


# Public Testimony Sign-Up Sheet

Agenda Item C-3(d) BSAI CRAB CUSTOM PROC.

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NOTE to persons providing oral or written testimony to the Council: Section 307(1)(I) of the Magnuson-Stevens Fishery Conservation and Management Act prohibits any person "to knowingly and willfully submit to a Council, the Secretary, or the Governor of a State false information (including, but not limited to, false information regarding the capacity and extent to which a United State fish processor, on an annual basis, will process a portion of the optimum yield of a fishery that will be harvested by fishing vessels of the United States) regarding any matter that the Council, Secretary, or Governor is considering in the course of carrying out this Act.

MEMORANDUM

TO: Council, SSC and AP Members  
FROM: Chris Oliver   
Executive Director  
DATE: September 24, 2007  
SUBJECT: BSAI Crab Fishery Management

ESTIMATED TIME 10 HOURS (all C-3 items)
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**ACTION REQUIRED**

Initial review of analysis.

**BACKGROUND**

(d) Exemption of custom processing from processing share use caps

The recent reauthorization of the Magnuson Stevens Act (MSA) included a provision to exempt custom processing in the North region of the Bering Sea *C. opilio* fishery from processing use caps established under the crab rationalization program. The exemption is believed to be intended primarily to improve efficiency in processing in that fishery. At its February 2007 meeting, the Council received a staff discussion paper concerning the implementation of this amendment and the potential for the Council extending the exemption to other fisheries included in the crab rationalization program. After receiving the discussion paper, input from the Advisory Panel, and hearing public testimony, the Council elected to consider whether this exemption should be extended to include all of the traditionally small crab fisheries governed by the rationalization program:

- the Western Aleutian Islands golden king crab fishery,
- the Western Aleutian Islands red king crab fishery,
- the Eastern Aleutian Islands golden king crab fishery,
- the St. Matthews blue king crab fishery, and
- the Pribilof red and blue king crab fishery.

At its June 2007 meeting, the Council adopted a draft purpose and need statement and elements and options for the action. The regulatory analysis to implement the exemption for the North region of the *C. opilio* fishery is combined with the analysis and development of the amendment package considering extension of the exemption to the other fisheries. As requested by the Council, the analysis also examines a provision to exempt custom processing of transferred shares in their community of origin from the use cap. This issue arises because of the possible divestiture of shares by an entity to comply with the use cap. Under the current rules, on divestiture those shares could not be custom processed at the plant of origin, effectively forcing either a new processor (either shore plant or floater) to be opened in the community or the shares to be moved from the community. At this meeting the Council is requested to decide whether the analysis is sufficient to be released for public review. The executive summary of the analysis follows.

### Executive summary

In August of 2005, fishing in the Bering Sea and Aleutian Island crab fisheries began under a new share-based management program (the “rationalization program”). The program is unique in several ways, including the allocation of processing shares corresponding to a portion of the harvest share pool. Under the program, 90 percent of the annual harvest share allocation is issued as “Class A” individual fishing quota (IFQ), which must be delivered in a designated region and may only be delivered to a processor holding unused individual processing quota (IPQ). The recent reauthorization of the Magnuson Stevens Act (MSA) included a provision to exempt custom processing in the North region of the Bering Sea *C. opilio* fishery from processing use caps established under the crab rationalization program. This document analyzes that exemption and the interpretation of the MSA language, as well as options to extend the exemption to the following other fisheries:

- the Western Aleutian Islands golden king crab fishery,
- the Western Aleutian Islands red king crab fishery,
- the Eastern Aleutian Islands golden king crab fishery,
- the St. Matthews blue king crab fishery, and
- the Pribilof red and blue king crab fishery.

### Purpose and need statement

The Council has adopted the following purpose and need statement for this action:

*In remote areas and small TAC fisheries, the extended fishing seasons under rationalization may cause processing activity to be extended over a longer period of time. This temporal extension of processing activity, together with the lower throughput levels, limits the ability of processors to achieve production efficiencies. Allowing concentration of processing in fewer facilities, by exempting custom processing at a plant from the use cap of the plant owners, could increase processing efficiency. This efficiency increase could improve competition in processing. In some cases, exemption of custom processing at a facility from use caps of the owner could provide for contingencies in the event of a facility breakdown, assist in allowing full harvest of the TAC, and contribute to community sustainability.*

*In remote areas (e.g. the western region) with small TAC fisheries for crab species (e.g. WAI golden king crab) and extended fishing seasons, the goals of sustaining communities in the region and allowing the full harvest of the TAC could be better achieved by exempting custom processing beyond the processing use cap by processors.*

*Two of the objectives of the proposed action are to protect the economic base of remote communities dependent on crab processing, and to allow for the efficient prosecution of quota held by fishermen.*

*Under the rationalization program, community interests in historic processing are protected by granting communities a right of first refusal on the transfer of shares from the community of origin. In some instances, the combination of consolidation of processing share holdings and the counting of processing at a plant against the plant owner’s cap on the use of processing shares could complicate the retention of processing in the community of origin. Exempting processing of shares in the plant of origin from the use cap of the plant owner could facilitate retention of historical processing in communities.*

### Alternatives

The Council has identified the following two alternatives for this action:

#### Custom Processing Cap Exemption

##### Fisheries and Regions:

Custom processing will be exempt from use caps in the following regions and fisheries:

The North region of the Bering Sea *C. opilio* fishery (analyzed here for regulation change from MSA reauthorization – not optional)

- Option 1) the Western Aleutian Islands golden king crab fishery,  
Suboption: West region only
- Option 2) the Western Aleutian Islands red king crab fishery,
- Option 3) the Eastern Aleutian Islands golden king crab fishery,
- Option 4) the St. Matthew Island blue king crab fishery, and  
Suboption: North region only
- Option 5) the Pribilof Islands red and blue king crab fishery  
Suboption: North region only

Definition of custom processing exemption:

- Option 1) Physical processing of crab at a facility owned by an entity does not count toward the cap of the entity (only processor share holdings count toward an entity's cap).
- Option 2) Custom processing is the processing of crab received with IPQ that has 50 percent or less common ownership with the processing plant.

Locations qualified for the exemption:

Custom processing will qualify for the exemption provided that processing is undertaken in the applicable fishery and region at:

- Option 1) a shore plant
- Option 2) a shore plant, or a floating processor that is moored at a dock or docking facilities (e.g. dolphins, permanent mooring buoy) in a harbor in a community that is a first or second class city.
- Option 3) any shore plant or floating processor

Facility cap

Outside of the West region, no facility may process more than 60% of

- a) EAI golden king crab
- b) WAI red king crab

Provisions to protect interests of the community of origin

- Option 1) In the event that processing shares are transferred to the community entity holding the right of first refusal for those shares, the processing of those shares in the community of origin will not count toward the cap of the processing plant.
- Option 2) In the event that processing shares subject to a right of first refusal are transferred from the initial recipient, custom processing of shares in the community of origin will not be counted toward cap of the processing plant (the shares would only count toward the cap of the share holder).

