exclusive use by the local and U.S. governments.

Much of the land held by the local government is in use for public buildings, roadways, utilities and other strictly public purposes. A significant portion of what remains is reserved for the Chamorro Land Trust, for distribution under lease to indigenous residents who meet certain qualifications. The majority of what remains is land with steep slopes, submerged lands and other properties with low value. Despite some isolated and intermittent objections, the use of land by the government of Guam has not generally been subject to dispute.

In contrast, the land held by the U.S. government is primarily devoted to military reservations. While it serves a public purpose, that purpose is primarily for the benefit of persons residing in the 50 States, with only a residual value for the people of Guam. In addition, it is commonly perceived that the greater proportion of these lands is being underutilized (if used at all), and that its value to the resident community (*particularly* its value to the people of Guam) would be far greater if it was released to local civilian control. The value of releasable lands has been estimated to be as high as \$2.4 billion, the development of which would add \$145.2 million annually to the government of Guam in the form of additional tax revenues and a total of \$709.5 million to gross island product.<sup>54</sup>

Under statehood, it is anticipated that current title to property would be continued, and that it would be secure (as guaranteed by the Fifth Amendment to the U.S. Constitution). There would be little change in land tenure during the early stages of statehood. However, it is possible that the transition of Guam to a self-governing status would allow the U.S. government to prolong the delays in releasing lands scheduled for disposition because of a reduction or removal of associated international pressures to do so. It is also possible (but not anticipated) that the U.S. government would call upon the equal protection clause<sup>55</sup> of the Constitution to prohibit any kind of ethnic or racial deference in the distribution of Chamorro Land Trust lands.

The shift to self-determination as a State should not be underestimated in terms of its effect on property rights in Guam, particularly as they relate to the U.S. government. There are a number of issues related to land that could presently serve as an inhibitor to U.S. control, since it is a general rule in international forums that the resources of a non-self-governing place should be reserved to the indigenous residents of that place. Clearly, the U.S. has not felt bound by this convention, since both the privilege of immigration and the right to land title have been extremely liberally applied in Guam for nearly a half-century. However, once Guam becomes self-governing, the level of international scrutiny would dissipate, and the U.S. government's actions in Guam relative to land would be legitimized.

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<sup>54</sup> Calculations made in deriving these estimates are based upon the relationship between total taxes revenues and the appraised value of real property in Guam in 1997, the estimated value of §1104 payments for 1997 developed by Barakat & Chamberlin in their "*Analysis of the Impact of the U.S. Military Presence in Guam*," and the relationship between total tax revenues and Guam's estimated gross island product (gross domestic product) in 1997.

<sup>55</sup> United States Constitution, Fourteenth Amendment, Section 1.

## *Natural Resources*

Aside from Apra Harbor, Guam has very few land-based natural resources in the traditional sense. Essentially, there is acreage, some arable soil, and coral pits for mining limestone. There are no known mineral deposits of any commercial value on the island. A discussion of the prospects for agriculture has already been made, concluding that, because of high wage rates, moderate-to-poor soil conditions, and potential crop loss due to pests and typhoons, it is only viable on a small scale or as a subsistence industry.

Outside of the Harbor area, the dominant element in the value of most land in Guam is in its acreage. Growth in the residential and commercial use of land over the past 30 years has created scarcity and a corresponding increase in price. Much of the land that is held by the government, particularly within the U.S. federal estate, is considered to be quite desirable for development purposes, and abuts civilian land that has unusually high value. The expansion of civilian lands in Guam would have a dual impact, both increasing the acreage of privately developable land and helping to reduce land prices in general. Whether individually or combined, these impacts would help to attract both internal and external investment to expand Guam's economic base, as well as allowing a greater proportion of the population to be able to afford to own land.

Unfortunately, this prospect is limited and will perhaps be delayed under the statehood option, for reasons described above. As a mitigating factor, though, there would be increased political power that could be brought to bear on U.S. federal decisions because of Guam's sudden ascension to voting representation in both houses of the U.S. Congress. The attendant influence could help to ensure that U.S. federal lands in Guam are released according to schedule. Without the unnecessary delays inherent in the U.S. federal process and under provisions superior to those that have been agreed by Guam's leaders in past, land issues may finally be handled in a way that is amenable to all.

## *Ocean Resources*

There is currently disagreement as to whether Guam or the United States holds the rights to the resources found in the ocean within the 200-nautical mile Exclusive Economic Zone (EEZ) surrounding the island. Although Guam has prior claim to these resources,<sup>56</sup> they are also claimed by the United States.<sup>57</sup> The Legislative Findings in Guam P.L. 23-17 (enacted May 25, 1995) provide an argument defending Guam's claim to its EEZ, based in part upon the United States' signing on July 29, 1994, of the United Nations Convention on the Law of the Sea ("UNCLOS"). With respect to territories that are not self-governing, the UNCLOS declares that:

"In the case of a territory whose people have not attained full independence or other self-governing status recognized by the United Nations, or a territory under colonial domination, provisions concerning rights and interests under the Convention shall be

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<sup>56</sup> See GCA title 1, Chapter 1, §402, made effective on March 24, 1980 under P.L. 15-114.

<sup>57</sup> See Presidential Proclamation 5030, signed by President Ronald Reagan on March 10, 1983.

implemented for the benefit of the people of the territory with a view to promoting their well-being and development."<sup>58</sup>

However, with a transition by Guam to statehood, it is likely that the U.S. would reassert its claim to Guam's EEZ, and that the rights to all resources within the EEZ would then reside indisputably with the United States.

In any event, the current economic value of these resources is not substantial in comparison to Guam's land resources. Guam's surrounding waters do not have commercially valuable quantities of pelagic fish (with the exception of their value in subsistence and sports fishing), and the manganese nodules known to exist on the ocean floor in the deep waters surrounding the island are not commercially extractable using current technologies.

## **External Economic Development and Financial Assistance**

### *From the U.S.*

Guam is already the beneficiary of substantial financial assistance and economic development assistance from the United States. This assistance comes in the form of revenue sharing, grants and subsidized loans, as well as technical assistance. The level of this assistance is expected to increase under statehood because of Guam's voting representation in the U.S. Congress.

### *From International Organizations*

Guam currently receives a small amount of technical assistance from international organizations, most notably from the Economic and Social Commission for Asian and the Pacific (ESCAP, a United Nations organization), the World Health Organization (WHO), the South Pacific Regional Environmental Program (SPREP) and the SPC. The technical assistance generally comes in the form of training and small grant programs for specific health conditions. This type of assistance will almost certainly be discontinued with a change to statehood, because of the perception that the U.S. is better able to help its States, and that it should do so, rather than passing the burden on to the international community.

### *From Non-U.S. Nations*

Guam receives virtually no technical assistance and no financial assistance from foreign nations at an official level. This is expected to continue under statehood.

## **Tourism**

The attractiveness of Guam as a "U.S. destination" to travelers from Asia could be moderately enhanced under statehood. The island already experiences an advantage in regional tourism because of its status as a U.S. flag territory, operating under the U.S. rule of law and with the stability of the U.S. dollar. These characteristics of Guam provide tourists with a level

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<sup>58</sup> Final Act of the UNCLOS, Annex I, Resolution III, 1(a).

of security and prestige that no other destination in the region can match. As a State, the perception of these characteristics would be heightened.

The increase in attractiveness of Guam to travelers would be slightly offset by an increase in the difficulty in gaining access to the island. Two programs implemented within the past several years by the Department of State and the Immigration and Naturalization Service, the “Guam-Only Visa” and the “Visa-Waiver Program,” have made it easier for tourists to visit Guam. While the Visa-Waiver Program operates in general application throughout the immigration territory of the United States, the Guam-Only Visa is applied only to Guam. This latter program would likely be terminated during a transition to statehood, thus making it slightly more difficult for some travelers to gain entry into Guam. This may keep some potential visitors away from the island.

On net, it is expected that statehood would increase the number of visitors to Guam above trend, and that this higher trend would continue indefinitely.

## **Defense**

There are two primary economic aspects of defense in Guam. The first of these relates to the protection of lives and property from aggression, whether external (i.e., foreign) or internal (civil insurrection). This will be referred to as “military defense.” For the purposes of this report, the focus of the discussion of military defense will be protection against external threats; it will be assumed that internal threats will be dealt with by civil authorities.

The second economic aspect of defense, although perhaps less important in an historical context, is far more important from the perspective of the ongoing, day-to-day performance of Guam’s economy. The need for military defense brings with it the continuous use of vast amounts of land, labor and capital, for bases, troops and equipment. This will be referred to as “the defense industry,” since its operations are comparable in most respects to any other type of enterprise.

Military actions, as horrible and disruptive as they have been, have only occurred infrequently in Guam’s modern history; the operations of the defense industry, though, have been an ever-present activity in Guam, and have had a major impact on the economy. It is likely that this will continue in the foreseeable future.

### *Military Defense*

Historically, Guam has never been effectively defended in a military sense, other than through deterrence. Indeed, with the exception of the Japanese efforts in 1944, Guam has never been defended by force at all. The principal reason for this is that it is much easier to take a high island than to hold it. History is replete with examples.

Deterrence, though, is an extremely valuable role for the military to play in Guam. The island, its people and its infrastructure are protected without force, but also without the economic and human suffering and disruption that an attack from the outside would cause. Because of this, economic activity is allowed to continue unimpeded, and the welfare of the population is all but ensured.

Under statehood, the level of motivation of the United States in defending Guam would increase inestimably. From the national perspective, the military would be charged with

protecting a member of the Union, rather than just “a small place full of strangers that the country owns out there.” The level of effort put into defending Guam (and, consequently, its people and its economy) would be greatly increased. It is difficult to estimate the value of this without also estimating the value of the level of deterrence under the *status quo* and the level of risk of the exercise of foreign aggression. Nevertheless, it is clear that some value exists, and that it is potentially as high as the value of the island’s entire economy.

### *The Defense Industry*

The value of the defense *industry* in Guam is far more readily observable. There are Dollars spent, there are troops stationed, there are civilians hired, there are buildings built and there is land occupied. There are secondary industries, funding for related and unrelated programs, and a multitude of other effects that would be absent without the military presence. These are all measurable, but it is difficult to distinguish the impacts of the military industry in Guam on the civilian community, what we usually mean when we refer to “the economy,” from those impacts that adhere exclusively to the United States as a whole. Nonetheless, such a distinction is necessary in examining how a transition to statehood would affect the economy of Guam.

In the past, both the Navy and the Air Force prepared annual economic impact statements for Guam. They were impressive documents, full of facts and figures, analyses and charts, descriptions of missions and estimates of their respective contributions to the community. Unfortunately, there were deficiencies in the methodologies applied, and they consistently overstated the impacts that their operations had on the local community. For instance, if the Air Force re-outfitted its Guam offices with \$100,000 worth of new desks, this was counted as an economic impact in Guam, and even had a “multiplier”<sup>59</sup> applied to estimate the total impact of the expenditure on desks. In reality, though, the desks were purchased from a factory in, say, Ohio, and shipped to Guam aboard U.S. vessels that ported at Naval Station. Most of the impact of the expenditure took place in Ohio and the shipyards in California. The only impact in Guam was that military personnel had new desks; the benefit to the civilian community was entirely dubious. Only those instances in which income was actually generated in Guam’s civilian community had a local economic impact, and those were far less common than the impact statements would suggest.

Clearly, the defense industry in Guam does have an impact, most particularly through its employment of many people in Guam’s resident civilian population. There have been several attempts to estimate this impact, but they have repeatedly fallen short of their mark. It is probably safe to estimate that the impact on the civilian economy is somewhere between 10% and 15% of total expenditures budgeted for Guam (after applying a multiplier), but summary details and research are simply not available. Nonetheless, should the U.S. Armed Forces expand their operations in Guam after statehood is achieved, the impacts on the local community would expand as well.

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<sup>59</sup> The concept of a “multiplier” is essentially that one action leads to another and that there is a cumulative effect that is far greater than that of the initial action. For instance, if one person earns a Dollar, and spends \$0.90 in payment to another, a total of \$1.90 in income is received by the pair. If the second person then spends \$0.75 from his new income, the total impact reaches \$2.65. As the process continues, income within the community increases by far more than the original Dollar earned; the original income is “multiplied” by some factor, called the “multiplier.”

With the prospect of military expansion in Guam under statehood, a brief return to the subject of land is in order. At present, the U.S. federal government, through the operations of the Department of Defense, owns substantial properties in Guam that are excess to their current level of operations. While that level of operations is expected to increase under statehood, it is not likely that additional lands would be required (nor is it likely that those lands would be made available, given the political influence in Congress that Guam would have as a State). However, it is likely that there would be greater use of existing lands within the U.S. federal estate in Guam, and that this would make it more difficult for the civilian community in Guam to recover those lands from the military in the foreseeable future.

There is currently a moderate degree of turmoil related to the civilian impact of U.S. defense industry activities in Guam. This is most notably because of the “A-76” process, which is transferring many activities, previously reserved for U.S. federal civil service employees, to civilian contractors. Many functions that were previously performed by resident workers in Guam are now being delegated to civilian corporations under contract, and a reduced level of civilian employment is looming. In addition, the U.S. military in Guam has been scaling down its activities over the past decade, and civilian employment has already fallen correspondingly. This reduction in civilian employment related to the defense industry has further reduced the impact of the military presence on the civilian economy.

An expansion of the activities of the defense industry in Guam under statehood would have a positive impact on the civilian economy, but the proportional impact relative to the expansion is expected to be some 10% of the increase in budgetary expenditures, even with a multiplier applied. Although it is not at all clear how much expansion will occur, it is safe to assume that the impact of the expansion on the civilian community’s gross domestic product will be to add something in the range of \$30 million to \$100 million annually.

## **Transportation**

Little change in the transportation environment in Guam is anticipated under statehood, other than the possibility of increased funding for airport and seaport operations and infrastructure. The Civil Aeronautics Board (CAB) will continue to negotiate landing rights in Guam as a part of their comprehensive negotiations with their counterparts in other nations; Guam may receive some additional consideration in these negotiations because of its new political status, but the effects are expected to be nominal. The Federal Aviation Administration (FAA) will continue to control air traffic into and out of Guam with no change in their operational status. There may be a few million Dollars in additional funding available for airport and seaport infrastructure maintenance and expansion, but the overall impact of this would be insignificant to the economy. Highway funding is expected to remain the same as under the *status quo*.

Perhaps the most important impact, which is no change from the *status quo*, is that the Jones Act would continue to apply to Guam; there would be no relief from high surface shipping rates. It is possible that Guam’s voting representation in Washington would eventually be able to modify the impact of this law as it applies to Guam, but it is unlikely that this would occur within the study period, or that complete relief would be forthcoming. Thus, the effects on transportation during the transition to statehood are considered to be nominal.

## Trade

As a State, Guam would automatically enjoy duty- and quota-free trade with the other States; Headnote 3(a) and the Generalized System of Preferences would no longer apply. However, this would not constitute a significant change in practical terms, since manufacturing for export in Guam is not economically viable for most items. Labor and transportation costs, combined with a lack of raw materials, dictate that Guam exports services rather than goods.

Under statehood, Guam would become a part of the Customs Territory of the United States, and so be subject to import quotas on some goods from some foreign nations. While the quota issue is probably unimportant because of the small volume of imports into Guam relative to the United States as a whole, there is also the issue of import tariffs imposed under the Harmonized Tariff Schedule of the United States. Some goods brought into the island from foreign nations would be subject to a duty (an import tax) that would be paid into the U.S. Treasury, directly raising the cost of living in Guam.<sup>60</sup> There may also be some trade restrictions in relation to some foreign nations to which Guam is not currently subject. These restrictions are often part of the economic sanctions that the U.S. sometimes imposes in an attempt to influence the policies of foreign governments, but typically do not apply in Guam under the *status quo*.

In other respects, trade in Guam would not change significantly with a status change to statehood. The island would still be a net importer of goods and export activity would continue to be dominated by pass-through trade. On net, the cost of some goods would rise because of import duties and other goods may become less available because of quotas or other trade restrictions.