Effects of the custom processing exemption on processors

One of the potential benefits of this action is an improvement in processor production efficiency. Under the status quo, the cap binds only if custom processing prevented by the cap would increase processor production efficiency gains from being achieved. Processors are unlikely to engage in custom processing prevented by the cap, unless they can achieve gains through that consolidation. The benefits from consolidation could also have distributional impacts within the sector. For example, consolidation of processing at a single facility beyond the cap will redistribute landings to the processor exceeding the cap from other facilities. In some cases, the share holder contracting for custom processing will be the operator of the facility losing the processing activity. In this case, it is difficult to argue that the plant suffered any loss from the cap exemption. In other cases, the removal of the cap will be a redistribution of custom processing activity from one plant to another. In this case, the redistribution of activity will have a processing efficiency benefit for both the share holder and the facility receiving the exemption, but that benefit will be at a cost of a loss of processing by the losing facility.

Several factors other than processing efficiency could influence the extent to which processing would consolidate under the exemption and its effects on the processor sector. First, processors must be able to reach an agreement on price of custom processing. In some instances competition within the sector could diminish consolidation, if a processor perceives a benefit from keeping its processing independent. Some processors may wish to attempt to develop new products which might not be possible (or as advantageous) under custom processing arrangements. Given that the proposed exemptions do not apply to all fisheries or regions, it is likely that these efforts would not curtail consolidation under the exemption – ample amounts of landings exist that could be used for product development in other fisheries and regions. In addition, product development is least likely to occur in remote regions with less access to the markets. Only in three small fisheries (the Western Aleutian Islands red king crab, Western Aleutian Islands golden king crab, and the Eastern Aleutian Island golden king crab fisheries) is the exemption being considered for less remote areas. Given these factors, the potential for consolidation under the exemption to curtail product development is limited.

The effect of this action will differ across processors. Since the exemption is necessary only, if a processor would exceed the 30 percent processing cap, a processing company will need to be a large presence in a fishery to benefit from the proposed exemption. Consequently, large processors in a fishery are the primary beneficiaries of this action. Processors that participate in the market the exemption is being used could be disadvantaged by the exemption. Processors not limited by the cap could find that the exemption constrains their ability to grow by removing shares from the already limited market. In some instances, small processors that choose to have their shares custom processed could benefit from this action, but that benefit is likely to be relatively small in comparison to the benefits to larger entities that use the exemption to consolidate processing activity beyond the current cap.

Since potential for custom processing under the exemption varies across regions and fisheries, the effects on the processing sector for each fishery and region are discussed independently. In the North region of the Bering Sea *C. opilio* fishery, in the first year of the rationalization program four plants operated. In the second year, only three operated. Based on the number of active processor accounts, most consolidation appears to have occurred at floating processors that have received deliveries for several different IPQ holders. IPQ holders in the North region in general have suggested that the current cap limits consolidation that would occur through custom processing in the absence of the caps. These IPQ holders generally assert that efficiency gains are possible by allowing processing to consolidate into a single facility. In drawing this conclusion, IPQ holders point to the extended period over which deliveries are made under the rationalization program. In the first two years of the program, North deliveries in the fishery were made over a period of in excess of four months. Based on the current TAC and IPQ cap (without the exemption) and the number of days between the first and last landing in the first two years of the program, a processor in the North region would receive on average between 50,000 and 65,000 pounds per day. If processing consolidated to a single facility in the absence of the cap, average daily delivery to the plant would be approximately 75,000 and 95,000 pounds (based on the current TAC and number of days between the first and last landing in the first two years of the program). In the North region, little processing occurs other than crab processing. Crab processing tends to be labor intensive, requiring relatively large crews. The cost of transporting, housing, and provisioning crews at more than a single plant in the North region is asserted by IPQ holders to substantially drive up the cost of processing. Allowing custom processing in excess of the cap could relieve some of these costs by reducing the costs of capital and crew.

The different options under consideration could influence the effects of the exemption on processors. Applying the exemption only to shore plants would provide a competitive advantage to the only shore plant in the area that currently processes crab – the shore plant in St. Paul. The ability to use floating processors would increase competition that might be limited, if the exemption applies only to shore plants. Requiring floaters to operate at a dock or docking facility to qualify for the exemption might drive up the cost of using a floater by requiring it to pay docking and wharfage costs (and in some instances additional costs related to permitting).

Applying the exemption to the North region of the Pribilof red and blue king crab and the St. Matthew Island blue king crab fisheries would have an effect on the processing sector similar to effect on the Bering Sea *C. opilio* fishery. The Pribilof and St. Matthew Island fisheries have not been open for several years. Both fisheries were historically prosecuted in the early fall, with most of the catch being made over a few weeks. Under the rationalization program, it is likely that the season would lengthen to some extent, but most participants believe that the fishery would continue to be prosecuted during the fall, possibly extending into the early winter. The current cap would require at least three processors to operate in the North region in both fisheries. As in the Bering Sea *C. opilio* fishery, consolidation through custom processing would reduce costs of capital and crews (transportation, housing, and provisions) by allowing all processing to occur at a single plant. Applying the exemption to the South would effectively allow consolidation by IPQ holders that are at or over the cap based on their North share holdings and processing activities. Processor efficiency benefits could be realized through the applying the exemption to the South, but those benefits are likely to be relatively minor.

Applying the exemption only to shore plants in the Pribilof and St. Matthew Island fisheries would provide a competitive advantage to the St. Paul shore plant - only shore plant in the North region. In the South, where several shore plants process crab, limiting the exemption to shore plants is unlikely to provide any competitive advantage to one plant or processor over another. Extending the exemption to floating processors could increase competition. Limiting this extension to floaters operating at docks or docking facilities would reduce that competition to some extent, but not substantially.

Processing in the Eastern Aleutian Islands golden king crab and the Western Aleutian Islands red king crab fisheries takes place almost exclusively in Dutch Harbor. In the Eastern Aleutian Islands golden king crab fishery, most processing takes place in the early fall, preceding or early in the Bristol Bay red king crab season. The Western Aleutian Islands red king crab fishery was historically prosecuted in the late fall, opening after the Bristol Bay red king crab fishery. Under the rationalization program, it could be prosecuted simultaneously with Bristol Bay red king crab. Applying the exemption to these fisheries is likely to provide some processor efficiency by reducing the number of plants that must maintain crab lines during these seasons and coordinate landings with harvesters. The processor benefit arising from the exemption is likely to be substantially less than the exemption will provide in other fisheries where substantial processing takes place in more remote regions. It is likely that most plants receiving deliveries from these fisheries will be multispecies plants that maintain crews throughout the seasons for these fisheries regardless of whether consolidation is permitted under this action. Efficiencies might still be realized by reducing the number of crew that need to be on hand for deliveries and through other operational efficiencies arising from specializing operations within a plant. Limiting consolidation by applying the option to cap processing at a single plant at 60 percent of the IPQ in the fishery would still allow for some processor benefit from consolidation, while limiting the potential for processing to be consolidated in a single facility.