However, the higher costs of some goods imported into Guam may have an adverse impact on tourism spending, reducing average levels of retail spending. The number of tourists may decline modestly as well, listing “shopping” in exit polls as being among the reasons that they selected Guam as their travel destination.

## Attractiveness of Investment

Guam would continue to offer relatively unrestricted investment opportunities under statehood, with little change from the *status quo*. However, because of full state’s rights and the increased stability associated with statehood within the U.S. system, these opportunities may appear more attractive, locally, at the national level and internationally, providing an impetus for increased investment. Unfortunately, the increase in taxes in Guam under statehood would serve to offset the increased stability in making investment decisions, and may ultimately make Guam a less attractive place to invest from some perspectives.

Presently, Guam has a set of investment incentive programs, offering both low interest rate loans and reduced taxes to new enterprises in select industries. The abatement of real property taxes and gross receipts taxes could continue, but the Guam Economic Development Authority could no longer offer to rebate corporate and personal income taxes collected under the mirror of

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<sup>60</sup> These duties would only apply to some goods, and the tax rate would be fairly low for those items that are affected. In the modern regime of liberalized international trade, these trade restrictions are gradually being reduced in any case. However, as long as they are in place, they tend to raise the overall price of goods and to distort the relative prices among goods, discouraging some types of consumption of foreign products versus their domestically-produced substitutes.

the Internal Revenue Code. Under statehood, those tax revenues would flow to the U.S. federal government rather than the local government, and Guam would have no latitude to determine how they are used. Should Guam implement its own income tax (a move which appears inevitable under statehood), the State government could, of course, rebate or even abate a part or all of those taxes in order to attract investment. Nonetheless, the available tax incentives could not be as attractive as under the present system, since only part or all of a higher tax could be forgiven, but no part of the income tax that exists under the *status quo* could be rebated.

Although Guam collects its income taxes under a mirror of the Internal Revenue Code (IRC), the island is typically not a party to the various tax treaties that the U.S. has with some other countries. Under the IRC, the distribution of wages and profits to residents of foreign nations is subject to withholding at a 30% rate; this provides an incentive for the recipients of this income to file a U.S. (or Guam) tax return. However, under U.S. tax treaties with some foreign nations (Japan, for instance), this rate is reduced (in Japan's case, to 10%). Because Guam is not a party to the treaty with Japan, though, wage and profit disbursements to Japan are still subject to the 30% withholding rate. This is considered by some to be a disincentive to invest in Guam (although there is no difference, except in interest earnings, to those who file their tax returns on Guam-source income as required by law), but it would be relieved under statehood.

As a final element of the attractiveness of investment in Guam under statehood, there would be the continuing authority for the Guam government to issue tax-exempt bonds on its own account and for some authorized private purposes. This would not be a change from the *status quo*.

## **Labor**

There would be only two changes in the labor environment in Guam with a transition from the *status quo* to statehood. First, as mentioned above, it may be more difficult and costly to recruit non-resident alien labor under statehood due to a total reversion of control to the U.S. federal government. Second, an unemployment compensation system would be implemented, with the attendant direct costs to employers and indirect costs to employees. Unemployment compensation costs typically make up some 0.6%<sup>61</sup> of the wage bill in the United States, so employers could expect to pay a slightly higher amount for their workers, and workers could expect lower gross wage rates, helping to share this increase in costs. A slight increase in unemployment may also occur.

Other U.S. federal labor laws and regulations would continue to apply to Guam under statehood, including:

- Fair Labor Standards Act
- Occupational Safety and Health (OSHA) standards
- Fair Employment Practices (EEO)

Additional labor programs would also continue in Guam, including:

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<sup>61</sup> *News*, United States Department of Labor, USDL: 99-173, June 24, 1999. This is the average for civilian employers in the United States as of March 1999. The average rate for civilian workers in U.S. service industries, which dominate Guam's economy, was 1.0% at that time.

- Federal and local statistical programs
- Employment and placement programs (such as the Employment Service and programs administered by the Agency for Human Resources Development)

### **Other Private Sector Considerations**

Because U.S. laws and regulations would continue to apply, there are no significant changes anticipated due to a transition to statehood other than those enumerated under the other sections this segment of this report.

### **Health**

In contrast to the *status quo*, all U.S. federal health programs, grants and technical assistance would apply in Guam under statehood. This would increase outside funding for health programs in Guam, from nutrition through treatment to research. In addition, there are a number of areas where Guam has an unusually high incidence of health problems (such as diabetes), which may attract even more funding. Improved matching funds formulae and the removal of expenditure caps for some U.S. federal programs in Guam could help to reduce the local government's expenditures on health care, or improve the level of services available.

Although Guam is presently a participant in several international health organizations, this participation would likely cease upon a transition to statehood, with the U.S. government taking over representation on Guam's behalf. Information disseminated through these organizations would reach Guam through a different route, but most would still be available (although somewhat delayed, if not altogether absent). The delay or absence of information on regional health trends could make preventative efforts less timely or effective.

### **Education**

The unusually high costs of education in Guam, which are partially due to the island's expenses in assimilating students of a multilingual, multicultural background into an American society, would continue unabated. However, as a State, it is likely that Guam would focus additional efforts on meeting or exceeding mainland standards in education; those efforts will require additional funding. While there may be access to higher U.S. federal education grants as a State, U.S. performance standards would have to be adopted to achieve and maintain eligibility. Therefore, it will be necessary for Guam to secure additional funding internally at the outset, and this will most likely be achieved through increases in the real property tax rate.

Once uniform U.S. standards are met in education in Guam, it is likely that the DODEA schools would reintegrate with the local public school system, bringing a resumption of impact funding. The influence of Guam's voting representatives in the U.S. Congress may also help to bring in more direct student financial aid.

Once Guam's educational standards reach national performance levels, the island will have a higher skilled workforce, generating greater productivity and increases in *per capita* income. However, this result would occur outside of the study period of this report.

## Fiscal and Monetary Policy

As a State, Guam would continue to use the U.S. Dollar as its medium of exchange and unit of account. Because the Dollar is issued by the U.S. government, Guam would have no independent control over monetary policy.

Guam would, however, have control over its internal fiscal policy, including public debt, local taxation and local expenditures (within the limits of U.S. law). The limitation in the Organic Act that, “no public indebtedness of Guam shall be authorized or allowed in excess of 10 per centum of the aggregate tax valuation of the property in Guam,”<sup>62</sup> would cease to apply.

The U.S. federal government would also continue to exercise control over its fiscal policy, and elements of this policy would continue to affect Guam. It is likely that, with voting representation in both Houses of the U.S. Congress, Guam would fare better under U.S. fiscal policy as a State than it does under the *status quo*.

### Taxation

The change in the structure of taxation would be perhaps the most adverse aspect of a transition to statehood for Guam. At the time of the transition, the Organic Act, including §§30 and 31,<sup>63</sup> would terminate, and Guam would lose approximately 60%<sup>64</sup> of its tax revenues. This would obviously be catastrophic from a fiscal policy perspective, and either those revenues would have to be replaced from another source or public services and employment in Guam would have to be sharply curtailed.<sup>65</sup>

There are a number of ways that this reduction in revenues could be replaced, but each would have a depressing effect on the economy, and some would also have the effect of redistributing income, wealth or both.

Implementing a state income tax would be one way of replacing the lost revenues, but even the implementation of a parallel to the Internal Revenue Code would not replace all of the lost revenues, since the §30 receipts would not be replaced. The new income tax would have to be levied at approximately 114% of the current income tax rates to recover all lost revenues; this would increase the average taxpayer’s tax burden by some 61%. The fact that the income tax is a progressive tax means that higher income individuals would bear a proportionately higher burden than lower income individuals, redistributing disposable income toward greater equality, but severely reducing the amount of savings and internally generated investment in the economy. In addition, in combination with other taxes, the total tax burden in Guam would increase from

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<sup>62</sup> 48 USC Chapter 8A, §1423a.

<sup>63</sup> Found at 48 USC Chapter 8A, §§1421h and 1421i. §1421h reserves for Guam (among other revenues) all receipts of income tax paid under the Internal Revenue Code of the United States by U.S. federal government employees either resident of or domiciled in Guam; §1421i applies a “mirror” of the Internal Revenue Code to Guam, but makes the receipts of that tax payable into the Treasury of Guam rather than the U.S. Treasury.

<sup>64</sup> Data developed from *1994 – 1997 Annual Report*, Department of Revenue & Taxation, Government of Guam, Table on pg. 7.

<sup>65</sup> It is noted that there are seven States (Alaska, Florida, Nevada, South Dakota, Texas, Washington and Wyoming) that do not levy a state income tax. However, each of those States has other sources of revenues that are unavailable to Guam, at least at this time.

approximately 20% to approximately 32%. While this tax burden would still be at the bottom of the range of tax burden among the States, the impact on standards of living would be harsh, as overall disposable income falls by some 15%.

Other taxes could be increased to help recover the lost revenues resulting from the termination of §§30 and 31 of the Organic Act, but most other taxes (such as the gross receipts tax and the liquid fuels tax) are regressive. A regressive tax is one through which lower income individuals pay a higher proportion of their income in the tax than do higher income individuals. Raising the necessary revenues through an increase in a regressive tax would also have a redistributive effect on disposable income, but away from equality rather than toward it.

It is unclear whether the property tax is progressive or regressive in Guam, since even those who do not own property indirectly bear some burden of the tax through their rental rates. However, on net the tax is probably mildly progressive.

As an alternative to raising taxes, government services and employment could be curtailed in response to a sudden reduction in tax receipts by the government of Guam. However, there are few services currently provided by the local government that would be provided by the U.S. federal government under statehood, so there would be a substantial net reduction in overall government services.

There would also be a substantial loss of the corresponding local government jobs (as many as 8,000). This, too, would have a devastating effect on the economy.

A third alternative would be to combine the two extremes, both raising taxes and reducing government services and employment. In any event, though, the negative impact on the economy of suddenly removing approximately 12% of gross domestic product (“gross island product”) from the system in the form of tax payments to the U.S. federal government would, by itself, be severe.

### *Transfer Payments*

The U.S. federal government funds a number of entitlement programs in Guam, many of them providing transfer payments to individuals. Commonly known as social welfare programs, some of these are only partially funded by the U.S., with some level of matching funds being provided by the local government. Many of the more prominent programs operate this way, but the level of the U.S. federal share of the costs is often lower in Guam than it is in the States. Further, there is often a designated maximum total amount, a “cap,” imposed on the U.S. federal expenditure in support of the program costs, with the result that the local matching proportion of the program cost is much higher than the matching percentage would indicate.

As a partial offset to the reversion of current income tax revenues to the U.S. Treasury, Guam would receive full- or higher-match funding for several social welfare programs, and the caps on U.S. federal expenditures on the programs would be lifted. As a result, some \$10 million to \$15 million that the government of Guam currently spends on these programs would be replaced by U.S. federal expenditures, and saved by the local government.

In addition, as a State, the Supplemental Security Income (SSI) program would be extended to the island. SSI provides transfer payments to those in society who are generally agreed to be the most needy: the aged, the blind and the disabled. In the early 1970s, the SSI program replaced three older programs in the States and the District of Columbia. Those older

programs were Old Age Assistance, Aid to the Blind, and Aid to the Permanently and Totally Disabled. While the older programs were funded with state and federal matching funds, SSI is 100% federally funded. SSI was not extended to the territories at the time because of disparities in *per capita* income; the U.S. government thought that the relatively high level of benefits payments would be “socially and economically disruptive” if they were paid in Guam, Puerto Rico, American Samoa or the U.S. Virgin Islands. Although the benefits available to recipients under the older programs in Guam today are higher than the level of SSI benefits paid in the States (and Guam pays higher than its matching share because of program expenditure caps), SSI has still not been extended to the island’s needy. Under statehood, this situation would change, and Guam would receive an additional \$10 million to \$15 million annually in U.S. federal funding for the SSI program.

### *Retirement Programs*

There are no changes anticipated in the Social Security or Medicare programs available in Guam as a result of the transition to statehood, and therefore there would be no economic impact under this category because of the status change.

### **Distribution of Income**

The modern history of Guam’s economic development has been one of dichotomy: one portion of society has progressed fairly rapidly in terms of participation in the “mainstream” economy, experiencing rising standards of living and a “western” working environment. Another portion of society has remained relatively static, maintaining more traditional employment patterns and slower changes in its standard of living. Over time, the gulf between the two is observed to have been widening.<sup>66</sup>

Under statehood, there will be two forces affecting the dichotomy in Guam’s society, pulling in opposite directions. The first of these relates to the tax structure of the island, where the tax burden is expected to become more progressive. This force will serve to make standards of living more equal across all classes, albeit at a lower standard for nearly everyone. The second force relates more to the social assimilation of Guam into American society. This force will tend to continue and accelerate the process that has been ongoing in Guam for decades (or even centuries, considering the Chamorro experience under Spanish rule).

It is not possible to estimate at this point which of these forces will prevail, so the effect on the distribution of income of the transition to statehood is indeterminate.

### **Free Association**

Although far less firmly defined than statehood, the analysis of the free association option has the benefit of fairly recent examples of change in the Republic of Palau, the Federated States of Micronesia and the Republic of the Marshall Islands (collectively, the “Freely Associated States”). These three former Trust Territories began negotiating their sovereignty in the 1970s, and the latter two were granted their new status in 1986; Palau made its transition in 1994. As a part of their Compacts of Free Association, each of these three nations received substantial

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<sup>66</sup> This is indicated both by the research conducted by John D. Gilliam in the early 1990s and by various reports from the Bureau of Labor Statistics of the Guam Department of Labor on household income.

economic aid and assistance packages from the United States. The use of the Compact funds has had mixed success in the FSM and the Marshalls, and continued funding is open to negotiation this year. Palau has used its funding more effectively, and is commencing a major public works project to further develop the resources of the nation's largest island, Babeldaub.

Both the FSM and the Marshalls have faced the problem of developing new economies where essentially none existed before. Aside from small pockets of trade and light industry, the principal engine of these two nations' economies under the Trusteeship was public administration, which still dominates economic activity. Population, available resources and remote location have made the task of economic reform particularly difficult, and standards of living remain generally poor. In the Marshall Islands, the primary cash economy is based upon copra, and there is a price disadvantage in comparison to other places in South America and Asia because of transportation costs; fishing activity is mostly subsistence, and the tourism industry is miniscule. In the FSM, commercial fishing activity has grown substantially, but is primarily concentrated among foreign fleets that pay licensing fees to fish in the nation's expansive waters. Although tourism is growing in importance, the industry is still in its infancy, and there is little capital available to support its growth in the near term.

Palau's economy is better developed, with agriculture, fisheries and tourism each providing significant employment. Standards of living are correspondingly higher than in the other two former Trust Territories. Since its status change, Palau has been able to attract both Japanese and Taiwanese investment, in part because of superior infrastructure. Nonetheless, there are still a number of improvements to be made in the nation's economy, but a reasoned, methodical approach to development is helping to avoid many of the obstacles that were encountered by the other two jurisdictions.

Each of the Freely Associated States has joined several international organizations, including the United Nations, and has significant access to technical assistance and other economic development programs. Each, though, has established land alienation restrictions, prohibiting those not native to the islands from owning real property (at least for a period of years). This is generally viewed from two perspectives: First, it reserves the resources of the islands for the indigenous population. Second, though, it sometimes interferes with the attraction of foreign investment, and may be hampering the pace of economic growth in each jurisdiction.

Because of the difference in Guam's current political status from the Freely Associated States prior to their transition (flag territory v. Trust Territories), there are likely to be significant deviations between Guam's negotiated status and those of the others. However, there is sufficient experience with the free association model in recent years to draw several comparisons in various factors under consideration in this report.

## **Immigration**

It is expected that Guam will control its own immigration policy under free association, and that the island will no longer be a point of entry for U.S. immigration; time spent in Guam will not be counted toward residency for U.S. naturalization purposes. It is also unlikely that the free entry of habitual residents from the Freely Associated States for residency or work will continue; entry of FAS citizens would nonetheless be allowed on a temporary basis for tourism, visiting relatives and educational purposes. However, it is expected that free entry of U.S. citizens and Guam citizens from Guam into the United States will continue, including entry for

purposes of work and residency, and that open immigration into Guam by U.S. citizens will be allowed.