Fifty percent of the Western Aleutian Islands golden king crab fishery IPQ allocation is required to be landed in the West region; the remainder may be landed anywhere. The number of days between the first and last landing in the fishery fluctuated greatly in the first two years of the program. Even with a relatively short period of landings of 80 days, the average landing poundage per day is less than 40,000 pounds. If only the West region IPQ are landed in the West during this period, the daily landings will average less than 20,000 pounds. Applying the exemption in the West could be beneficial to holders of West IPQ by allowing efficiencies to be realized at a single plant. As with other remote region processing, allowing consolidation in a single facility could reduce capital and crew related cost that arise from requiring multiple plants to operate to fully process the IPQ allocation.

If the exemption is limited to shore plants, the Adak shore plant (the only crab processing plant currently processing in the region) will be provided a competitive advantage over other plants. Extending the exemption to floating processors would increase competition among facilities. Limiting the exemption to floating processors at docks or docking facilities could increase processing to some extent. Extending the exemption to processing of all IPQ in the fishery could provide minor additional efficiency benefits to IPQ holders by

allowing consolidation of any processing outside of the West in a single facility. Most likely any such processing would be in a shore plant in Dutch Harbor, where most of the processing in the fishery has historically taken place. The extension of the exemption to floating processors (or floating processors at docks or docking facilities) is unlikely to affect the level of competition.

#### **Effects of the custom processing exemption on harvesters**

The effects of this action on harvesters are likely to be limited. In some cases, harvester operational efficiency could be improved, if processing is consolidated in a single location that has access to goods and services that might be desirable during the season. Harvester operational efficiency could suffer, if a single processor is unable to receive and process landings in a timely manner. This effect, however, is not likely except possibly in the Bering Sea *C. opilio* fishery, since the other fisheries have typically had relatively small TACs. In those smaller fisheries, harvester consolidation is likely to spread landings over time, limiting the potential for landings to overwhelm a processor. Additional harvester efficiencies could be realized in the Western Aleutian Islands golden king crab fishery, if processors choose to move their processing of Undesignated shares to the West region, closer to fishing grounds in that fishery. This consolidation will occur, only if processors are able to process landings in the West at the same or lower cost as in ports outside of the West region. In addition to harvester operational efficiency, the Council has suggested that this action should address two other harvester concerns – inseason contingencies and harvesting of the full TAC.

In certain instances, allowing a processor to exceed the share use cap through custom processing could address inseason contingencies (such as breakdown of a processing plant). For example, if one of two plants operating in a fishery subject to the exemption were to breakdown, all processing scheduled for the plant suffering the breakdown could be consolidated into the other plant, regardless of whether the plant would exceed the 30 percent cap. It is important to bear in mind that the exemption proposed in this action would be irrelevant, if the remaining processor is not at or over the cap. In addition, processors may be able to juggle deliveries between facilities with both remaining within the cap, if one plant is disabled temporarily. The exemption is important to addressing the contingency, only if consolidation of the processing in a single plant is beneficial to addressing the contingency and that consolidation would exceed the cap.

The custom processing exemption is likely to be most useful for addressing contingencies in circumstances where participants are not using the exemption but for the contingency. In most fisheries and regions, if processing is consolidated beyond the 30 percent cap through custom processing, few opportunities to further consolidate are likely to exist, limiting the effectiveness of the exemption in quickly addressing contingencies. In both the Bering Sea *C. opilio* fishery and the Western Aleutian Islands golden king crab fisheries, application of the cap without the exemption requires only two plants to operate. Consolidation beyond the 30 percent cap under the exemption is likely to lead to processing being consolidated in a single plant. In the case of a contingency arising, the exemption is likely to help most, if processors have not previously chosen to consolidate their processing to a single plant. In that circumstance, two plants are likely to have been operating in the fishery or region, allowing concentration of landings at one of the plants. Despite this limitation, the exemption could provide flexibility to address contingencies through use of floating or shore plants.

The potential for this action to affect harvest of the full TAC is limited and difficult to discern. The only fishery affected by this action in which participants have failed to fully harvest the TAC is the Western Aleutian Islands golden king crab fishery. Harvesters took the full TAC in that fishery in the first season of the program, but only slightly more than 80 percent of that TAC in the second season of the program. Exemption of custom processing from use caps would likely have had no affect on this failure to harvest the TAC (or any future failure to harvest the TAC). It is believed that the weak market for golden king crab together with the relatively high cost of processing in the West region led to failure to fully harvest the Western Aleutian Islands golden king crab TAC. It is also believed that harvester who left the largest number of shares unharvested failed to timely commit those shares to and eligible IPQ holder to be eligible for arbitration. Had the harvester followed the timeline for matching shares and arbitration, the TAC might have been fully harvested.

Under the current rules governing IFQ/IPQ share matching and arbitration in the fisheries, holders of A shares are permitted to unilaterally commit A share IFQ to IPQ holders and establish a price through the arbitration system. The only circumstance in which a custom processing exemption from IPQ share caps could affect harvest of the TAC would be, if a harvester were to perceive that the arbitration system is capable of creating a higher ex vessel price based on sharing of processing efficiencies arising from the exemption with harvesters and if the ex vessel price created in the absence of the exemption is not high enough to justify fishing. In addition, the increase in the price determined by the arbitration with custom processing exempt from the use cap would need to be high enough to justify fishing. The potential for these circumstances to arise is not known.

#### **Effects of the custom processing exemption on communities**

The effects of this action on communities and community sustainability vary by region and fishery and depend on the specific options selected by the Council. In considering the effects of the action, it is important to distinguish effects arising out of the action – the exemption of custom processing from the processing share cap – from effects that would arise independent of the action. Under the current caps, in which custom processing counts against the cap of the processing plant owner, custom processing arrangements have facilitated the movement of shares among plants. The effect of this action is limited to the contribution of the exemption to that consolidation.

The effect of this action on communities will be determined by the extent to which the exemption would facilitate the movement of shares to, away from, or among communities. The potential for the action to result in the movement to or away from communities depends on the options selected by the Council. Specifically, if the Council chooses to limit the exemption to either shore plants or floating processors at docks or docking facilities, the action will clearly not facilitate the movement of shares away from communities. Under either of these options, it is not clear that the action will contribute to the movement of shares to communities. If the action limits the exemption to shore plants, and consolidation of processing under custom processing arrangements at shore plants does not offer benefits to processors beyond those attainable at less consolidated floating processors outside of communities, it is likely that the exemption will have no effect on the geographic distribution of processing. Similarly, if applicable to both shore plants and floating processors docked or at docking facilities, the exemption will only have an effect, if the consolidation under the exemption is of greater benefit to IPQ holders than less consolidated operations outside of communities. Considering only the potential for consolidation of processing within communities, it would appear that extending the exemption to floating processors docked or at docking facilities increases the potential for processing to be located in communities under the exemption. Qualifying docked floating processors will increase the potential for a community based processor to be more efficient than a less consolidated operation outside of a community by simply qualifying more community based operations for the exemption.

In the Bering Sea *C. opilio* fishery, the exemption of custom processing is limited to shore plants and floating processors “moored in the harbor” by the Magnuson Stevens Act reauthorization. Currently, the only option defining platforms eligible for the exemption that meets that definition would limit the exemption to shore plants and floating processors at docks or docking facilities in a city. Under this option, the shore plant in St. Paul and floating processors in St. George and St. Paul would qualify for the exemption. The current trend is that processing has moved from St. George to St. Paul. A substantial number of IPQ holders have elected to move their processing to floating processors. While the exemption might appear to further facilitate this movement of processing from St. George, it is not clear that the exemption will effect that migration. On the other hand, the exemption could bring a benefit to St. Paul, if it requires the custom processing to be conducted at a shore plant or a docked floating processor to qualify for the exemption. This influx of activity and workers could bring additional economic activity to the community, which would otherwise be lost to other locations in or outside of Alaska.

The St. Matthew Island and Pribilof fisheries have been closed for several years. In the North region, shares in these fisheries are linked only to St. Paul by the ‘cooling off’ provision and right of first refusal. Since most



North shares in the Pribilof fishery were historically processed in St. Paul, application of the exemption to the North region is unlikely to facilitate the movement of shares into St. Paul; however, granting the exemption to floating processors regardless of their location could facilitate the movement of shares away from St. Paul. If the exemption is granted only to custom processing by shore plants or docked floating processors, the exemption would not facilitate movement of shares outside of communities, but at some point could be used to move processing from St. Paul to another community (such as St. George), if a processor believed that greater efficiencies could be realized in that other community. In the St. Matthew Island fishery, most processing in the North has occurred outside of any community. Approximately 10 percent of the qualified historic processing occurred in St. Paul. Granting the exemption to shore plants or docked floating processors could facilitate the movement of processing into communities, if processors believe that consolidation will provide economic benefits. Currently, consolidation is most likely to occur in St. Paul, but in the long run, another community (such as St. George) could be a more attractive location for the consolidation of processing. If the exemption is granted to any floating processor, consolidation could draw historic processing from St. Paul reducing benefits to St. Paul and communities in general.

Granting the exemption in the South region for the St. Matthew Island and Pribilof fisheries is unlikely to have much effect on communities. Less than 35 percent of qualified historic processor occurred in the South in these two fisheries. Several processors participated, who have facilities in several locations. Since the cap is unlikely to bind in the South, and many facilities are available for processing, it is unlikely that the cap exemption is necessary for consolidation.

In the Western Aleutian Island red king crab fishery, processor shares are not subject to the 'cooling off' provision, rights of first refusal, or regional landing requirements. Processor shares are currently held by several processors, with most shares held by processors with Dutch Harbor plants. The fishery has been closed in most recent years. If the exemption is granted in this fishery, it is possible that processing could either consolidate in Dutch Harbor or move out of Dutch Harbor, most likely closer to the fishing grounds west of Dutch Harbor. If the exemption is limited to shore plants and docked floating processors, movement out of Dutch Harbor is likely to be to a community closer to the fishing grounds in the west, such as Adak or Atka. If the exemption is granted to any floating processor, it is possible that no community would benefit from consolidation beyond the cap. The exemption in this fishery and the Western Aleutian Islands golden king crab fishery could interact, contributing to consolidation of processing from both fisheries in a single plant west of Dutch Harbor nearer to the grounds for the two fisheries, if this fishery opens. Since processors are required to process 50 percent of the Western Aleutian Islands golden king crab in the West region (which does not include Dutch Harbor), if processor efficiencies can be gained by consolidation of processing from both fisheries in that region, it might be undertaken. Consolidation in the West could be stimulated, if harvesters are willing to share a portion of the efficiencies they realize by not needing to travel to deliver in Dutch Harbor. If the exemption is granted to any floating processor, it is possible that no community would realize any benefit of the consolidation of processing in excess of the cap.

Almost all qualified historic processing in the Eastern Aleutian Islands golden king crab fishery occurred in Dutch Harbor. Granting the exemption in this fishery is unlikely to have any community effects since the fishery is prosecuted relatively close to Dutch Harbor and most processor share holders operate shore plants in that community. If the cap is extended to any floating processor, it is possible that consolidation could occur on a floating processor outside of the community.

The Western Aleutian Islands golden king crab is not subject to the 'cooling off' provision or the right of first refusal. The fishery is subject to regional landing requirements, under which 50 percent of the IPQ are required to be landed in the West region, with the remainder free to be landed in any location. Extension of the exemption to this fishery could lead to consolidation of processing, particularly in the West region. If limited to shore plants consolidation could currently occur only in Adak. Extending the exemption to docked floating processors could make consolidation more likely increasing competition, providing increased options to processing share holders to achieve benefits needed to stimulate that consolidation. Limiting the exemption to

shore plants and docked floating processors would ensure that benefits are realized by a community. If the exemption is granted to any floating processor, it is possible that the consolidation would move shares from communities that currently process landings in the fishery. If the exemption is granted to any processing in the West region (including processing of undesignated shares), it could attract processing to the West region from locations outside of the West, primarily Dutch Harbor. For this to occur, processor share holders would need to perceive a benefit from this consolidation. It is possible that harvesters could share some of their operational efficiency benefits with processors (i.e., accept a lower price) to save on costs of travel from the fishing grounds to Dutch Harbor. If the exemption is granted to shore plants only outside of the West region, it could contribute to the consolidation of processing of regionally undesignated shares in Dutch Harbor. Granting the exemption to docked floating processors is unlikely to have any additional effects, since most of the processing share holders operate facilities in Dutch Harbor. If the cap is extended to any floating processor, it is possible that consolidation could occur on a floating processor outside of the community.

#### Exemption of custom processing in the community of origin

The second part of this action would extend cap exemption to custom processing that occurs in the community of origin after the transfer of processing shares from the initial recipient of those shares. Under the first option, the exemption would apply only if the shares are transferred to the entity that holds the right of first refusal on behalf of the community of origin. Under the second option, the exemption would apply to custom processing of the shares in the community regardless of the holder of the processing shares.

Granting the cap exemption to custom processing could facilitate improvements in processing efficiency, particularly if a community entity is committed to maintaining processing of its holdings in the community of origin. If the entity would be compelled to open a new, second facility in a community because custom processing at an existing plant would not comply with the cap, it is clear that the cost of processing would increase. Likewise, if the exemption is granted to entities other than the community entity, it is possible that some efficiency gain could occur for a share holder that wishes to comply with a commitment to process in the community of origin under the right of first refusal. The effects of this action will differ across processors. Since the exemption is irrelevant, if a processor does not exceed the 30 percent processing cap, only large processors in a fishery are likely to derive a benefit from the proposed exemption.