Guam's immigration policy will be based upon the needs of the island and the net economic benefits that immigration often provides. Therefore, Guam will establish a quota for new immigrants from various other countries and will promulgate procedures for attaining naturalization; this quota may change periodically to reflect evolving economic circumstances. Guam will also establish a relatively liberal policy for entry by tourists and business travelers, non-immigrant workers and inter-company transferees. In order to control immigration and permanent residency, it is likely that there will be few economic or social benefits available to short-term residents and non-citizens.

Because of its continuing relationship with the U.S. in defense matters, Guam's immigration policies will be structured to accommodate U.S. security concerns. In this regard, Guam will work closely with the U.S. federal government in establishing some aspects of its own foreign policy.<sup>67</sup>

The local control of immigration into Guam will carry several economic benefits, although there are no changes from the current system that are anticipated to affect tourist or business travelers, or inter-company transfers. The conditions for obtaining an investor's visa into Guam would be liberalized, reflecting the island's less-developed economic status in comparison to the United States.

In terms of costs, the current demands on infrastructure and the educational system imposed by relatively unrestricted immigration will be moderated. Many of the costs associated with law enforcement and social benefits programs due to unrestricted immigration will be avoided. With the residency requirements toward U.S. citizenship no longer being met in Guam, those who do immigrate to the island are more likely to remain in residence permanently, allowing a more complete recovery of the costs associated with their assimilation.

The process of recruiting non-immigrant labor during times of economic expansion would be simplified, avoiding many of the delays encountered under the *status quo*. Thus, enterprises in Guam could react more quickly and effectively to investment opportunities, accelerating the rate of growth in the economy during expansionary periods. In addition, a preference program for admitting immigrant workers would be designed to give preference to those having skills in short supply in Guam.

There is one risk associated with free association in terms of immigration that must be acknowledged. Given the uncertainty involved with a status transition of this type, it is possible that Guam would experience a moderate amount of emigration before and during the status transition, as expatriates from the U.S. and immigrants from elsewhere choose to seek residence elsewhere. There is the potential that this could adversely affect Guam's economy because of the loss of some professionals, entrepreneurs, managers and skilled workers.

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<sup>67</sup> Some have suggested that Guam's immigration laws and policies should be enforced under contract by the U.S. Immigration and Naturalization Service, because of that agency's experience and expertise in these matters. However, that is a proposal that is subject to negotiation, and is by no means a certainty under Guam's new status.

## Individual Rights

As noted in the overall assumptions, it is anticipated that individual rights under free association will be protected by a constitution in Guam that is adopted by general referendum. These rights are likely to be substantially the same as those in the U.S. model. This anticipation is reinforced by the expected close relationship between Guam and the United States, and Guam's acceptance of international standards of individual human rights. However, deferential rights for the indigenous residents of Guam are likely to be affirmed under Guam's constitution.

### *Nationality*

Under free association, the nationality of those residing in Guam permanently will be Guamanian. The culture in Guam will be relatively more Chamorro, but there will also be relatively more linkages with the United States because of the affirmation of the association between the two nations.

### *Citizenship*

Because of the current status of Guam and the residents of Guam in relationship with the United States, this is one of the more difficult and ambiguous issues involved in a transition to free association. In this regard, it is one of the primary levers that will be manipulated by the United States in its negotiations toward a freely associated Guam, just as it was with the Northern Marianas and has been with Puerto Rico. Because this is one element in the overall negotiation process, the value of U.S. citizenship to the people of Guam must be carefully weighed.

It is beyond the scope of this report to fully discuss all of the political and social aspects of citizenship; only the economic aspects are to be considered here. However, there will certainly be extensive discussions surrounding this issue as the political status debate moves forward. For the purposes of this report, it is assumed that dual citizenship rights will be allowed for those citizens of Guam who have the rights of U.S. citizens at the time of transition to free association. The U.S. citizenship of future generations is possible under the principle of *jus sanguinis*,<sup>68</sup> but this is far from certain in a situation of a voluntary change in political status. The U.S. citizenship of those in Guam who are not U.S. citizens at the time of the transition to free association is not likely; it is possible that they would become citizens of Guam, or remain citizens of their home countries.

For many people, the economic aspects of citizenship are relatively unimportant, except as it relates to rights to and ease of travel, the protection of and recourse to U.S. consulates and embassies while in foreign nations, and other factors considered elsewhere in this report. For a large segment of the population, though, U.S. citizenship holds the promise of assured stability and affirmed economic rights as the foundation for their economic wealth and prospects for the future. Either position is a matter of personal perception, and no judgement is necessary for the purposes of this report.

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<sup>68</sup> Latin; "law of the blood," meaning "blood right," and referring to citizenship based on ancestry. Under this principle, a child inherits the citizenship of its parents, regardless of where it is born.

Under free association, all citizens of Guam (whether U.S. citizens or not) will be subject to the constitution of Guam while in Guam, and the protections of the U.S. Constitution will not apply, except as replicated in Guam's constitution. There may, however, be diplomatic relations between the U.S. and Guam which could extend some advantages to citizens of Guam that are not usually accorded to non-citizens of the United States. For instance, citizens of the Republic of Palau have access to the protection and programs of U.S. embassies abroad.

### *Culture*

Although there will be a stronger manifestation of the Chamorro culture under free association than there is under the *status quo*, there will remain a very liberal and open acceptance of other cultures in a tradition that predates Spanish colonization. The use of the Chamorro language will become more common in everyday conversation and in public debate, but U.S. English will remain as the most common means of communication for business and instruction. Close ties to the U.S. will mean that there is a continuing influence of the U.S. "culture" in Guam, but increased effort and resources devoted to preserving the Chamorro culture may have a modest impact on the relationship, and have the potential to enhance the tourism industry. Any economic effect will not be significant.

### *Travel*

Travel to and from the United States, for whatever reason, will be relatively unrestricted under free association for citizens of Guam, and there will be no visa requirements. International travel for Guam citizens will be completely unrestricted by the U.S., as long as the appropriate visas are obtained, since U.S. travel restrictions will not apply. However, it may be more difficult for people traveling with Guam passports to gain entry into some countries until those passports are recognized and acknowledged internationally.

Even so, Guam citizens, whether or not they are dual citizens of the U.S., will have access to and the protection of U.S. consulates and embassies abroad. The economic impact of this is expected to be moderate, but may be significant in some individual instances.

### *Affirmations*

Under free association, the relationship between Guam and the United States can be terminated at any time by the unilateral decision of either nation. However, this is unlikely to occur because of the close relationship that is anticipated. This relationship will be based upon mutual understanding and respect, and there should be few areas of contention since the U.S. will freely accept Guam's political status. In return, Guam will freely accept the continuation of U.S. policy as it relates directly and indirectly to matters of defense. Because of this relationship, there may be a continuation of U.S. policy in Guam in many significant areas to which the island voluntarily agrees.

As a sovereign nation, most of the decisions made in Guam will be unilateral, without concern for the views of the United States. The only areas of contention may relate to defense and to mutual cooperation. Guam, though, agrees to the primacy of U.S. military interests in the relationship, enabling the U.S. to deny access to Guam for national security purposes. Guam is likely to acquire substantial U.S. economic development aid in exchange for this concession.

Although subject to negotiation, the benefits to Guam under this arrangement could be far higher than current levels of assistance.

### *Protection of Rights*

Rights in Guam will be protected under a constitution and a set of laws that are very similar to the U.S. model after free association is implemented. However, there may be some constitutional provisions for Chamorro preferences, particularly in the area of access to Chamorro Land Trust lands.

As a matter of continuing policy, Guam will not abridge the rights of any guest resident or visitor. On the contrary, in keeping with established tradition, the people of Guam will convey an ongoing feeling of welcome to all suitably respectful guests and visitors to the island.

The more firmly established is the protection of rights in Guam, the more attractive the island will be for both tourists and investors. The economic value of these protections, while strongly positive, is inestimable.

### **Legal and Judicial Framework**

Legal rights in Guam would be negotiated if the island's eligible voters choose free association in the plebiscite. Guam could either reenact existing laws (i.e., substantially maintain the *status quo*), or create an entirely new code and constitution that differs in indeterminate ways from the *status quo*. Under free association, the government and constitution of Guam would determine legal rights in Guam.

Guam's current legal and economic stability would be at least temporarily affected if free association is chosen, even if the island's legal structure is maintained. As it stands under the *status quo*, the Guam Code Annotated and the Organic Act have provisions respecting business and the economy, with U.S. federal oversight. Examples include the contracts clause contained in Article 1 of the Constitution, the takings clause of the 5<sup>th</sup> Amendment, civil procedure, remedies, business regulation, real property law, business structure and function, the Uniform Commercial Code and the Uniform Consumer Credit Code. Under free association, without U.S. federal oversight, any number of changes could occur that, *a priori*, are unpredictable. Stability is critical to economic performance and growth, and the economy could suffer, perhaps substantially, if legal stability and the protection of economic rights were removed or significantly altered.

If the eligible voters of Guam accept free association, it is unlikely there will be any major change in the current judicial structure of the island. Federal funding of the judiciary, though, will undoubtedly depend on the status option the people of Guam choose. If free association is chosen, federal funding would be subject to negotiation. The results of this negotiation cannot be foretold, but over the past seven years, the Superior Court of Guam has benefited from some \$4.26 million in federal appropriations.

### **Foreign Affairs**

It is expected that Guam and the United States would exchange diplomatic representatives at the State Department level once Guam makes the transition to free association. Among other things, this will allow the rapid and systematic resolution of most matters relating to economic

cooperation. However, Guam would have no official representation to the U.S. Congress; any delegation to the Congress would essentially be as an observer, and would serve more as a liaison in matters related to the budgetary process relative to the annual funding of negotiated aid programs for Guam.

Because of its limited sovereignty in foreign affairs due to the role that the U.S. plays in the military defense of the island, Guam would concede to the interests of the United States in several significant affairs of state. However, Guam would simultaneously maintain a separate international profile, and would establish consulates in selected foreign nations (i.e., Japan, Taiwan, South Korea and the Philippines) for the conduct of economic and other affairs. Guam would enter into bilateral and multilateral trade negotiations and agreements, and would participate in regional and international organizations, including the United Nations, however it desires. However, Guam would also defer to the U.S. federal government on many issues out of recognition and respect for the greater leverage wielded by the U.S. in international negotiations.

It is anticipated that Guam would establish a closer relationship at a diplomatic level with the other U.S.-affiliated Micronesian nations for mutual benefit. While this may be a time consuming process because of historical issues, such a consortium would allow each of the islands to more effectively coordinate their own foreign policies with one another and with those of the United States.

## **Land**

Secure title to private property will be continued under free association, but there may be restrictions on the transfer of land to persons who are either not Guam nationals or, in the extreme case, who are not indigenous to Guam. The Chamorro Land Trust will remain intact, and will no longer suffer the risk of legal challenge under U.S. law, since that law will no longer apply in Guam. However, either Guam's constitution or laws will define the available property rights in Guam of foreign national and commercial interests. It is anticipated that foreign ownership of land will continue to be allowed in Guam under conditions similar to the *status quo*, but that there will be restrictions placed on the sale of land currently owned by the government to non-citizens.

The U.S. federal government will have incentives to reduce and even minimize its landholdings in Guam. While it is unlikely that the U.S. government will be required (or willing) to make lease payments for the land that it occupies in Guam, it is likely that the U.S. will be compelled to provide both defense services and economic aid in exchange for the right to maintain military bases in Guam. For national security reasons, it is likely that ownership of land in Guam by foreign governments will be prohibited under agreement with the United States, except as such ownership relates to embassies, consulates and other diplomatic missions of such governments.

It is anticipated that, by some mutually agreed formula, the more land that the U.S. federal government desires to retain, the higher will be the corresponding economic assistance. Because of the high inherent scarcity value of Guam's land, the economic impact of this arrangement is expected to be positive and substantial.

It is also expected that Guam will develop a set of tax and other incentives for the private development of land for approved commercial and residential purposes. These incentives would

stimulate increased local and international investment, and further enhance the economic value of land in the intermediate- to long-term.

### *Natural Resources*

The utilization of land and other natural resources under free association would be subject to local law and selectively adopted international convention, with more flexibility in environmental standards than under the *status quo*. This will be particularly so as it relates to the use of private land, some of which is currently constrained by an apparently arbitrary “natural habitat” overlay.

There is likely to be continued coordination with U.S. government environmental programs related to various types of pollution, particularly of water and the soil, as well as increased participation in Pacific regional environmental and resource management programs.

As a side effect of other characteristics of free association in Guam, the current level of strain on some classes of renewable resources will be mitigated, partly as a result of reduced immigration and partly because of a more comprehensive and unified land use plan.

### *Ocean Resources*

As an independent nation in free association with the United States, Guam would enjoy undisputed control over its Exclusive Economic Zone. While this may hold economic promise in the indefinite future, once technology progresses and manganese prices rise, the current benefits are less pronounced. In conjunction with control, Guam will incur enforcement costs (to the extent that enforcement is economically viable); however, at least a portion of these costs will be offset by cooperative agreements for commercial and scientific ventures, as well as by U.S. and possible international grants-in-aid.

## **External Economic Development and Financial Assistance**

Under free association, Guam will continue its evolution in focusing on support for development and growth of the private sector. As a U.S. colony, the focus throughout history has been on the development of public administration, with little attention paid to private economic development, except as it has benefited the administering power. Since the mid-1960s, this focus has gradually changed, but this change is expected to accelerate as Guam recognizes that political independence enables economic independence, as well, and *vice versa*.

With improved access to international and regional organizations, as well as a heightened awareness of self-reliance, strong economic development planning is expected to become more central to the political decision making process. With this imperative linked to financial assistance from the U.S. as a result of negotiations over defense and access rights, substantial opportunities will arise for another renaissance in the island’s economic growth. Nevertheless, Guam will initially gravitate toward the U.S. for the majority of its development funding, and technical assistance will be focused on clearly identified and mutually agreed capital formation and economic development goals.

More attention will be given to tax- and trade-related investment incentives, and less to social support programs. Initially, the U.S. Department of the Interior will coordinate U.S.

federal program funding, but responsibility for these matters will revert to the U.S. State fairly quickly.

Private development programs, while constrained by a somewhat higher initial level of political and economic uncertainty, will be supported by a level of corporate and individual income tax policy incentives that were not possible in the past.

Bilateral and multilateral governmental assistance, both from the U.S. and from other nations, will increase gradually as Guam systematically reduces its dependence on the U.S. and increasingly focuses its attention on its role in the Asian-Pacific economic sphere. This process will extend beyond the term of this report's time horizon, but will begin during the period under consideration, with generally favorable economic results.

## **Tourism**

The sun, the sand and the sea in Guam are constants that will not be affected at all by whatever political status Guam's eligible voters choose. Similarly, the island's tropical climate and location in proximity to the emerging Asian nations will not change. Nonetheless, the transition to free association will bring with it a certain amount of perceived turmoil, and it is likely that there will be a moderate decrease in visitor arrivals to Guam during the first year or two after the status change. This will be due to market and tour operator concerns in Japan and elsewhere regarding security and the uncertainty surrounding political stability.

A more positive aspect of the change will be that Guam (rather than the U.S.) will generally determine the admissibility of visitors through Guam's ports of entry (within the constraints imposed by the defense considerations with the U.S.). The longer-term effect will be a stronger tourism industry than under the *status quo*, as continued stability and ties with the U.S. become more evident and Guam provides more attractive tax (and other) incentives for airlines, tour operators and tourism infrastructure/superstructure investors. This impact may be slightly moderated, though, by the absence of the U.S. flag flying over the airport, since one of the attractions of Guam to some tourists is that it is a "U.S." destination today.

## **Defense**

As in the former Trust Territories, it is expected that defense will be a U.S. responsibility to Guam under free association, as the island's military value has always been the primary interest of the United States in Guam.<sup>69</sup> The primary objective of the United States' interest in Guam and the other states of Micronesia is U.S. hegemony in the region as a remote defense against attacks upon or invasion of the States, not the deterrence of foreign intrusion into the islands. Because of a reduced role of the U.S. military in determining internal conditions in Guam politically, while fundamentally maintaining its economic impact on the island's

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<sup>69</sup> See, for instance, the 1945 memorandum to the Secretary of the Navy from then-Commander of the Navy in the Marianas, Mr. G.D. Murray, in which he stated:

"Military control of these islands is essential as their military value outweighs their economic value. The economic development and administration of relatively few native inhabitants should be subordinate to the real purpose for which these islands are held....the commercial and/or industrial value and resources of the islands is of little or no relative importance to the welfare of the United States."

economy, the local influence of U.S. military leadership will fluctuate counter to the performance of Guam's other economic sectors.

Guam's status negotiations toward free association are likely to result in the U.S. taking responsibility for the defense of Guam's borders. However, under this new status, the ongoing U.S. military expenditures in Guam will be moderately lower than what is experienced under both the current station manning levels and the existing level of capital improvement project funding. This change in the industrial aspect of the U.S. military in Guam, though, should be more than offset by the substantial long-term economic development aid accorded to Guam in exchange for the right of the U.S. to limit foreign access to Guam in the event of a military emergency. It should be noted that this aspect of the Guam-U.S. military arrangement is separate from land issues, and should be negotiated under a different (part of an) agreement.

As a freely associated nation, bilateral and multilateral pacts for the defense of Guam are possible. Although the U.S. would have primary authority and responsibility for the island's defense, Guam may be free to negotiate defense agreements with other, regional governments, as well. This could be quite beneficial to Guam, since it could potentially bring in many times the financial aid and economic development assistance that is available under the U.S. system alone.

## Transportation

Guam would gain control over air and sea transportation into and out of the island as a part of its new status of free association. This includes airline landing rights and maritime access rights. Nonetheless, it is anticipated that airport and seaport financial assistance from the United States could be negotiated, ensuring continued operations and improvements during an intermediate period of time.

Airline landing rights are typically negotiated in bilateral agreements, wherein one nation's airlines are granted landing rights on specified routes and schedules within the other nation, and *vice versa*. Because Guam does not have a domestic airline, it is likely that landing rights in Guam would be exchanged for some other concession, which may include a monetary payment to Guam that might be used for airport operations and maintenance, and for other purposes. In addition, it is anticipated that Guam may be able to retain the services of the U.S. Federal Aviation Administration for air traffic control for a modest fee, since the U.S. would continue to desire the maintenance of safe aviation in and around Guam because of its military interests.

Guam would be likely to remain an open port for civilian vessels under free association. However, the passage of non-U.S. military vessels through Guam's territorial waters<sup>70</sup> would continue to be strictly controlled. Perhaps the greatest advantage of free association in terms of transportation will be that Guam is no longer subject to the so-called "Jones Act,"<sup>71</sup> a part of the Coastwise Laws in U.S. maritime law. The costs of goods shipped to Guam from the States is artificially inflated by the requirement that cargo, baggage and passengers shipped between two successive U.S. ports must be carried aboard U.S.-flag vessels.<sup>72</sup> Such vessels, if large enough to engage in ocean transport, must also be U.S.-hulled, meaning that they must be built in U.S.

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<sup>70</sup> The twelve-mile limit of Guam's territorial sea.

<sup>71</sup> The Merchant Marine Act of 1920.

<sup>72</sup> Vessels carrying United States registry.

shipyards, typically by U.S. labor, and also manned by U.S. labor. As a result, the vessels are among the most costly built and operated anywhere in the world.

In addition to these costs, the veritable monopoly granted to U.S. shipping lines in the Guam trade allows the imposition of monopoly prices on goods shipped to Guam from the U.S., raising the landed cost of goods on the island. These costs are passed through to businesses and consumers, artificially increasing the cost of living in Guam to the benefit of the U.S. shipping lines, shipyards and, ultimately, shipbuilding unions. The best estimate of the impact of the Jones Act on the cost of goods from the United States sold in Guam in 1994 was \$32.5 million, or 1.1% of Guam's gross island product.<sup>73</sup>

Overall, it is expected that air and sea traffic into and out of Guam would remain approximately the same under free association as in the *status quo*, with lower surface shipping costs, improved funding for air and sea ports, and substantially reduced shipping costs for Goods arriving from the United States. The combination of benefits to Guam's economy could range from \$75 million annually to a significantly higher amount.

## **Trade**

The terms of trade into and out of a freely associated Guam are expected to be quite similar to existing conditions under the *status quo*. Ultimately, Guam's Customs agency would regulate the importation of goods into the island; Guam's export trade, primarily in services, would remain largely unregulated.

In terms of trade preferences accorded to the manufactures of Guam, it is possible that Headnote 3(a) or substantially similar provisions would govern Guam's trade with the United States. A continuation of favorable treatment under the Generalized System of Preferences (or its successor) is likely, as is the possibility that Guam would be granted "most favored nation" status where the GSP does not apply. However, it is unlikely that any of these preferences will have a significant impact on Guam's economy, since manufacturing in Guam will be a relatively unimportant element of the island's future economic development. Nonetheless, it is possible that Guam will impose quotas and/or tariffs on some select imported items in order to foster the development of some strategic small scale manufacturing for consumption in the local market; trade restrictions imposed by Guam are otherwise unlikely.

Under free association, Guam will maintain its bias for free trade and unrestricted capital movements into the island. This will be beneficial because it helps to minimize consumer costs and provides a greater volume of trade. However, Guam will perpetually carry a merchandise trade deficit, and the majority of exports from Guam will be considered "pass-through" trade.

## **Attractiveness of Investment**

By definition, a change in political status will bring a period of instability to Guam's investment climate. One of the primary tasks that the island faces in a transition to free association will be to build an image of consistency and permanence in its business environment. However, if properly managed, Guam will be able to overcome prospective investors' uncertainty and the related risk avoidance by adopting internationally accepted institutional

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<sup>73</sup> Barakat & Chamberlin, "Freight Rates vs. Costs in the Guam Liner Trade," 1994.

models and adhering to the rule of law. A continuing close affiliation with the United States will help in this process.

Once Guam has reinforced its reputation of providing a stable business platform, the relatively unrestricted opportunities that the island offers, in conjunction with the added flexibility it has in providing investment incentives, should help to attract substantial new investment. The potential to provide innovative, significant corporate and individual tax incentives will be particularly effective in attracting new capital into the community. In addition to the familiar growth in tourism and commercial enterprises, though, Guam can expect the formation of new industries centered around transportation and telecommunications to accelerate, as well as those based upon the island's physical location, although restrictions on technology transfers may complicate this initiative.

The conversion of political status will partially isolate Guam from U.S. financial markets, since there may be no tax advantage for Guam's public debt under U.S. law. While there is the possibility that Guam's public debt would be accorded the same tax exempt status under the U.S. Internal Revenue Code as is granted to the Federated States of Micronesia, this benefit is negotiable and is by no means certain.

## **Labor**

While Guam would have complete sovereign control over its internal labor laws under free association, it is likely that a system similar to that currently in place in Guam and the United States would prevail. There may be differences in the minimum wage and overtime compensation rules to reflect regional competitive realities, but the general system of workers' rights and employer privileges is expected to continue. Occupational safety and health requirements may be somewhat more lenient, but would still be uniformly enforced, and prohibitions against child labor may be somewhat strengthened. Equal employment opportunity regulations may be slightly less stringent than under U.S. federal law.

Labor programs would also include statistical programs similar to those in place under the *status quo*, but the collection of data regarding payroll employment, unemployment and occupational characteristics would be contingent upon the availability and prioritization of public funds.

The use of non-immigrant foreign labor may become more prevalent in some industries, but controls governing non-competition with resident labor resources would be maintained and perhaps strengthened.

## **Other Private Sector Considerations**

As a legacy of U.S. administrative policies in Guam, the island has focused its attentions on government activities and public employment for many decades. As an independent nation in free association with the United States, though, the luxury of relative inattention to private economic activity will no longer be possible. As a result, Guam will place greater emphasis on the growth and development of private firms and industries, redirecting community resources away from public sector agencies and enterprises to achieve the island's economic goals and enhance the delivery of goods and services for private consumption. As a part of this shift from the *status quo*, there will be an acceleration of privatization of services that have traditionally been provided by the government, converting inefficient public enterprises that draw upon public

funds into more responsive private businesses that generate tax revenues. Public/private partnerships in the provision of some services will also become more common, helping to reduce resource usage while improving delivery and quality. Economic efficiencies will be introduced into the pricing mechanism.

Because of its close relationship with Guam, the U.S. federal government will support these efforts, providing substantial support through the transition and beyond in several service areas. For instance, can expect the same level of public services from the Federal Deposit Insurance Corporation (FDIC) for banks and savings and loan associations that are already insured under the *status quo*. With some minor modifications, the services of the U.S. Postal Service will still be in place. The Small Business administration will continue to offer several of its more popular programs in Guam throughout the study period and for many years thereafter, and will continue to complement the work of the (U.S.) Federal Emergency Management Agency in providing disaster assistance. The Economic Development Agency of the U.S. Department of Commerce can be expected to continue its programs in Guam for several years after the transition to free association, as will the U.S. Legal Services Corporation and the Farmers Home Administration.

Because of a continuing presence in Guam of the U.S. military, the programs and services of the National Weather Service and the Public Health Service (supplemented by the work of the international World Health Organization) will continue in Guam, as will the efforts of the U.S. federal government in law enforcement and drug interdiction.

Most other U.S. laws and regulations, particularly those administered in support of economic development, whether or not applicable under the *status quo*, will be subject to negotiations. Some public services provided by the U.S. federal government under the *status quo* may continue to be provided at an expense reimbursable by Guam.

## **Health**

As a condition of the transition to free association, Guam is likely to negotiate the continuation of most major health programs currently operating under the *status quo*. Guam is also likely to continue, and possibly elevate in status, as the health care center for the islands of Micronesia.

Because of its status as an independent nation, Guam will seek and probably achieve full participation in all international health organizations operating in the region, and take greater advantage of the relevant existing international health assistance programs.

Regulatory agency controls, such as those of the Food and Drug Administration, the U.S. Department of Agriculture and the Health Care Financing Administration, will likely continue through a transition period, and gradually be replaced with a set of internally established policies. Close ties to these U.S. health agencies will likely become permanently established, and will allow access to the latest products, procedures & equipment.

Under Free Association, strong affiliations are likely to be established with several Asian medical organizations, allowing for the adoption of alternative treatment modalities not presently sanctioned by the U.S.

The overall cost of health care could decrease significantly without any reduction in quality, as Guam would have the ability to obtain its equipment, supplies and medications from

non-U.S. sources. U.S. pharmaceutical firms and medical equipment manufacturers have licensed many processes to Asian firms, whose lower labor costs would allow identical medications and equipment to be available to Guam residents at half the cost they pay today.

While it is likely that Guam will continue to mirror its present licensing policies for health care professionals, it will also have the opportunity to permit the entry of additional, well-trained health professionals from foreign countries. This will relieve some of the severe manpower shortages the island periodically experiences in a variety of medical specialties.

## **Education**

Within the study period, it is anticipated that there will be a continuation of existing educational standards in Guam, but that a process will be underway to redirect the focus the resources of the educational system toward the needs of long-term residents and their children. This will be made possible by a net reduction in the number of new immigrants and habitual residents entering Guam. Further, Guam's local school system will be empowered to develop and implement curricula that are more relevant, both locally and regionally, than are dominant under the current system. Guam's history, culture and language will play a more prominent role in future educational prerogatives. However, U.S. accreditation standards will continue to apply in Guam, and international standards may also be adopted.

Although expected to be at a lower level than under the *status quo*, there will be a negotiated continuation of U.S. federal education grants provided to Guam. In addition, some level of U.S. federal student financial aid programs will be made available to college students from Guam attending school in Guam and in the United States; these programs will probably provide greater assistance to students attending school in the U.S. It may also be possible to negotiate a continuation of the land grant status of the University of Guam under free association.

During the study period, the Department of Defense Education Agency (DODEA) will continue to provide classroom education for the majority of school-age military dependents domiciled in Guam. As the quality of Guam's public education system improves, this situation may change, but the process could take a long time because of recent investments in educational infrastructure by the Department of Defense.

## **Fiscal and Monetary Policy**

In free association with the United States, it is likely that Guam will retain the U.S. Dollar as its unit of currency.<sup>74</sup> By doing so, Guam would effectively surrender all control over its monetary policy, as most policy parameters would be set by the U.S. monetary authorities, with no consideration of their impact in Guam. However, in exchange, Guam would continue using a universally recognized medium of exchange that is generally quite stable. This will assist in maintaining stable trade relationships and the confidence of the tourism industry.

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<sup>74</sup> While this is likely because of Guam's continuing political ties to the United States, it is by no means certain. Its location places Guam clearly within the Asian economic sphere, and a time may arise when Guam wishes to adopt the Yen (for instance) as its legal currency. In the alternative, Guam could establish a mixed system, such as currently exists in Europe and other places, or even opt to issue its own currency. This latter is unlikely, though, for several practical reasons.

Under free association, virtually all fiscal expenditures in Guam would be under the control of the government of Guam, with the exception of U.S. defense expenditures and most U.S. federal grants. All taxes in Guam, though, would be under local control and authority. There is no anticipation of any change in the structure or level of excise taxes after the transition to free association, but may opt to change its income tax code. In addition, either the property tax or the gross receipts tax may be raised to make up for the loss of so-called “Section 30” funds coincident with the repeal of the Organic Act.<sup>75</sup> For illustration purposes only, raising the gross receipts tax rate to approximately 5.0% (from the current 4%) would make up for nearly all of the loss in §30 revenues. However, it is possible that Guam’s local income tax may be modified from the current “mirror” of the U.S. Internal Revenue Code. This could make the provisions of the code more relevant to an economic structure such as Guam’s and raise additional revenues to make up for the elimination of §30 funds. The prospect of taxing the income of U.S. federal employees residing or domiciled in Guam is possible, but not certain.

### *Taxation*

As a sovereign nation, a freely associated Guam will have complete authority over its system of taxation, the items and activities that are taxed, the level and structure of tax rates and levies, and the impact that its system of taxation has on the structure and performance of its economy. Nevertheless, it is unlikely that Guam will significantly change the structure of its taxes immediately upon its transition to a new political status. This is so for the simple reason that such changes can be unpredictably disruptive, and there will already be some level of instability inherent in the transition. Therefore, it is anticipated that the changes in Guam’s tax code that take effect within the study period will be directed almost entirely toward providing a few automatic incentives for investment (both from the outside and from within) and economic development activities. While these incentives may be in the form of rebates, as is the case with the principal incentive program under the *status quo*, it is more likely that they will be in the form of reduced tax rates or abatements. The incentives will apply to those types of action predetermined to be desirable or crucial in support of economic expansion or diversification, and may be changed from time to time.

Because of Guam’s new sovereign status and the inapplicability of the U.S. Internal Revenue Code to Guam, the island’s taxpayers would no longer be paying taxes into the U.S. Treasury under the Federal Insurance Contributions Act (FICA, or “Social Security” taxes) or Medicare. These programs would revert to the control of the government of Guam, and become local programs. The accounts of those in Guam who have already paid sums into these two programs would be returned to Guam under a negotiated agreement, with the disbursement possibly taking place over a period of years. In order to obtain greater financial leverage, it is likely that Guam’s private and public pension funds would be merged into a single Retirement Fund. However, it is also likely that more strict controls would be placed on the designated uses of this Fund, so that its assets could not be diverted to cover current government expenditures.

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<sup>75</sup> Between 1993 and 1997, the funds that Guam received under §30 of the Organic Act amounted to an average of 12.5% of all income taxes, or 7.7% of all tax revenues received by the government of Guam. Data developed from *1994 – 1997 Annual Report*, Department of Revenue & Taxation, Government of Guam, Table on pg. 7.

## *Transfer Payments*

Just as in the Freely Associated States (Palau, FSM & Marshalls), U.S. federal government grants and other transfers to the government of Guam are expected to increase for a period of time after the transition to free association. However, because of Guam's relatively well-developed infrastructure, these transfers will be proportionally smaller than those paid to the former Trust Territories. In any case, the level of transfers will decline over time, but will extend well beyond the study period.