The effects of this action on harvesters are likely to be very limited. Although the action would exempt some processing from the current cap, the exemption is likely to have limited applicability and be used infrequently. Harvester operational efficiency could be improved or impaired, depending on the circumstances. If the processing location requires additional travel or has fewer goods and services available, harvesters could lose efficiency. If processing is concentrated in an advantageous location, harvesters could realize a benefit from processing concentration under this action. In any case, the effects on harvesters are likely to be limited since the exemption is unlikely to apply to many circumstances.

The effects of this action on communities are likely to be limited and differ across communities. Communities that seek to retain historic processing could benefit from processors being permitted to process in excess of the cap under the exemption. Although some communities could benefit from retention of crab processing, others are likely to be frustrated to the extent that this action prevents the development of additional processing activity. The specific effects of exemption created by this action on the distribution of processing are uncertain and largely depends on the actions of processors in the fisheries.

The two different options under consideration could have different effects on different communities. Under the first option, a community entity would be required to hold shares for the exemption to apply. This option could be cost prohibitive for some community entities, which have limited resources to acquire shares. Under the second option, the exemption would apply to processing in the community of origin, regardless of the holder of the shares. This provision may help a community retain shares that the community entity could not afford to purchase, by allowing others to use the exemption. Under this provision, however, the nexus between the share holdings and the community is much weaker than when those shares are held by the community entity.

Since the exemption defined by this action is unlikely to be used extensively, its effect on management and enforcement will be limited. The management burden of the different provisions will differ slightly under the two options. Under the first option, the exemption will apply only to shares held by a community entity. Administration of the provision will be simplified, since any time the shares are held by a community entity, the physical processing of the shares will not affect compliance with the share cap. Under the second option, monitoring the cap will be slightly more complicated. The exemption will apply to any processing of the shares in the community of origin, after the shares have been transferred from the initial recipient of the shares. This provision will require administrators to track share holdings of any entity after their first transfer and disregard any processing of the shares in the community of origin. Administration of this provision will require administrators to monitor the processing of shares in the community of origin, regardless of the share holder, for purposes of applying the exemption. Although the provision is relatively straight forward to apply, the tracking of shares is more complicated than under the first option. Since neither of the options is anticipated to have broad applicability, the administrative burden under either is anticipated to be minimal.

**MICHAEL A. D. STANLEY****ATTORNEY AT LAW**

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September 26, 2007

North Pacific Fishery Management Council  
605 W. 4<sup>th</sup> Avenue, Suite 306  
Anchorage, Alaska 99501-2252

Sent via Facsimile Only

Re: Proposed Exemption of Custom Processing from Processor Use Caps

Dear Council Members:

I am writing on behalf of Alaska Trojan Fisheries (ATF), a member of the Bering Sea Cooperative, to address two subjects: (1) the proposed exemption of custom processing from use caps on processor shares, an item on your agenda for the upcoming meeting; and (2) a request that for the season currently underway, the Council encourage NOAA Fisheries to waive and not enforce the requirement that half of the quota in the Western Aleutian Islands golden king crab (WAG) fishery be delivered west of 174 ° W. longitude, in order to avoid the problem that occurred last season when approximately 400,000 pounds of west-designated IFQ went unharvested due to the lack of available processors in the West region.

**The 2007-2008 Season**

Regardless of what action the Council takes on the proposal to exempt custom processing from use caps on processor shares, regulations to implement such an exemption will not be in place this season. Yet ATF confronts the same situation as last year -- the holders of processor quota share for the WAG fishery appear unwilling to provide platforms for processing of crab that must be delivered in the West region. As a result, once ATF completes harvesting the cooperative's undesignated IFQ, it will have to cease operations and, like last year, leave a substantial portion of the TAC unharvested. This loss of available harvest is not consistent with the goals of the management plan or the Magnuson-Stevens Act.

Last October, ATF requested NOAA Fisheries and its enforcement division to consider waiving the west delivery requirement. The agency declined this request and suggested that we bring the issue to the Council. That has been done. While we have some reservations about the proposed solution, discussed below, we appreciate the Council's recognition that there is a problem in the WAG fishery. An immediate question is what to do about the problem this year.

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We urge the Council to request NOAA Fisheries to waive and not enforce the delivery requirement for west-designated IFQ this season. Such a request from the Council would not constitute a plan amendment or regulatory proposal, but would simply call upon NOAA to exercise its management and enforcement discretion to avoid a repeat of the loss of harvest opportunity that occurred in the WAG fishery last year.

#### **Exemption for Custom Processing**

ATF is skeptical that exempting custom processing from use caps will solve the problem in the WAG fishery. As recognized in the RIR/IRFA for the proposal, the WAG fishery is characterized by a lengthy season, a relatively small TAC, a small number of IFQ holders, an even smaller number of vessels that actually fish (so small that catch data cannot be revealed due to confidentiality restrictions, *see* RIR/IRFA at 7), a small number of PQS holders, and only one shore plant in the West region, on Adak. The theory of the proposal to exempt custom processing from use caps assumes that consolidation of deliveries to fewer plants and processing vessels will lead to more efficient processing and thus provide incentive for PQS holders to operate in the West region. However, as recognized in the RIR/IRFA (at 28), the potential for consolidation will not be realized unless PQS holders and potential custom processors – primarily, the plant on Adak – are able to come to agreement on the terms for custom processing, including price. Recent experience does not encourage us in the belief that this will likely happen.

Nor do we understand how this proposal will fit with the arbitration system. Arbitration is designed to resolve price disputes between IFQ and IPQ holders, not disputes regarding custom processing agreements, including the price the IPQ holders must pay to have their crab custom processed. The arbitrator cannot force a custom processor to offer a competitive price to the IPQ holder nor order the custom processor to commit to processing crab for the entire season. How can an IPQ holder craft a last best offer for an arbitrator to consider if the IPQ holder is not able to secure a firm agreement with a custom processor to handle west-designated crab for an entire season? We see nothing in the RIR/IRFA that addresses this problem.

ATF supports processing of WAG crab on Adak. Prior to rationalization, ATF operated one of the few active catcher vessels in the West region and delivered most of its crab to Adak. It's much more efficient to deliver crab to Adak than sail back to Dutch Harbor. If all of the WAG IFQ were B shares, an idea that was floated last spring and which ATF supported, we would expect a similar result – most of the crab would go to Adak. But if the plant there is unable or unwilling to handle crab, either on its own or in a custom processing arrangement, then there needs to be a mechanism that will allow IFQ holders to deliver their crab wherever they can find a market. The alternative is simply to let the west-designated crab go unharvested, which does not make any sense at all.

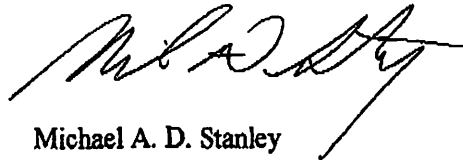
Despite these reservations about the proposal, if the Council intends to move forward with it, we encourage adoption of options that provide the greatest flexibility for custom processing to occur. These include applying the exemption to all WAG crab, not

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just in the West region; option 1 for the definition of custom processing (physical processing of crab does not count against an entity's cap); and option 3 for locations (any shore plant or floating processor).


Thank you for considering this comment.

Sincerely,



Michael A. D. Stanley

Cc: Alaska Trojan Fisheries

	<p>Corporate Offices        800 E. Dimond Blvd., Suite 3-400        Anchorage, AK 99515-2043        Phone: 907-561-3400        Fax: 907-561-3401</p>
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September 26<sup>th</sup>, 2007  
**RECEIVED**  
 SEP 23 2007  
 N.P.F.M.C.

Chris Oliver  
 Executive Director  
 North Pacific Fishery Management Council  
 605 W 4<sup>th</sup> Ave Suite 306  
 Anchorage, Alaska 99501

Re: Custom Processing RIR/IRFA and Crab 18 month review

Dear Chris and Council members,

Our comments are directed to the Custom Processing Use Cap Exemption analysis, however it is impossible to entirely separate this issue from the 18 month review. We apologize in advance for the length of this letter, but the impacts of Crab Rationalization are a huge issue for Adak and we ask you to consider our comments carefully.

The draft RIR/IRFA generally does a good job on laying out issue surrounding custom processing exemption.

There are several areas we wish to address in our comments:

- New LAPP standards
- Confidentiality
- Excessive Shares
- Sideboards
- Who Benefits from Competition to Custom Process?
- Anti-trust Considerations
- Preferred Option

Before addressing the above list of issues, we want to focus on one point that is critically important.

On page 31 the RIR/IRFA presents a discussion of why harvesters left 427,814 lbs out of 568,432 lbs of A share of west region WAG crab un-harvested last season. This is correctly characterized as 80% of the TAC being harvested (when CP shares and non-

west region shares are included). However it is equally true that this represents 75% of the west region A shares that were left in the water.

The author speculates: "It is believed that the weak market for golden king crab together with the relatively high cost of processing in the West region led to the failure to fully harvest the Western Aleutian Islands golden king crab TAC."

While it is true the market was weak, and processing cost are higher in the west region, this is NOT the primary reason WAG crab went un-harvested.

It is important to note that the Adak community quota was harvested and processing in the Adak, despite the weak market and the higher costs, after the community agreed not to charge a royalty if the crab were delivered to Adak. Adak Fisheries paid \$1.75/lb last season, almost exactly the same as the average price for the WAG fishery as a whole (including Dutch Harbor) as shown in table 12.

It is even more significant that one major IPQ holder did harvest their entire west region WAG IPQ after their matched IPQ holder transferred its IPQ to Adak with no royalty.

What prevented 75% of the west region WAG crab from being harvested was the PQS system that adds an additional royalty cost into the equation in order for processing to occur in the west region in the face of the thin margins.

While a custom processing exemption in the west has the potential to bring more crab processing activity to Adak which will benefit the community, and to increase the likelihood of that the TAC can be harvested, it is only a band-aid that doesn't address the underlying problem of IPQs in the Aleutian Island king crab fisheries.

#### LAPP Standards Under the MSA

Crab Rationalization is a LAPP program as defined under the re-authorized MSA, though the new standards would not allow the creation of PQS within a LAPP program. While the Act does not require the Council to retroactively meet the new standards, neither does it prohibit the Council from doing so.

Section 303 A(c)(5) of the new MSA strengthens the requirements to consider current and historical harvests; employment in the harvesting and processing sectors; investments in, and dependence upon, the fishery; and the current and historical participation of fishing communities.

It also strengthens requirements to deal with excessive shares by establishing any other limitations or measures necessary to prevent an inequitable concentration of limited access privileges.

Adak was harmed by Crab Rationalization precisely because current participation by our community was not presented in the original EIS. Nor did were meaningful



measures adopted that prevented extreme concentration of limited access privileges for processing WAG crab.

#### Confidentiality.

Good decision making requires transparency. Confidentiality rules may not obscure an analysis involving large numbers of stakeholders, but in fishery sectors with small numbers of players, it means the Council is forced to make decisions in the dark.

Confidentiality rules intended to "protect" us have had instead had devastating impacts on us. The fact that Adak processed virtually all of the CV WAG crab harvests between 1999 and final action on the Crab Rationalization program was never presented in the EIS analysis. We don't believe the previous Council would have chosen the options it did for Aleutian Island crab if it had full information before it at the time.

We are concerned that confidentiality continues to be a problem in this EA. At least 8 times in the analysis it states information can not be presented due to confidentiality. Adak Fisheries has repeatedly offered to waive confidentiality, so that the Council can fully appreciate how dependent our company and community were on crab until the program was implemented and what it has done.

Attached to this letter are table with some of our data. We invite NMFS to confirm the accuracy or provide corrected data. Detailed supporting spreadsheets have been provided to staff for verification, and are available to the Council.

#### Excessive shares

The Council that created the Crab Rationalization program set an excessive share cap on ownership and use at 30% of the IPQ. Due to confidentiality, it had no way to know that it was allocating double the cap or 62% of the IPQ to one company (Westward).

After the fact, this information on PQS holdings in not confidential, but ironically, IPQ use is still confidential. Table 7 presents maximum PQS holdings, and is accurate. However, since the table was prepared, one WAG PQS holder chose not to apply for WAG IPQ this year. The result is there was a pro-rata reallocation of IPQ, 90% of which went to Westward. So, now one company owns 90%, or three times the excessive share cap, of WAG IPQ.

This outcome is totally inconsistent with the whole concept of excessive share caps.

**If 90% of a limited access privilege isn't excessive, what is?**

#### .Sideboards

Since the AFA, each rationalization program has had sideboards on harvesters who were allowed to consolidate there operations, so that the excess harvest capital from a

rationalized fishery was not allowed to show up in someone else's backyard to exacerbate the race for fish in an un-rationalized fishery.

Crab Rationalization did have sideboard provisions restricting the use of excess harvest capital. It does NOT have provisions restricting the use of excess processing capital, even though the creation of PQS allowed for massive consolidation in the processing sector.

The one un-rationalized fishery in the BSAI is cod, and with the loss of crab Adak is extremely dependent on cod. As a result our cod fishery is very vulnerable to excess processing capital from PQS holders.

We support shorebased processing of Alaska's crab and cod resources. If the northern region opilio custom processing exemption results in companies with floaters leasing their IPQ to a shore plant in St. Paul, that is a good thing for that community and should be encouraged.

At the same time we are very concerned about where that excess steel ends up. If consolidation means those floating processors end up in the Aleutian Islands processing cod, the net benefits to remote Alaskan communities are eroded.

We believe that the Council should consider sideboards the cod fishery on both the PQS holders and the floating processing vessels that previously processed northern region opilio if they consolidate their IPQ use through custom processing or otherwise.

#### Benefits of Competition to Custom Process

The problem statement includes a sentence that states: *"This efficiency increase could improve competition in processing."* On page 25, there is a statement that *"Compelling the development of additional shore facilities to induce competition would seem inappropriate and inconsistent with the some of the stated rationales for the exemption."*

One comment we'd offer is that nothing in the option restricting the exemption to shore plants *"compels the development of additional shore facilities."* PQS owners would remain free to process their IPQ allocations themselves, or the contract with multiple custom processors up to the existing caps.