Transfers to individuals under the various social welfare programs will be subject to negotiation, but are expected to continue through the study period on the basis of a declining U.S. federal government matching funds schedule. The government of Guam will be expected to absorb an increasing proportion of the costs of these programs as time progresses. As a result, both participation in and the benefits paid by these entitlement programs is expected to decline throughout the study period and beyond, and the benefits to those who are not citizens of Guam will be reduced significantly, while benefits to local citizens remain relatively stable.

## *Retirement Programs*

As discussed, the accounts of Guam citizens held within the U.S. federal Social Security System will be transferred to the government of Guam gradually after the transition to free association. It is probable (but not certain) that these funds will be merged into the existing government of Guam Retirement Fund for purposes of efficiency in investment, but additional safeguards on those funds will prohibit them from financing current expenditures of the government. There is, though, the possibility that the funds could be used to finance long-term government projects under the equivalent of a bond issue. In any case, retirement benefits under both the public retirement fund and Guam's replacement for the U.S. Social Security System should remain approximately the same as under the *status quo*.

Tax-deferred retirement savings and investment plans (Individual Retirement Accounts, 401(k), etc.) will remain available to Guam's citizens, but with some modification. It will be essential to encourage saving and the corresponding investment in Guam's economy, so the rules for the types of saving and investment to be eligible for favorable tax treatment will be changed. Therefore, the eligible investment instruments for these plans will require that all or a substantial portion of the funds be invested for economic development purposes in Guam, rather than in U.S. stocks, bonds and other securities.

## **Distribution of Income**

No recent or comprehensive studies of the distribution of income in Guam have been uncovered in the research in preparing this report.<sup>76</sup> Therefore, it is not possible to form a *status quo* baseline for comparison of the overall distribution of income under the status options. However, other factors in the study indicate that there will be shifts in the distribution of income

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<sup>76</sup> The Guam Department of Labor does produce its annual *Per Capita and Household Income on Guam* reports based upon sample surveys, but the level of aggregation in the reports does not allow strong conclusions to be drawn about the distribution. An attempt was made in 1990 and 1991 to analyze data from Guam's personal income tax records, but the results are dated and reflect an unusual period in Guam's economic history, so may not be particularly useful in this report.

in response to a status change, moving in favor of Guam citizens and, most particularly, those who save and reinvest their income in economic development projects in Guam.

## **Independence**

Although the political status of independence is fairly well defined, the economic arrangements and relationships thereunder are not. The only other former U.S. jurisdiction ever gaining independence from the United States is the Republic of the Philippines, and that transition was completed more than 50 years ago; changing economic, political and technological conditions since then make comparisons difficult and unreliable. More recently, Puerto Rico has been contemplating becoming independent from the U.S., but this political status has not yet even been selected by the populace there, let alone implemented. Nevertheless, there are several useful lessons to be learned from the work that has been done toward independence in Puerto Rico, and a number of parallels can be drawn.

Many of the prospects for Guam under independence are similar to those under free association. After all, the principal difference between the two relates primarily to military defense and shared sovereignty in foreign affairs. However, because of the cooperative relationship with the U.S. under free association, there are several economic opportunities in Guam that would be foreclosed. While these constraints would not exist for Guam under independence, neither would the same level of economic development assistance. These two aspects of the difference between independence and free association form the basis for the differences in their comparison to the *status quo*.

## **Immigration**

As an independent nation, Guam would have complete and exclusive control over immigration. The island would no longer be a point of entry to the United States for immigration or naturalization purposes, nor for any other purpose. During the study period, immigration into Guam for residency may be tied to commercial investment and/or other anticipated benefits to Guam.

Although there may be some preference granted to citizens of the United States and the Freely Associated States for entry into Guam, such entry would not be as “habitual residents.” Such entry for extended periods may also be subject to a means test, as it may be for entry from other points, as well. Few social or economic benefits will be available to short-term visitors and non-immigrants. However, unrestricted emigration to the United States for U.S. citizens will continue.

Immigration standards for the entry of tourists will probably be relaxed in order to provide all possible support for that industry. Non-visa entry from most nations is likely, provided that the visitor can show a non-refundable return ticket and a valid passport. Short-term entry will be allowed for business purposes under similar requirements.

Because of Guam’s need for flexibility in meeting its labor requirements and the desirability of controlling unemployment during times of economic downturn, a very liberal

program for E-, L- and H-category visas<sup>77</sup> will be established. In line with this, a comprehensive job registry for Guam citizens will be established to ensure that there is no displacement of resident workers by non-residents. In addition, a two-tiered wage scale, residents at a higher rate than non-residents, is likely to be established in order to reduce overall labor costs.

Because of concerns and uncertainty among expatriate U.S. citizens and naturalization concerns among resident aliens at the time of the transition to independence, there is a moderate to high risk to Guam of labor emigration to the U.S. during the study period. This may have a significant adverse effect on the number of workers and the range of skills available to employers in Guam. For Guam citizens, though, there may be moderately restricted access to U.S. labor markets.

## **Individual Rights**

The personal rights of individuals residing in an independent Guam will be protected by the island's constitution. In comparison to some other nations, these rights will be reinforced in Guam by the explicit acceptance of international standards of individual human rights and the island's history of association with the United States.

As in many other small, formerly colonized nations, it is likely that deferential rights and benefits will be defined or affirmed for individuals of indigenous descent, either in law or in Guam's constitution.

### *Nationality*

Under independence, the nationality of those residing in Guam permanently will be Guamanian. The culture in Guam will be relatively more Chamorro, but there will also be relatively more linkages with Asian nations because of the close association between the economy of Guam and those of Asia.

### *Citizenship*

Citizenship is one of the more complicated issues under independence. Upon initial assessment, it would appear clear that an affirmative election to become independent from the United States would be the same as rejection of citizenship in that nation in favor of citizenship in Guam. However, there are several different ways, legal theories that have been applied in practice, in which U.S. citizens residing in Guam could retain their citizenship after a transition to independence.

*The Maastricht Treaty* – Under the 1992 Treaty that formed the European Union, “Every person holding the nationality of a Member State shall be a citizen of the Union.”<sup>78</sup> This fundamental document of the European Union essentially brings the eleven original signatory

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<sup>77</sup> E-visas are for “treaty traders” having a substantial investment in Guam's economy. H-visas are for temporary, non-immigrant employees of Guam firms. L-visas are for intra-company transfers of foreign firms conducting operations in Guam.

<sup>78</sup> *The Maastricht Treaty*, Part 2, Article 8, Paragraph 1.

nations<sup>79</sup> together in a union patterned after the United States. Each national of the original signatory nations retains their national citizenship, but also becomes a citizen of the Union. While the Union is primarily based upon the perceived need for economic cooperation and transparency among the European nations, the Treaty intends (among other things) to establish economic mobility for individuals within Europe, just as exists among the several States of the United States. Citizenship in the Union extends rights to the point that a national of one country may vote and even stand as a candidate for office in municipal elections in any other member country where they happen to reside.

*The U.S.-Israel Model* – Persons of the Jewish faith are allowed to enter Israel under “Oleh” visas, which support the return of the “tribes of Israel” to their traditional homeland. Someone entering Israel under an Oleh visa will automatically become an Israeli citizen after a period of three months, unless they take affirmative steps to refuse such citizenship. The U.S. State Department does not regard automatic acquisition of Israeli citizenship (Par. 2 of the Nationality Law of Israel) as an expatriatory act, so the issue of intent does not even arise. However, if someone acquires Israeli citizenship by naturalization upon his application (Par. 5 of the Nationality Law), that can be regarded as a potential expatriating act. But, if the State Department cannot prove that the person intended thereby to give up his U.S. citizenship, that citizenship is not lost. As a result, it is possible for an individual to hold dual citizenship in two countries that is legally recognized in both. There are numerous other countries in which similar dual citizenship is possible.<sup>80</sup>

*The proposed Puerto Rico Model* – During the 101<sup>st</sup> Congress (1<sup>st</sup> Session, 1989), the “*Puerto Rico Status Referendum Act*”<sup>81</sup> was introduced in the Senate by Senator Bennett Johnston. Title III, Section 311, of the Bill addressed the matter of U.S. citizenship should Puerto Ricans elect independence in the proposed referendum. Under the provisions of this Section, U.S. citizens residing in Puerto Rico would retain their U.S. citizenship after the transition to independence. However, for those who obtained U.S. citizenship by having been born in Puerto Rico before the transition to independence, their children born outside of the United States after the transition would not automatically be U.S. citizens.

Thus, under the provisions of this legislation, U.S. citizens would retain their status, but would not pass that status on to their children if Puerto Rico became independent. However, children of Puerto Ricans born in the United States after the transition would be U.S. citizens, and children of U.S. citizens born in the United States would be U.S. citizens regardless of where

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<sup>79</sup> France, Germany, Italy, Spain, Portugal, Finland, Ireland, Belgium, the Netherlands, Luxembourg, and Austria.

<sup>80</sup> According to research compiled by the City University of New York as of June 1999, dual citizenship is allowed by the following countries after their citizens have acquired U.S. citizenship through naturalization:

Albania, Antigua, Barbados, Barbuda, Belize, Benin, Bulgaria, Burkina FASO, Cambodia, Canada, Cape Verde, Central African Republic, Colombia, Costa Rica, Cote D'Ivoire, Croatia, Cyprus, Dominica, Dominican Republic, Ecuador, El Salvador, France, Ghana, Greece, Grenada, Guatemala, Hong Kong, Hungary, Iran, Ireland, **Israel**, Jamaica, Latvia, Lesotho, Liechtenstein, Macao, Maldives, Mexico, Morocco, Namibia, Nevis, New Zealand, Nigeria, Panama, Peru, Poland, Portugal, Romania, St. Christopher, St. Kitts, St. Lucia, Slovenia, Sri Lanka, Switzerland, Syria, Togo, Tunisia, Turkey, Tuvalu and the United Kingdom. There may be others not included in the study.

<sup>81</sup> 101<sup>st</sup> Congress, S. 712. See <http://thomas.loc.gov/cgi-bin/query/D?c101:3:./temp/~c1011wuys9::> for the full text of the Bill as reported to the Senate.

they were born. As a further provision of Section 311 of the Bill, Puerto Ricans were to be granted an immigration status similar to the “habitual resident” status accorded to citizens of the Republic of Palau, the Federated States of Micronesia and the Republic of the Marshall Islands under their respective Compacts of Free Association.

Bill S. 712 in the 101<sup>st</sup> U.S. Congress was never fully reported out of Committee,<sup>82</sup> and so was never brought to a vote before the full Senate. Companion legislation in the House of Representatives (H.R. 4765) was passed, but proposed a different approach to the Puerto Rican political status vote and was silent on the subject of citizenship. The sponsors of the two Bills in the House and in the Senate were unable to agree on compromise legislation, and the 101<sup>st</sup> U.S. Congress expired without the matter being resolved.

Regardless of the model chosen (except the Maastricht model), if dual citizenship is provided for in the negotiations between Guam and the U.S. toward independence, that citizenship will almost certainly be limited to those who are already U.S. citizens at the time of the political status transition. It is unlikely that the principle of *jus sanguinis* will apply, and all those born to U.S. citizens residing in Guam after the transition will be citizens of Guam, but not citizens of the United States unless their parents were also born in the States. There is also the possibility that any U.S. citizen taking affirmative steps to become a citizen of Guam will surrender their U.S. citizenship in the process, but this is subject to negotiation. In any event, anyone who is not a U.S. citizen but resides in Guam at the time of the transition will not attain U.S. citizenship while continuing to reside in Guam.

U.S. citizenship is clearly one of the major issues in Guam in the selection among the eligible voters of their desired political status. Just as clearly, though, it is more a political and social issue than it is an economic issue. Nonetheless, because it is an ambiguous issue, citizenship will be one of the key levers used by the United States to gain a better negotiating position should Guam opt to become independent. It is incumbent upon the people of Guam to carefully evaluate the value of citizenship in a rational and dispassionate manner so as to avoid surrendering economic advantages in exchange for the vestiges of emotional ties to the United States through continuing citizenship.

Looking at the citizenship issue from a different perspective, it is possible that an independent Guam will offer citizenship in exchange for substantial commercial investment or other significant activities of economic benefit to the island and its people. This practice, which takes place in many other countries (including the United States) is likely, particularly during the early stages of independence.

### *Culture*

It is anticipated that there will be a resurgence in the Chamorro language and culture in the independent nation of Guam. There is even the remote possibility that the use of the Chamorro language will be mandated for some of the island’s governmental activities. Nevertheless, it is almost certain that U.S. English will remain the language of instruction in the nation’s school system and will generally be used in business transactions.

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<sup>82</sup> Bill S. 712 was reported out of the Senate Energy and Natural Resources Committee and the Senate Finance Committee, but was never reported out by the Senate Agriculture, Nutrition, and Forestry Committee.

Expression and exhibitions of the Chamorro culture will help to enhance the experience of tourists visiting Guam, strengthening that dimension of the visitor industry in a positive way that supports increased economic activity.

In accordance with tradition, there will be continued open acceptance of other cultures. This will be particularly true for those who are members of cultural groups that contribute significantly to the economy of Guam.

### *Travel*

There will be few restrictions imposed upon travel by the citizens of an independent Guam. Those citizens will continue to have access to the United States, but such access will be controlled by visas; non-visa entry to the U.S. by U.S. citizens will continue.

Travel to other places will also be controlled by visas, and entry may be delayed during the initial period of independence, until foreign immigration officials become familiar with Guam's status and passports. However, international travel by Guam citizens with appropriate visas will be completely unrestricted by U.S. requirements and international relationships, since Guam will no longer be required to adhere to U.S. foreign travel regulations.

The enhanced right to travel for citizens of an independent Guam may have a modest positive impact on trade and the availability of some products in Guam, but this is expected to be insignificant to the overall economic conditions of the island.

### *Affirmations*

With the complete sovereignty accorded by Guam's independent status, the internal and external unilateral decisions made by Guam are primarily directed by the desires of the resident population and its leadership. There will be relatively less concern regarding the political and economic agenda of the United States, except in the areas of financial dependency and mutually beneficial cooperation, which will almost exclusively be dictated by the defense interests of the United States and (to a lesser extent) Guam.

Sovereign decisions will also be influenced by the historical ties of friendship between Guam and the U.S., reinforced by cordial diplomatic relations, although many of the economic ties will be based upon Guam's acquired preferences for U.S. goods. There will also be more harmonious relations between Guam and the U.S., as affirmations will be based upon mutual respect and mutually agreed sovereign ties.

### *Protection of Rights*

Guam has been a U.S. territory for over a century, and there are innumerable economic, social and political relationships within Guam and with outside entities that have been established based upon the U.S. system of laws. It is unlikely that this system, as applied in Guam, will change suddenly or radically because of a transition to independence. Therefore, it is anticipated that Guam's constitution and laws will at least initially be patterned after those of the U.S. It is also expected that they will be consistent with the International Declaration of Human Rights. As a result, individual and collective rights are expected to be well defined and strongly protected. Further, it is unlikely that Guam would abridge the rights of any guest resident or

visitor to the island; on the contrary, a general and ongoing feeling of welcome will be conveyed, in keeping with long-standing traditions of hospitality on the island.

Although rights are expected to be strongly protected, it is also possible and even likely that Guam's constitution will incorporate some provisions granting preferences to people of Chamorro descent. For instance, the indigenous population may be accorded some preferences in hiring for government jobs. It is also likely that there will be preferences granted to Chamorros for access to and acquisition of government land, including Chamorro Land Trust land and land released by the U.S. federal government in Guam. Economic development programs and initiatives sponsored by Guam's government may also grant preferences for the participation of Chamorros.

## **Legal and Judicial Framework**

As an independent nation, Guam will have full authority to establish whatever legal and judicial system it chooses. However, two factors will guide the island toward a system that is similar to the *status quo*. First, Guam has some 100 years' experience with the U.S. legal system, and has become comfortable working within the general framework which it provides. Second, as a negotiated status, it is likely that a system similar to that of the United States will be required, at least for a period of time.