Our main concern is that there not be confusion about who benefits from *"competition"* to custom process. As a custom processor we are basically competing to provide contract labour to a PQS owner. We never own the product, we can't pass our efficiency gains on to the consumer or to the harvester.

The only real beneficiary of competition to be the low cost service provider to the PQS owner is the PQS owner. The buck stops there.

### PQ holder benefit

Section 2.4.5 discusses the effects on the processing sector. This discussion would benefit from a clear distinction between PQS owner and facility owners.

Page 28 paragraph 2, states "large processors in a fishery are the primary beneficiaries." This is true as it applies to the PQS owner who owns the crab being custom processed, not to the custom processing facility that may be a small player in the crab market even though they process a large percent of the quota.

Page 30 paragraph 2, states "Adak will be provided a competitive advantage over other plants" if the option is to apply the exemption to shore plants only. This is true relative to other plants, however, that competitive advantage is nothing compared to the competitive advantage created by owning the vast majority of the IPQ.

As the analysis makes clear the main benefit of a custom processing exemption ultimately flows to the PQS owner, because they will only allow us to custom process their quota if we can do it cheaper than they can.

### Community benefit

If custom processing does take place in the western region, as the analysis states the community benefits are clearly greater from a shore plant with resident employees than from a floater, particularly one that isn't tied into city utilities and paying city taxes and whose employees aren't able to walk ashore to patronize local businesses.

### Harvester benefit

The current requirement for two platforms to operate in the west region has meant that it is too costly to send a floater out for 350,000 lbs of crab. The one benefit to the harvester from a custom processing use cap exemption is that there is a better chance that they can deliver all of their WAG IFQ crab.

Harvester benefits are limited under a custom processing exemption. There is no guarantee that the PQS owner will pass the savings on to the harvester. In fact, on page 34, the analysis suggests that the PQS owner may expect the harvester to accept a lower price and pass on part of the cost savings of not having to travel the extra 400 miles to Dutch Harbor to the PQS owner.

### Anti-trust considerations

The analysis, doesn't fully explore the implications of the choice definition of "custom processing." However, the second option appears really to facilitate Processing Coops rather than custom processing.

Appendix B appears to touch these concerns. The analysis should look a deeper into the anti-trust implications of custom processing processor cooperatives.

We are also concerned that we could be dragged into a legal swamp where we are at risk of anti-trust violations, just by trying to negotiate a custom processing contract with a fellow IPQ holder.

For example, we were offered a formula price custom processing contract this season by Westward. It offered a base price that is less than the actual cost of processing in the western region, supplemented by an amount to be determined based on two variables:

- 1) the ex-vessel price
- 2) the wholesale price of the product

It would be foolhardy for Adak Fisheries to accept the offer, unless we have some reasonable idea of what the values of the two variables are.

The catch is that both Westward and Adak Fisheries are IPQ holders for the same species of crab. The whole binding arbitration system is structured to make sure IPQ holders don't exchange ex-vessel and wholesale price information.

On the one hand we look like jerks if we are seen as not facilitating the fleet's ability to deliver its WAG IPQ. On the other we would be chumps if we ended up processing for the flat rate below our costs. But in any case, we don't want to end up facing an anti-trust violation because we discussed ex-vessel and wholesale price information with a competitor.

#### Preferred Option

The real fix is to get rid of PQS for all AI king crab delivered west of 174, and to maintain regional landing requirements.

NMFS has to do an implementation analysis of the custom processing use cap exemption for the north region opilio, and the Council is poised to take final action in December.

Therefore, we support short term band-aid fix that has the net effect of grandfathering our ability to process as much crab as we were processing during the period when the Council designed and NMFS implemented this program.

This could be achieved by either by simply explicitly grandfathering in our facility, or by a combination of the options and elements to allow an exemption from the use cap for custom processing (definition option 1) in the west region only for the three species of Aleutian Island king crab

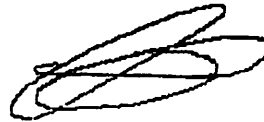
Conclusion

We look forward to the completion of the 18 month review process and hope that this Council will chose to make significant modification to the Crab Rationalization program as it applies to the Aleutian Island king crab fisheries that truly recognize the dependence Adak had on crab when the program was being created.

In the interim we appreciate anything that results in more crab flowing through Adak, and if the use cap exemption will do that we support moving ahead to final action in December.

Thank you for considering our comments on as issue of great importance to our company and community.

Sincerely,



dave fraser  
Adak Fisheries

Summary table of Adak Crab processing history between opening of Adak to commercial activity and implementation of the Crab Plan.

WAG brown crab	Processing in Adak
Quota Year	best available data
1999/00	1,040,532
2000/01	1,270,458
2001/02	1,858,199
2002/03	1,606,635
2003/04	2,064,180
2004/05	1,808,723

Summary table of Adak processing history of EAG brown crab and Petrel RKC.

EAG brown crab		
2002	2003	2004
70,233	177,650	412,492

Petrel RKC		
2001	2002	2003
126,648	154,625	117,822

A full spreadsheet of supporting fish ticket data has been provided to Council staff.

Adak Fisheries LLC  
100 Supply Road, Adak, Alaska 99546 USA Tel 907 592 4366 Fax 907 592 4241  
Email Adak@adakfisheries.com

Under Crab Rationalization the sum of all the CV shares in the AI WAG brown crab fishery is only 1,305,842 lbs. In every year between 2000 and implementations of Crab Rationalization, Adak was processing more than what is now the entire CV allocation.

**Data the Council didn't have for final action on the Crab Plan:**

<b>Average % of Western Aleutian Golden King (WAG) Crab GHL Processed by Adak Fisheries in the Five Seasons Prior to Final Council Action on Crab Rationalization</b>	<b>55% of GHL (including CP harvest) this represents about 90% of CV harvest</b>
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<b>% of the WAG GHL for which Adak Fisheries Received Allocation of PQ</b>	<b>2.30%</b>
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<b>Adak Fisheries WAG 2006 PQ Allocation</b>	<b>61,732 Lbs</b>
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<b>PQ Use Cap for WAG Crab</b>	<b>342,234 Lbs</b>
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<b>Maximum Custom Processing of WAG PQ Possible by Adak Fisheries</b>	<b>280,502 Lbs</b>
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<b>Companies Holding More Aggregate Crab (all crab species) PQs than the WAG PQ use cap</b>	<b>Amount of Aggregate Crab PQs Holdings</b>
TRIDENT SEAFOODS CORPORATION	10,529,552
PETER PAN SEAFOODS, INC.	6,997,702
WESTWARD SEAFOODS, INC.	5,362,349
UNISEA, INC.	4,972,273
ICICLE SEAFOODS, INC.	4,827,401
ARCTIC SEA HOLDINGS, INC.	3,523,134
ALYESKA SEAFOODS, INC.	2,390,078
SNOPAC PRODUCTS, INC.	1,824,866
YARDARM KNOT, INC.	1,724,185
ROYAL ALEUTIAN SEAFOODS, INC.	1,334,189
NORQUEST SEAFOODS, INC.	954,400
OCEAN BEAUTY SEAFOOD, INC.	566,608