The maintenance of some degree of continuity in the legal and judicial framework of Guam will, in fact, carry many economic benefits with it. Existing economic relationships will be preserved and protected, and the familiar rules of commerce will remain the standard under which business is conducted.

Even if the legal structure of Guam is maintained, though, legal and economic stability will at least temporarily be affected because of latent uncertainty and the residual effects of new laws that are required during the transition to independence. In contrast, if legal stability and economic rights are removed or significantly altered during the transition, Guam's economy could be subject to substantial adverse effects.

## **Foreign Affairs**

Just as would any other nation, an independent Guam would be responsible for its own foreign affairs, providing its own representation internationally. This sovereign characteristic would extend to relations with the United States, regardless of other negotiated provisions in the island's political status change. Guam and the United States will exchange diplomatic representatives at the State Department level, enabling consistent discussion and relatively easy resolution of matters of mutual concern, including economic cooperation. Beyond these issues, the political relationships and international agenda of the United States will no longer hold as much relevance to Guam, except where they are overlaid with mutual issues of security.

In the international arena, Guam will be directly involved in foreign relationships on a state-to-state basis, with primary emphasis initially on the U.S. and on the other nations of the Asian-Pacific region. Many of these relationships will be carried out under the auspices of the United Nations, of which Guam will be a member. These relationships will allow the formation of new economic and political alliances, forged within the framework and limitations of existing and new economic ties, as well as mutual defense pacts.

Guam's new status as a sovereign nation, combined with its evolving relationships with other nations within the Asian-Pacific economic sphere, will lead to opportunities to attract new investment and generate additional sources of economic growth. These opportunities will be tied to Guam's ability to discover and expose credible areas of mutual benefit through direct discussions and negotiations with other Asia-Pacific governments and commercial interests.

## Land

According to international standards applied under the auspices of the United Nations to non-self-governing places, alienation of land and other resources to settlers and immigrants is proscribed. This standard acknowledges the heritage of the indigenous peoples of a place and their rights to the properties that they occupied prior to colonization. Unfortunately, this standard has not been conscientiously applied by the United States in Guam, so there is a legacy of land alienation on the island, both to settlers from the U.S. and to immigrants born in foreign lands. As a practical matter, this is a difficult legacy to undo, and it is expected that non-indigenous rights to private property in Guam will be continued under independence. However, there may be some restrictions on the ownership of land by foreign citizens, just as there are in existing Guam law under the *status quo*.<sup>83</sup>

Within the limitations cited above, it is likely that Chamorro property rights under independence will be given precedence over those of others, although this preference may be expanded to all citizens of Guam. For instance, the constitution and laws of Guam will sanction the Chamorro Land Trust, and there will be no remaining question regarding its validity or efficacy. Further, in any sale or other distribution of public lands and released U.S. federal landholdings in Guam, priority will be given to indigenous citizens and ownership by others may be prohibited in the first instance of private title.

The matter of retained U.S. federal landholdings in Guam becomes a more difficult issue because of the assumed continued role played by the U.S. in the military defense of Guam. There will be an ongoing need by the U.S. for military bases in Guam, yet it is clear that the amount of land that will be retained for that purpose will be far less than under the *status quo*; a substantial portion of the landholdings will be released to Guam's control. However, in compensation for the retained lands, the U.S. will be expected to pay some form of lease. This lease payment may be in the form of monetary fair market value, long-term economic development aid, defense services, or some combination of the three. This arrangement will ensure that the U.S. military optimizes its use of land in Guam, presumably at a much lower level, and will also provide for the release of significant lands for private and public development.

The structure of laws governing foreign investment in land in an independent Guam are expected to be the same as or substantially similar to that under the *status quo*. However, the success with which Guam attracts this investment will be significantly influenced by confidence in judicial system. This is one of the major areas in which a stable legal and judicial framework for Guam will be essential in building economic prosperity.

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<sup>83</sup> See Title 21 GCA, Chapter 1, Article 2, §1204, as amended by P.L. 12-192.

## *Natural Resources*

Within practical environmental constraints, it is expected that the laws governing the exploitation and use of natural resources in Guam (including land) will be redefined under independence. The resulting resource use practices will more appropriately reflect local conditions, including Guam's limited acreage, and support long-term economic development prerogatives. Nonetheless, the new standards will be compatible with international conventions.

As an independent nation, Guam will more actively participate in a wider variety of Pacific regional environmental and resource management programs. This perspective will help to ensure that errors in natural resource management in the short-term are not compounded into long-term problems for the island and its economy.

As a synergistic benefit from independence, the strain on Guam's renewable resources will be mitigated, and this will partly be a result of reduced immigration into the island.

## *Ocean Resources*

Although there may be little or no immediate benefit to the economy, one of the more valuable impacts on Guam's economy from the transition to independence will be its control over the island's Exclusive Economic Zone. Formalization of the right to control and manage the environment and resources within 200 miles of Guam's shores (abutting the corresponding zones of the Commonwealth of the Northern Mariana Islands and the Federated States of Micronesia) will add significant resources to Guam's economy. The economic impact will occur some time in the indefinite future, though, as extractive technologies advance and the relevant commodity prices escalate.

Along with control of its EEZ come the costs of enforcement, but these costs are expected to be insignificant in the short-term, since there is little opportunity to exploit those resources and therefore little reason to enforce all but the environmental aspects of resource management.

## **External Economic Development and Financial Assistance**

Under its new status, Guam will continue to recognize that economic self-sufficiency is fundamental in support of political independence. The island will therefore immediately focus on private sector development and growth. A new level of access to and assistance from international and regional organizations will stimulate improvements in Guam's economic development, and coupled with U.S. and international financial and technical aid, will lead first to maintenance and then to accelerated growth in the economy.

As a part of the negotiated provisions for Guam's transition to independence, it is anticipated that the island will receive substantial economic development funding over a period of 15 or more years, partly in exchange for U.S. military access rights in Guam. This funding also includes amounts negotiated to remedy infrastructure and environmental issues that were left unresolved prior to the status change. The U.S. State Department will administer this composite funding program.

Although U.S. entitlement programs are terminated upon Guam's transition to independence, similar local programs will replace them. However, these programs will be operated at a lower total cost because of reduced immigration into Guam over time, but the net cost to Guam will be higher during the study period than under the *status quo*.

Bilateral and multilateral international assistance to Guam will be significantly higher than under the *status quo* because of Guam's new sovereignty, but the relatively advanced state of Guam's economy will place limits on which programs and what level of assistance is available. Nevertheless, Guam will look regionally for the majority of its development funding, loans, aid and technical assistance; loans and technical assistance will be more readily available than grants and other direct aid.

During the study period, it is expected that external investment into Guam will be somewhat constrained because of the higher perceived levels of economic and political uncertainty associated with the status transition. This perception of risk will gradually dissipate, though, as Guam exhibits continued stability in its legal and judicial system. Further, under independence Guam will provide powerful investment incentives through its corporate and individual tax policies, and will augment those incentives through the cooperative planning and implementation of infrastructure projects that support new investment projects.

## **Tourism**

Although there is little to change the visitor industry profile of Guam because of the transition to independence, it is possible that arrivals, expenditures, tax revenues and the level of activity will decline during the study period pending a reinforcement of confidence in Guam's political and judicial stability. Unless this stability is clearly evident, the decline in tourism activity could be more serious.

On the affirmative side, an independent Guam would have complete control over its immigration policies. With the authority to determine admissibility, it is likely that individuals arriving from preferred tourism markets would be granted entry under extremely preferential conditions. Although this may generate some modest enforcement problems, it would also provide a significant boost to the expansion of Guam's visitor base. Being able to avoid the effort and delays spent in obtaining a visa to other destinations would make Guam relatively more attractive to casual travelers, and they would be even more inclined to select Guam over other places for their travel plans.

If Guam is able to expressly exhibit continued ties to the U.S. and, more especially, to the American system of government, this effect should become even stronger over time. The income tax incentives that Guam would likely grant to airlines and tour operators serving the island will enhance and accelerate growth in the industry. However, lingering doubts about stability and the resulting investor and traveler uncertainty regarding a newly independent country may lead to slower growth in tourism than would be the case under other status options.

## **Defense**

Because of Guam's historical ties with the United States, a supportive arrangement regarding mutual defense is virtually certain. Given the value to Guam's economy of the industrial aspects of the U.S. military presence, and the value to the U.S. of its military infrastructure and strategic positioning in Guam, it is expected that U.S. military operations will continue in Guam, at least through and beyond the study period. This arrangement will be accomplished subject to an agreement between Guam and the United States as a part of the regional defense pact that includes the former Trust Territories. It must be clear to the people of Guam, though, that U.S. interests will dominate this arrangement.

While Guam will maintain its own small military force, primarily for local coast guard activities and to control civil disorder, there will be a great deal of reliance on U.S. technical, financial and intelligence assistance to reinforce domestic defense capabilities. Through joint training exercises and loans or grants of surplus equipment, Guam's forces will be closely aligned with the U.S. military. A portion of the recurring value to the U.S. of military base retention in Guam will be offset by associated U.S. federal contributions to Guam, both in the area of defense and in other areas more associated with economic growth and development. Depending on the U.S. view of the volatility of the Asian region, coupled with Guam's degree of acceptance of a U.S. military presence (in comparison with the acceptance by other nations in the region, e.g., the Philippines and Japan), there may be a moderate-to-high industrial impact associated with the continuing U.S. military presence in Guam.

Under this relationship, the U.S. will sponsor Guam's participation in bilateral and multilateral defense pacts in the region. This will help Guam by providing multiple sources of defense assistance to the island, and will also help the U.S. by serving to distribute the costs of maintaining its influence in this part of the world among other nations.

## **Transportation**

Just as every other sovereign nation does, Guam will control transportation into and out of the island under independence. As a result, Guam will enter into bilateral agreements with other nations, including the U.S., regarding airline landing rights. Because Guam does not have a domestic airline that flies international routes, it is likely that the island will dispense these rights in exchange for guaranteed service, as well as financial assistance associated with airport operations and maintenance. The continuation of Federal Aviation Administration air traffic control oversight is possible, for a fee. However, this service should be heavily subsidized, since the U.S. will seek to leverage facilities, infrastructure and personnel to support parallel military aircraft activity. In bilateral negotiations with other nations for landing rights, Guam may also incorporate consideration of maritime access in its bargaining position.

Seaport operations would continue to be conducted by Guam, although U.S. and other foreign financial assistance may be available, either through negotiation of harbor rights or by unilateral grants and loans. However, a significant economic benefit to Guam from independence would result from the termination of the applicability of the Jones Act in U.S. trade with the island. Because of the corresponding reduction in shipping costs, the prices of goods from the U.S. arriving in Guam would be significantly lower than they are under the *status quo*.

While the level of air and sea-borne transportation services into Guam would be approximately the same under independence as under the *status quo*, both this level and the associated unit costs for shipping passengers, cargo and baggage would fluctuate with the level of economic activity. Overall, though, there will be little or no change in the level or patterns of air and sea travel into and out of Guam after the transition to independence.

## **Trade**

There will be virtually no practical change in Guam's external trade due to the transition to independence, other than changes that would have occurred regardless of political status. Those practical changes that will occur relate to increased restrictions on technology transfers and a

termination of little-used trade preferences with the United States. The Guam Customs and Quarantine Department will continue to control inbound shipments through Guam's ports, pass-through trade will remain dominant, and merchandise imports will far exceed exports. Guam will maintain its bias for free trade, with no quotas or tariffs on imported goods, except possibly to protect whatever new manufacturing enterprises may develop.

Because Guam is outside of the Customs Territory of the United States under the *status quo*, there are already significant restrictions on technology transfers into the island. The objective of these U.S. State Department controls is to prohibit the transfer of technology (particularly technology with potential military uses) to most foreign nations, and especially to nations that are perceived as being hostile toward U.S. interests.<sup>84</sup> As an independent nation, though, Guam is likely to lose those few waivers that are granted under the *status quo*. This will make it more difficult to acquire the latest computer, medical and manufacturing technologies in Guam, but because the waivers are rarely used, the impact on the economy from this will be moderate.

As an independent nation, Guam will no longer qualify for duty-free entry of its products into the U.S. under Headnote 3(a) of the Harmonized Tariff Schedules, but this preference will be replaced with a superior trade preference granted to Guam as a part of the political status negotiations. It is likely that Guam will remain eligible for favorable treatment under the Generalized System of Preferences of some nations, and most-favored-nation status is also likely for trade activity with most countries. However, these provisions are not likely to have a significant impact on Guam's overall economy because of other factors that make manufacturing generally impractical on a remote, resource-poor island.

### **Attractiveness of Investment**

From the beginning of the study period, Guam's investment climate will be perceived as presenting a moderate-to-high level of risk to both outside and local investors due to the sudden change in the political environment and the uncertainty over how Guam will exercise its new powers. This perception, though, should change fairly quickly as Guam exhibits stability in its legal and judicial system, and implements a tax code that is favorable to investments in furtherance of the island's economic development.

Provided with the increased flexibility that comes with sovereignty, Guam will prepare a comprehensive set of incentives designed to attract and retain investment, jobs and income producing activities. Early in this process, there will be a general review and reform of the structure of taxes, with special emphasis placed on recognizing contributions to the community in the form of economic development as an offset to tax liabilities levied on income, property, sales revenues and specific commodities. Later, with improved planning and a greater social consensus, infrastructure will be developed to accommodate the needs of a growing economy, with a distinct emphasis on the types of industry that most appropriately utilize Guam's unique characteristics. There may be an inversion in the structure of property taxes to discourage the retention of idle land and to reward the constructive use of real estate.

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<sup>84</sup> The controls are administered by the U.S. Department of Commerce' International Trade Administration in cooperation with the U.S. Customs Service.

After the transition to independence, it is unclear whether Guam will retain the ability to issue tax-exempt municipal bonds in U.S. markets, and this will be a matter for negotiation. However, the issuance of private-purpose municipal bonds will certainly be more difficult than it has been in the past, and this should not be expected under an independent status. Nevertheless, Guam will have the authority to exempt its own bond issues and those of other jurisdictions from its internal revenue claims, and this may have the effect of bringing additional financial activity to the island.

## **Labor**

Under independence, Guam is expected to have a system of workers' rights and employer privileges similar to the *status quo*, with laws and regulations governing wages, hours, working conditions, job discrimination and other factors patterned after those of the United States. However, in contrast to the *status quo*, Guam's labor laws will be more flexible and readily adaptable to changing regional conditions in order to improve the island's competitive position in some industries. This may include separate wage scales for resident and non-immigrant workers, coupled with a job registry for resident workers.

Among other related functions, Guam's labor programs will include locally-funded statistical programs to monitor employment and industry conditions. These programs may be linked with broader statistical functions to measure the performance of the overall economy for policy and planning purposes.

## **Other Private Sector Considerations**

In recognition of the need to stimulate more rapid and aggressive development of private economic activity, Guam will emphasize private sector development immediately upon the transition to independence. One of the first initiatives in this process will be the privatization of a host of government services that are not directly related to the public health and safety. This will both expand the island's tax base and reduce the demands on the public purse, allowing the implementation of a lower average tax burden and tax incentives to encourage further private development.

These efforts to restructure Guam's economy with a bias toward private activity and away from dominance by the government will be supported by the U.S. and international agencies through planning and technical support, along with moderate levels of financial aid. To ease the transition, there will be a temporary continuation of public programs provided by the U.S. federal government in Guam, including economic development support (particularly in the area of infrastructure development) and depository insurance. It is likely, though, that the financial industry in Guam will expand and diversify relatively quickly as Guam exhibits increasing openness to the entry of U.S. and foreign banks, securities trading houses, insurance companies and other intermediaries.

Because of the nature of the services provided and the continuing presence of the U.S. military, it is likely that some U.S. federal programs will be institutionalized in Guam, to continue indefinitely after the status transition. These include the programs of the National Weather Service, the Federal Emergency Management Agency (with some curtailment of that agency's sweeping powers), the various law enforcement agencies (particularly as they relate to drug enforcement) and those related to public health. Some of these programs will be extended

to Guam on a fee basis, but are likely to be substantially subsidized by the U.S. government. For instance, as mentioned earlier, the activities of the Federal Aviation Administration in Guam are likely to be continued, as they relate as much to military aircraft as to civilian aviation activity.

If the activities of the U.S. Postal Service are maintained, postal rates will be rationalized at a significantly higher level. A few other U.S. federal services may also continue.

Generally, though, as a sovereign, independent nation, most U.S. federal laws and regulations will no longer apply in Guam. Only a portion of the full body of U.S. law, of course, is relevant to Guam, but there will be a need to adopt new Guam laws to replace their U.S. precursors. In this process, it is likely that some of the U.S. Code will be adopted wholesale, while other U.S. laws will be tailored to more effectively meet the needs of the island. In some cases, it will be appropriate for Guam to build portions of its legal structure through innovative and creative processes. While the island will not begin its independent status with a “clean slate,” the latitude of the community to formulate a suitable legal environment will be substantial.

## **Health**

Because health and health care are high U.S. and international priorities, the U.S. government is likely to make substantial efforts to maintain a baseline level of health care services in Guam, despite the transition to independence. However, funding for the attendant programs will change, with a phased discontinuance of formal, direct U.S. health care funding through grants. Support will come in the form of advisory services and technical assistance, as well as through foreign aid, whether directly or through third-party international organizations.

Obtaining technical assistance in health care through international organizations will be more complicated than the systematic assistance under the *status quo*, but this type of help in maintaining standards of health care in Guam will be readily accessible.

## **Education**

Although the transition to an independent political status will occur at a moment in time, the repercussions of the transition, perhaps better termed the “transition phase,” will occur over a period of many years. There is a great deal of inertia in the system that will be difficult to overcome, and it will take time for the transition phase to finally work its way through. Therefore, during the study period (the first five years of independent status), there will be a continuation of existing educational standards in Guam. During this period, there will continue to be a substantial resource reallocation, increasingly directed to the benefit of long-term residents as the vestiges of uncontrolled immigration gradually dissipate.

It is expected that there will be a negotiated continuation of U.S. federal education grants and student financial aid programs dedicated to Guam, but at a significantly lower level than under the *status quo*. Because Guam’s public school system will be empowered to develop a more locally- and regionally-relevant curriculum, the educational system will continue to be segregated. While Guam’s public schools will operate under international standards, the Department of Defense Education Agency (DODEA) will continue to operate under U.S. standards.

## Fiscal and Monetary Policy

Once a set of laws governing commerce is in place, fiscal and monetary policies are the primary ways in which a national government can attempt to control the level of operations of its economy. Even so, there are certain limits on how effective these policy tools can be. If they are misused, they could cause significant difficulties in the economy, and adversely affect standards of living. If used properly, though, they can help to sustain periods of expansion and shorten periods of recession within the economy, generating more rapid long-term growth.

As a sovereign nation under independence, Guam will have essentially complete control over its fiscal policy, within the limits of its ability to incur debt or, in the alternative, rationalize accumulated surpluses. While there will be uncontrolled levels of some funds flowing into the government of Guam due to both international aid programs and U.S. expenditures, grants and transfers, most of the public sector's revenues will be derived from taxes and fees levied locally. Whenever there is an imbalance between the government's tax revenues and its expenditures within the domestic economy, the effect will either be stimulative (if expenditures exceed revenues, and the government incurs debt) or contractionary (if the government operates with a fiscal surplus) on the level of economic activity. While this imbalance is inevitable during the course of government operations, it will usually be small and often unintentional. When it is intentional, though, it will also typically be relatively large. In these instances, the government is engaged in discretionary fiscal policy, and may actually succeed in smoothing the fluctuations of the business cycle, improving the long-term pattern of economic growth.<sup>85</sup>

Under independence, the comprehensive authority of the government of Guam over its fiscal policy will allow (but not necessarily require) some control of the economy through budgetary deficits (financed with government debt) or surpluses (by drawing down accumulated debt or outright saving). It should also be noted that the structure of taxation and/or expenditures can be manipulated in order to affect the level of economic activity, but this method is rarely used to control cyclical fluctuations because of the instability and long-term uncertainty that it introduces into the business environment.

It is almost certain that Guam will adopt the U.S. Dollar as its currency under its independent status. If so, there are virtually no elements in monetary policy (except for usury laws and the reserve requirements applied in the banking system) that the government of Guam could exercise. As the U.S. federal government exercises its discretionary monetary policy authority, with little or no regard for Guam, the island will have to passively accept changes in Dollar-based interest rates, foreign currency exchange rates and, to some extent, the rate of inflation.

It has been suggested by some that Guam issue its own currency, but even disregarding the historical record of governments abusing their own currencies, there are several factors that dictate against this. Not the least of these is that the currency would hardly be recognized internationally because of the miniscule volume (by global standards) that would be in circulation. Establishing a stable exchange rate would be almost impossible. Even if a stable

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<sup>85</sup> This discussion of discretionary fiscal policy is very generous and optimistic. To exercise this type of control over the business cycle, the government would need nearly perfect information about the economy and its future, and would have to be willing to accept the political risk of running budgetary surpluses during cyclical peaks. This is a risk which governments, historically, have been unwilling to take.

exchange rate were possible, it would probably be accomplished by “pegging” the value of Guam’s currency to the U.S. Dollar, some other currency, or a weighted average of several other currencies. In any case, a currency “peg” would still obviate Guam’s discretionary authority over monetary policy unless the ratio at which the “peg” is set is periodically changed. This, though, would be similar to using a pipe wrench to fix a wrist watch: the tool would overpower the system it intends to repair.

It has also been suggested that Guam adopt a different currency for its internal use. One obvious candidate is the Japanese Yen, since it is a relatively stable currency that is internationally recognized and widely used in the Asian-Pacific region. While this idea has some appeal, there are a few complications involved. One of these is that Guam imports approximately fifty percent of its goods from the U.S. under the *status quo*, and the adoption of the Yen would introduce exchange rate risk into the island’s primary trading relationship. Although the possibility of adopting the Yen as Guam’s currency is certainly an idea that merits further study, it is one that is far beyond the scope of this report.

### *Taxation*

Although there are several ways to group the numerous taxes that are levied in Guam, they can perhaps most effectively be divided into three categories for the purposes of this report: income taxes, business privilege taxes (which include excise taxes and licensing fees) and real property taxes. Within these broad categories, it is not likely that there will be substantial changes in the general framework of Guam’s taxes because of the transition to independence, but there will be some modifications in the details and structure that will have significant effects on the economy and economic development.

As a part of the transition by Guam into a sovereign and independent nation, the Organic Act will be repealed. This will terminate Section 31 of the Act, which establishes a “mirror” of the U.S. Internal Revenue Code as Guam’s local income tax code.<sup>86</sup> It is likely that Guam will initially adopt this same code as its own internal income tax law, but that it will be modified to provide for automatic incentives for investment and other economic development activities. In essence, a process that is now administered by the Guam Economic Development Authority under its Qualifying Certificate program will be codified, with the types of activity eligible subject to periodic updating, and providing tax credits or exemptions rather than rebates for eligible activities. The perceived “loss” of revenues in specific instances will be more than recovered through an expansion of the tax base.

With the repeal of the Organic Act comes the termination of Section 30,<sup>87</sup> as well. This Section provides for the recovery by Guam of income taxes anticipated to be paid during the following year by employees of the U.S. federal government who are either residents of or domiciled in Guam. While it is possible that there will be a continuation of this transfer into the Treasury of Guam, it will be subject to negotiation, and is likely to be phased out over time in any case. However, the annual funds received under Section 30 averaged 7.7% of the government of Guam’s overall tax revenues from FY’93 to FY’97. Eventually, these would either have to be replaced with a modification of the Guam tax code (whether through income

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<sup>86</sup> 48 USC Chapter 8A, § 1421i.

<sup>87</sup> 48 USC Chapter 8A, §1421h.

taxes or otherwise), or there would have to be a net reduction in the services provided by the government of Guam.

It is not likely that there would be any significant change in business privilege taxes due to the transition to independence, since one of the primary objectives of the government will be to maintain as much stability and continuity for business as possible. However, it is likely that there would be substantial changes in the real property tax. Guam's effective property tax rates under the *status quo* are 0.175% of the appraised value on land and 0.35% of the appraised value of improvements (structures). These rates are extremely low by U.S. standards, and generated only \$13.9 million annually from FY'93 through FY'97, some 2.3% of Guam's total tax revenues. Aside from the issues that the tax rates are abnormally low and the revenues generated are almost inconsequential, the structure of the real property tax, at best, fails to encourage development; at worst, it actually withholds scarce land resources from productive economic activity. After the transition to independence, it is likely that real property tax rates in Guam will be increased to generate additional revenues. It is also possible that the structure of property tax rates will be inverted, so that a higher tax rate applies to undeveloped land, thus encouraging development.

Wage earners in Guam pay into the U.S. federal Social Security and Medicare systems through the Federal Insurance Contributions Act (FICA) taxes. While it is possible that the application of these taxes and the associated entitlement programs will be negotiated to continue in Guam, it is more likely that there will be a reversion of the U.S. federal programs and the supporting taxes into local programs and taxes. If so, it is likely that the equivalent of the Social Security program will be merged into the government of Guam retirement system for more efficient investment and administration. The equivalent of the Medicare program will probably be handled in the same manner as a group medical insurance program.

### *Transfer Payments*

It is expected that the U.S. system of entitlement programs and other social transfer payments will be terminated upon the transition to independence in Guam, with the possible continuance of those programs supporting the aged, the blind and the permanently disabled. However, in order to provide for a more orderly transition, it is likely that grants to the government of Guam will be increased to fund parallel programs in Aid to Families with Dependent Children, Women and Infant Care, Food Stamps and other entitlements for a period of time after the transition.

After the transition to independence, it is likely that the payment of benefits under entitlement programs to non-Guam citizens will undergo a significant reduction, while affected Guam citizens will experience only a moderate decline in entitlement program income.

### *Retirement Programs*

As mentioned above, it is expected that the structure of the Social Security System under the *status quo* will revert to a local system under independence, and likely be merged into the Government of Guam Retirement Fund. Other programs providing retirement security for the aged will be somewhat curtailed, as the people of Guam rely instead upon the traditional care for the elderly by their offspring and other family members. As a prominent exception, health care

for the elderly will be financed through a collective medical insurance program, but will probably be needs-based in order to reduce costs.

### **Distribution of Income**

Because of a moderate redistribution of rights and entitlements favoring Chamorros and other Guam citizens, it is anticipated that the distribution of income in Guam under independence will become more focused in favor of Guam citizens and/or indigenous residents. While opportunities for earning income will remain available to all persons residing in Guam, the income distribution will be skewed to the benefit of long-term members of society.

## **Estimates of the Magnitude of Impacts**

The fundamental question to be addressed in this report is, “How will each of the status changes being considered affect Guam’s economy?” As in many areas of economics, the answer is far more complicated than the question. In this particular instance, the problem is even more complex because the political status question itself is still unresolved.

From the perspective of the Commission on Decolonization and the Task Forces on Statehood, Free Association and Independence, the first issue is for Guam’s eligible voters to select from among the three options. Once that is done, the work of precisely defining what Guam wants under the chosen option will begin.

This, in itself, is an enormous task. However, the next step will be to convince the U.S. Congress that Guam should be granted the political status that the eligible voters have selected, and that the characteristics defined by Guam as to what it wants under that option should be granted. History has shown that the U.S. Congress is rarely disposed to give Guam exactly what it wants, so the characteristics of the island’s ultimate political status, and how they affect the performance of the economy, will undoubtedly be significantly different than what anyone could anticipate today.

Therefore, predicting Guam’s economic conditions five years after any political status change is both complicated and subject to several sources of error. The only certainty is that a status change will be accompanied by shifts in the internal and external forces that define the economic prospects and opportunities of the people of Guam. What these changes will be is subject to the status selected and to the negotiations that will follow. The magnitude of these changes is unknown, as is the speed with which they will occur. There may be other, unanticipated conditions that alter the ways in which the other changes manifest themselves.

Despite the prevailing environment of uncertainty in predicting Guam’s economic future under the three status options, there are several aspects of the change that are highly probable. Again, history serves as a general guide, and provides strong evidence regarding some of the likely institutional results of each available option. These probabilities are discussed in qualitative terms in the foregoing sections of this report; quantification is more difficult, but possible with a sufficient set of assumptions. Some of these assumptions are strong, almost to the point of being truisms. Others, perhaps most, are based upon the best information available, but are subject to that information being insufficient. They are the most carefully studied assumptions available, nonetheless.

While considering how to vote for a preferred political status option, individuals will typically try to predict how the outcome will affect them, their jobs, their families, their community and a number of other important considerations. In the ideal, this study would provide valuable guidance to each individual with regard to the details of the results of their specific vote. If this study were based upon certainties, it should at least give information as to how different industries within the economy would be affected. With comprehensive information regarding the factors affecting Guam’s economy in the past, it might at least be possible to develop a sectoral forecast of the economy under various scenarios within each status option. Given that none of the necessary conditions exist, the following represent the best estimates possible within the constraints that exist.

## **Objectives**

This portion of the report will examine the impacts of each prospective status change on the level of Guam's "Gross Island Product" (referred to as "Gross Domestic Product" in most jurisdictions). This is the broadest measure of Guam's economic performance, and measures the total amount of production, economic output, that is generated within the confines of Guam's borders in a year. At best, it answers the question as to how any particular status change will affect the overall community of Guam.

It is likely that there will be immediate impacts on the economy within each status option. These impacts will undoubtedly be small, since a negotiated status change would include provisions for a relatively smooth transition. Nevertheless, changes will occur, and some may be expedient. A description of the immediate economic impacts of each transition will be provided as a part of this analysis, but it will not be substantially different from the *status quo*.

The immediate "shock" of a political status change may be minor, but a more discernable impact will have manifested itself by five years after the transition. Many existing U.S. federal programs will have been modified or terminated altogether. A change in the number or other characteristics of immigrants will affect the GIP (GDP) of Guam. There may be significant changes in the level of private investment and/or military expenditures flowing into Guam. Although the full effects of a status change will not have worked their way through the system, both the direction and magnitude of the change in the island's GIP should be evident.

While this report will not predict the details of the changes in Guam's economy due to a political status change, it will give estimates of Gross Island Product one year after the transition to each prospective new status, as well as after a period of five years. This information, while not at the level of detail that some might desire, should help Guam's eligible voters in their evaluation of which status option they should select.

## **Obstacles and Complications**

As indicated, there are several factors that make forecasting future economic activity in Guam difficult. This is true with regard to the *status quo* to some degree, primarily because the socio-economic data available for the island are insufficient to support a comprehensive econometric model. Several attempts have been made over the past thirty years to develop models that provide reasonable estimates of economic activity, but each has suffered from data limitations. Making matters worse, the data itself is sometimes found to be flawed or inconsistent, making the results of the models less than reliable.

In reviewing existing models of Guam's economy, it was discovered that they had not been updated for several years; in trying to perform the updates independently, it was determined that figures for some data series that were available in the past are no longer compiled. Thus, Guam's ability to forecast economic activity using existing models has practically ceased. While it is not the purpose of this report to make recommendations, it must be noted that a good foundation in quantitative forecasts is essential in both public and private planning and budgeting. The failure of the government of Guam to compile the requisite information results in faulty decisions by both the government and by private firms and individuals. Therefore, it is recommended that Guam implement a comprehensive effort to develop a sound and reliable set of socio-economic statistics, regardless of which political status choice is made.

Because of the shortcomings of existing models and the data upon which they were based in the past, it has been necessary to devise an alternative approach to measuring the effects of a change in political status. The method used, though, has only been cursorily tested for accuracy. Initially, this was cause to reject this approach, but upon discovering that no other approach would be adequate, this alternative was reconsidered. While it is based upon estimated parameters and cautious assumptions about the actions of Guam and the United States, respectively, it more closely addresses the issues at hand than would any of the more traditional models.

The element of time should also be mentioned as an obstacle to the formulation of a more detailed and accurate economic model. There has simply not been sufficient time in the preparation of this analysis to reconstruct historical data or test various iterations of parameters against actual results. With sufficient resources and appropriate data, the construction of a comprehensive model of Guam's economy would be a worthwhile endeavor.

### **Methods Explored**

In 1994, there was a model developed by the KPMG Peat Marwick Policy Economics Group to estimate income in Guam. This model was primarily constructed to provide input data into another model that was designed to estimate prospective tax revenues, but offered the additional benefit of generalized economic forecasting. The model employed a simplified sectoral structure, and incorporated information regarding the principal sectors of Guam's economy, as well as several external ("exogenous") variables. While the model is relatively sound, and covers some 85% of Guam's economy within its scope, it also relied upon quantitative inputs that are no longer available. Thus, this model could not be used in preparing this report, and would have been of limited use in any event, since each political status option would modify some of the parameters of the model in ways that would be virtually impossible to address.

At the same time, the former Chief Statistician of the U.S. Department of Commerce, Mr. Frank de Leeuw, visited Guam and developed a model for measuring (but not forecasting) GIP based upon the "incomes approach."<sup>88</sup> The data used in this model were principally gathered from the tax records of the Guam Department of Revenue and Taxation, and published data from the Bureau of Labor Statistics, Guam Department of Labor. Custody of the model was with the Guam Finance Commission. With the departure of the responsible employee from that agency several years ago, maintenance of the model stopped. Furthermore, the Department of Revenue and Taxation quit compiling the data in the form and format necessary to operate the model. Thus, the model is not currently updated or used. However, tax revenues and their measurement are indirect results of economic activity, so for the purposes of this study, several new models would have had to be created to estimate the effects of changing political and economic parameters on different classes of tax revenues. This process would have introduced numerous additional potential errors into the estimates, making them less than thoroughly reliable.

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<sup>88</sup> Rather than measuring GIP by adding together the value of all of the final outputs in the economy during the year, the incomes approach adds together all of the sources of income for the year. If the data are accurate and complete, this will return exactly the same figure as the outputs approach, since every Dollar spent to purchase an economic output, thus registering its value, represents a Dollar in income for the seller.

A third approach was then developed for this study. It is simple and straightforward, and it directly addresses the types of change that are anticipated in the early years following a status change. As stated earlier, there will be internal changes in Guam's economy under each of the contemplated political status changes, but none of these changes are expected to be particularly radical, and their impacts on GIP should be small (at least during the first five years). The important changes that can be expected to occur during the time frame of this study relate to the cross-border flows of funds into and out of Guam. Depending on the types of economic activity related to each funds flow, their impacts on GIP will express themselves as some multiple of the change in each flow through the multiplier effect, discussed earlier. By estimating the changes in the flow of each category of funds under each status option and applying an appropriate multiplier to each in turn, the prospective change in Guam's GIP can be estimated.

### **Notes on the Selected Method**

As in any model of economic activity, the results of this model are subject to error. In this particular case, though, the margin of error will be especially large because of the uncertainty regarding the final negotiated conditions under any of the political status options, the estimates of the magnitude of assumed conditions, and the limitations of the predictive model.

Although each of the relevant socio-economic conditions are stated earlier in this report, based upon a carefully derived and generally accepted set of common assumptions (see Appendix 2), the final negotiated conditions under which the transition occurs could be quite different in many respects. By necessity, the method employed in the economic forecast must be based upon the assumed conditions, fully recognizing that the assumptions may be less than perfectly accurate.

Given the qualitative assumptions as stated, an estimate of the magnitude of the aggregate amount of cross-border funds flows that they engender has to be made. This is necessary in order to provide the quantitative measures to be used in estimating Guam's GIP. However, even within the context of the qualitative assumptions, the quantitative measures used in the model are, by definition, subject to variability. Although the measures used are based upon the experience of other places that have undergone (or are undergoing) a political status change, the fundamental differences between Guam and those other places require the estimates of the measures to be adjusted to more effectively represent the island's unique characteristics and circumstances. These adjustments are based on the history of status changes in other places and upon the collective experience of five long-term observers and analysts of Guam's economy relative to other places, but they are, in the final assessment, subjective. The underlying assumptions for each status option are provided in matrix form in Appendix 3.

Finally, the model itself is subject to three principal sources of error. First, it implicitly assumes that there are no substantial changes in the structure of Guam's economy that affect the strictly internal aspects of economic production. Second, exogenous changes such as a recession in the United States or a shift in the Dollar/¥en exchange rate are assumed not to occur. Third, although the outcome of the model is moderately sensitive to small changes in the multipliers, these values must be set at some level, and the best judgement of the researcher is again an element in deriving a final GIP figure.

It is likely that, by the end of five years, internal manifestations of the political status change will begin to become evident. However, the level of magnitude and even the direction

for some of these manifestations are debatable. The complex interactions that exist among various parameters of the economy may be altered, whether because of the status change or for some other reason, but the effect of these changes is not expected to be large in an overall sense. While there may be proportional shifts among different sectors in the economy, with some becoming relatively larger as others recede, it is not likely that there will be the significant changes in efficiency in such a short time frame so that a substantial impact on GIP would be realized.<sup>89</sup> Nevertheless, the possibility does exist that a status change could stimulate some latent internal dynamic that would lead to a significant change in the economy, independent of changes in cross-border flows of funds. Although this possibility is not ruled out, it also cannot be incorporated into or even accommodated by the model.

For purposes of this report, it is necessary to assume that there are no significant external shocks to the economy, such as a U.S. recession, a war, a massive change in trade activity or exchange rates, and so forth. For the results of this report to be meaningful to Guam's eligible voters, the effects of a political status must be isolated from the effects of a change in other, unrelated events. Although these other types of change are certainly important and their impact on Guam's economy can be substantial, they are held constant in this model so that the respective impacts of the prospective political status changes are not masked or distorted by other factors.

The model used in this project examines the impact of the changes in the flow of funds into Guam's economy. However, the accumulated impact of a status change depends not only on changes in fund inflows, but also upon how those funds are spent in the economy. Different types of expenditures will have different outcomes. In an initial expenditure from the outside, a Dollar spent in Guam's economy generates a Dollar of income; whatever is spent by one person must be received by someone else. That Dollar, though, can have a variable impact on the overall economy, depending on *how* it is spent. Perhaps the most clear example of this is the difference between a Dollar spent on paying a soldier and a Dollar spent on educating a student. The soldier receives his Dollar in income, and spends it at the Commissary, where ten cents stays in Guam as income to a store clerk and the other ninety cents flows out of Guam to pay for whatever the soldier purchased. The clerk, in turn, also spends that ten cents in the Commissary, with nine cents going off-island to pay for the goods and one cent remaining in Guam as part of a warehouseman's wages. In total, the first Dollar paid to the soldier generated \$1.11 in income in Guam.

Another Dollar is spent to educate a child. The school receives that dollar as income, and pays teachers and power bills and other obligations, but the full Dollar remains in Guam. The teacher buys groceries and other items in civilian stores, generating income for those stores that pays the salaries of clerks, some profits to the owners, income for managers and so forth.

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<sup>89</sup> For instance, the privatization of some functions performed by the government under the *status quo* may improve efficiency and release resources to be used elsewhere, but there is no assurance that those resources would not simply be left idle. This is particularly true, given the level of unemployed labor resources in Guam in recent times.

In addition, the distinction between income and wealth should be noted. There is the possibility that a change in political status to free association or independence would significantly change the availability of land resources to the civilian community in Guam. If so, land prices would fall, and a significant redistribution of wealth within the community would occur. This could have secondary effects on saving and investment, thus affecting the overall level of economic activity.

Perhaps sixty percent of the Dollar leaks out of Guam to purchase the goods that the teacher bought, but the other forty cents becomes income for other people in Guam. When those other people spend their income, another sixty percent leaks out of the island, but twenty-four cents becomes income for other people. In just two rounds of spending, the Dollar spent on education has had an impact of \$1.64 on incomes, far greater than the Dollar paid to the soldier. Therefore, *how* money is spent can have an important impact on the total income generated by that expenditure.

There are no summary figures for Guam that define the multiplier effect on income of various types of expenditures. The closest approximation available applies to Hawaii, but those figures will be higher than Guam's because Hawaii relies proportionally less upon imported goods than does Guam. The leakages out of Hawaii are generally smaller than for Guam simply because Hawaii has a better-developed and more diverse economy. As a result, the researcher must adjust the multipliers for Hawaii in order to estimate figures that are more appropriate in Guam's economic circumstances. Despite the consensus of a group of experienced researchers regarding the appropriate multipliers for Guam, there is still the potential for error in the final figures used.

### **Model Structure, Parameters and Data**

The model is based upon inflows of funds to Guam through U.S. federal government spending, tourism receipts and investment expenditures. The data which provide the foundation for the analysis is both comprehensive and current. The U.S. federal government expenditure data are for FY 1999 and are from published U.S. Department of Commerce expenditure reports for Guam. Data derived from local sources, such as tourism and investment inflows, are similarly current, as of the most recent fiscal year. Funds received by the government of Guam under §30 of the Organic Act are segregated from other grant awards within the U.S. federal budget because of their possible loss due to a change in political status. Also to accommodate a change in status, new categories of inflows are added to account for transitional assistance, possible U.S. military base rental payments to Guam and foreign aid. Potential new outflow categories consist of the redirection of income taxes under the U.S. Internal Revenue Code to the U.S. federal government rather than the government of Guam and the imposition of U.S. federal government excise taxes on items purchased in Guam. These categories of funds flows are the foundation for the investigation of each of the three political status options for ease of comparison.

Based upon the experience of other locations that have undergone a change in political status (wherever practical) and upon the collective judgement of the researcher and his associates, an income multiplier is assigned to each of the funds flow categories. Typically, these multipliers range from 1.2, for those expenditure categories which generate few or low-proportion subsequent rounds of expenditures as they circulate through Guam's economy, to 1.7 for those categories which support a greater amount of subsequent spending (particularly the purchase of locally-produced services rather than imported goods). Flows that support a moderate amount of subsequent spending were assigned a multiplier of 1.4. Defense procurement expenditures present a special case, since only a small fraction of those funds actually enter Guam's economy at all; this flow is assigned a multiplier of 0.2.

Normal outflows of funds from Guam's economy for the purchase of goods and services from other places are not expected to deviate significantly in structure within the study period due to a political status change. Therefore, they are left to be reflected by the multiplier rather than being incorporated into the model as an outflow of funds. Otherwise, different multipliers would have to be applied to funds flow categories in each time period. Although it is not likely that this exercise would significantly improve the results of the model, it would certainly introduce yet another source of error.

Multiplying actual expenditure figures in each flow category for 1999 by their respective multipliers served as a test for the model, generating an estimate of Gross Island Product of \$3.009 billion, remarkably close to the benchmark figure of \$3 billion designated for this report. This exercise served as a test of the model, and the outcome was also compared with other studies of sectoral contributions to Guam's GDP with good results. Although this validation of the model was limited, it is deemed sufficient within the limits of accuracy of the model discussed earlier.

As has been made abundantly clear, there is a great deal of uncertainty regarding the economic results of each status option. Although this uncertainty is greater for independence and free association than for statehood, each funds flow category was assigned a low, expected and high level of percentage change for one year following each potential political status change. A second set of low, expected and high percentage changes is assigned to each funds flow category for the period five years following the political status change. For some funds flow categories, the percentage changes are relatively certain and straightforward; for others, the best judgement of the researcher, in collaboration with his associates, is applied.

Finally, multiplying the actual 1999 funds flow for each category by its assigned percentage changes and then by its respective income multiplier results in a range of potential Dollar changes in Guam's GDP for each category under each status option, both one year and five years into the future. Summing these results under the low, expected and high levels of change for one and five years after the status change for each of the status options provides this report's estimates of the potential economic impact of each status option under consideration.

## **Model Results**

The results of the model indicate something less than a profound effect on Guam's economy due to a change in political status. Looking strictly at the expected case of the results after one year, statehood would generate an increase in Guam's Gross Island Product of some \$194 million, just 6.45% of the \$3 billion benchmark. Free association would cause a decline of \$239 million (7.98%) in GIP and independence a decline of \$374 million (12.48%).

After the fifth year, the results under each status change improve somewhat. GIP under statehood would increase by \$643 million (21.42%) versus the status quo, reflecting an uninspiring 4.0% average annual growth rate in the economy. The free association results turn positive, with GIP growing by \$151 million (5.02%) versus the *status quo*, or an average annual growth rate of 1.0%. The results under independence, in contrast, remain negative, but moderate somewhat, registering a decrease of \$255 million (8.51%) from the benchmark (an average annual growth rate of -1.8%). Since inflation is not a consideration in the model, these nominal growth rates also reflect real growth rates. For purposes of comparison, Guam experienced real growth rates approaching 20% annually in the late 1980s in the absence of any significant

change in the political relationship between the island and the U.S. federal government. A surge of foreign investment during that period had a far greater impact on Guam's economy than can be expected from the political status changes under consideration.

A table summarizing the results of the model is as follows:

Status	Change at One Year			Change at Five Years		
	Low	Expected	High	Low	Expected	High
Statehood	-\$116,347,493	\$193,529,809	\$680,867,942	\$78,793,762	\$642,672,767	\$1,403,944,560
Free Association	-\$917,794,711	-\$239,382,209	\$238,399,416	-\$665,231,016	\$150,526,972	\$965,366,115
Independence	-\$1,628,930,145	-\$374,252,603	\$590,653,208	-\$1,289,733,481	-\$255,158,877	\$1,015,875,968

With reference to the low versus the high cases in the first year under each option, it will be noted that the range of outcomes under statehood is more narrow than under free association, and that the range of outcomes under independence is even more broad than under free association. This is because there is greater certainty as to the results under statehood and less under independence. Of note, this pattern carries through to the fifth year, and the range of outcomes expands because of the increased uncertainty of predictions further into the future.

It should also be noted that, in the high case, the results for independence are somewhat better than those for free association, and approach the results for statehood in the fifth year. This is because of the greater latitude in policy formulation under independence than under free association. With the proper policies, Guam holds the potential under independence to establish a more dynamic economy and attract more external funds than would be possible under the closer ties to the United States inherent in free association.

Overall, the model and its results have withstood all of the tests that have been applied by the researcher and his associates. It provides a sound analysis of the prospects for Guam's economy under each of the three status options, within the constraints of the necessary assumptions. Beyond its use in this context, projecting future economic prospects from a base of current, reliable funds flow data, the model should be useful in making future economic forecasts for Guam's economy, and even for testing the potential outcomes of policy initiatives that may affect the island's economy.

**Appendix 1: Federal Expenditures in Guam, 1998 & 1999**











## **Appendix 2: Common Assumptions**

















## **Appendix 3: Model Assumptions**







## **Appendix 4: Economic Model of Status Option Results**





## **Interviews**

The following individuals were interviewed during the course of preparing this report. Their input and contributions were invaluable in gaining a more clear perspective on Guam's political status aspirations and the obstacles and potential pitfalls that the island and its people face in the process.

Mr. Jon Anderson, President, Sorenson Pacific Broadcasting

Ms. Eloise Baza, President, Guam Chamber of Commerce

Mr. Paul Calvo, former Governor of Guam

Mr. Mark Charfauros, former Senator, Guam Legislature

Mr. Charles Crisostomo, former Administrator, Guam Economic Development Authority

Mr. Eddie Duenas, former Guam Senator and Chairman, Statehood Task Force

Mr. Jose Garrido, Chairman, Free Association Task Force

Mr. Anthony Leon Guerrero, President, Bank of Guam

Mr. Peter Leon Guerrero, former Director, Guam Bureau of Planning

Mr. David Lujan, Esq., former Member, Commission on Self-Determination

Mr. Rufo Lujan, Chamorro Land Trust Commission

Mr. Joe Murphy, Editor Emeritus, Pacific Daily News

Mr. Pete Perez, Esq., former Member, Commission on Self-Determination

Dr. Robert F. Rogers, former Professor of Political Science, University of Guam

Mr. Tony Sablan, Chairman, Independence Task Force

Mr. Lee Webber, Publisher, Pacific Daily News

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