<b>Number of Companies That Hold More Than 342,234 lbs of PQ by Fishery</b>	<b>Top Amount of PQ Lbs by Fishery</b>
Bristol Bay Red King Crab - 9	3,182,985
Bering Sea Snow Crab - South - 9	2,589,849
Bering Sea Snow Crab - North - 9	4,135,816
Bering Sea Tanner Crab - 2	576,004
Eastern Aleutian Golden King Crab - 2	1,029,931
Western Aleutian Golden King Crab -- 1	718,416



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September 28, 2007

Mr. Chris Oliver  
Executive Director  
North Pacific Fishery Management Council  
605 West 4<sup>th</sup> Avenue, Suite 306  
Anchorage, AK 99501

VIA US EXPRESS MAIL and E-Mail

Ref: Crab Custom Processing RIR/IRFA: West Designated WAG

Dear Chris:

I am writing today to respond specifically to a number of errors and misstatements found in a letter to you dated September 26, 2007 from Adak Fisheries, LLC (ADAK). My remarks will focus specifically on these errors and misstatements. For Westward's views on the subject of crab custom processing caps generally, please rely on the written and oral testimony of Steve Minor and John Iani on behalf of the North Pacific Crab Association, of which we are members.

Having just yesterday received a copy of ADAK's letter I was obviously unable to submit a response to the Council in time to meet the September 26<sup>th</sup> deadline for written comments and instead I have asked Steve to deliver this letter to you during the meeting along with sufficient copies for Council members and staff.

In their introduction ADAK admits to mixing together the on-going 18-month Council review (and its defined scope) with the separate issue of custom processing caps. This allowed them to introduce their hypothesis that problems associated with harvesting all or part of the Western Aleutians Golden crab, West designated (WAG/West) resulted neither from market conditions, high costs nor ADAK's own monopolistic behavior as the sole plant located in the region but rather from:

**"the PQS system that adds an additional royalty cost into the equation in order for processing to occur in the west region in the face of the thin margins."**

Deliberately or inadvertently, ADAK then goes on to defend this hypothesis by standing on its head the reality of crab processing, the crab rationalization system and the facts about their own participation before and after Crab Rationalization, in order to conveniently arrive at the conclusion that the "real fix is to get rid of PQS for all Al crab delivered west of 174, and to maintain regional landing requirements", leaving unsaid of course that this leaves them in the enviable position of having a monopoly on buying all western area king crab.

Mr. Chris Oliver  
 Executive Director  
 North Pacific Fishery Management Council

The following is a look at several of the key assertions offered in support of their hypothesis and its conclusion that they receive a monopoly on Western Area king crab:

Royalties and ex-vessel prices

"It is important to note that the Adak community quota was harvested and processing in the Adak, despite the weak market and the higher costs, after the community agreed not to charge a royalty if the crab were delivered to Adak. Adak Fisheries paid \$1.75/lb last season, almost exactly the same as the average price for the WAG fishery as a whole (including Dutch Harbor) as shown in table 12."

ADAK first proposes that the Adak community quota was processed only because no royalty was charged. Throughout the late fall of 2006 Westward was negotiating to process the Adak Community quota and to pay a royalty for doing so, albeit not the royalty they originally proposed. In November we were asked if we would process their quota with no royalty, and of course, since we were negotiating in good faith to actually pay a royalty, we agreed that we would do so. Apparently the crab was ultimately processed by ADAK without a royalty, but was certainly not a requirement of getting the crab processed.

ADAK then proposes that their having paid \$1.75 ex-vessel is "almost exactly the same as the average price for the WAG fishery as a whole". In fact Westward paid an average of \$1.90 for EAG and WAG, so apparently the \$0.25 (\$0.15 divided by 59% recovery = finished value of the ex-vessel disparity) differential in finished product sales value went to ADAK rather than to the community or the fishermen. The Alaska Department of Revenue "2006 Statewide Average Price List for Crab" notes that the average ex-vessel prices paid for brown king crab were \$1.95 (Dutch Harbor) and \$2.10 (Adak and W. Aleutians) respectively.

Apparently after having received the right to process the community crab for free, ADAK then chose to pay less than market prices to its fishermen, behavior that does not inspire confidence in a firm seeking monopoly control of 3,000,000 pounds of king crab.

F/Y 2006/2007 Un-harvested WAG/West

"While it is true the market was weak, and processing cost are higher in the west region, this is NOT the primary reason WAG crab went un-harvested."

"What prevented 75% of the west region WAG crab from being harvested was the PQS system that adds an additional royalty cost into the equation in order for processing to occur in the west region in the face of the thin margins."

Here ADAK proposes that the PQS system, not poor market conditions, and certainly not their monopolistic position as the sole shore-based custom processor in the region as the root cause for leaving WAG/West uncaught and unprocessed. In Fishing Year (FY) 2005/2006 Westward incurred substantial losses while having our WAG/West custom processed. For FY 2006/2007 ADAK proposed to custom process our WAG/West for a fee of \$1.00 per finished



Mr. Chris Oliver  
Executive Director  
North Pacific Fishery Management Council

pound, by their own admission, \$0.25 - \$0.30 over current industry standards. ADAK suggested that the fee might be lowered if all or a large portion of WAG/West was processed by ADAK, and suggested the various IPQ holders coordinate to increase their custom processing volume. Such coordination, at least amongst the IPQ holders would be illegal. Considering that for our product, such a fee combined with poor market conditions and a difficult cost structure for the fleet would put us out of pocket again, we could not agree.

FY 2007/2008 WAG/West

At page six of their comment, ADAK offers the following remark about a proposal made by Westward:

"For example, we were offered a formula price custom processing contract this season by Westward. It offered a base price that is less than the actual cost of processing in the western region, supplemented by an amount to be determined based on two variables:

- 1) the ex-vessel price
- 2) the wholesale price of the product"

Westward concurs completely with the notion that we bear a responsibility to make our best efforts to ensure that all the WAG TAC is harvested. Consistent with that, for the 2007/2008 season Westward proposed to lease to ADAK its WAG/West IPQ (486,210 pounds) on terms identical to terms under which we are leasing a much smaller amount of EAG. We proposed a royalty equal to 50% of net revenue after all costs were deducted (including a sales commission to Westward of 2.5%), including a processing fee of \$0.75. As you can see from ADAK's comments, they declined. Except for the sales commission, we were proposing to bear all the market risk. From their comments ADAK declined because of market and fish price uncertainty.

"It would be foolhardy for Adak Fisheries to accept the offer, unless we have some reasonable idea of what the values of the two variables are."

An odd response considering that if nothing else is true, market and fish price risk is at the very core of our business. If it costs ADAK more than \$0.75 in direct costs to process crab, then they have a much more fundamental business problem than can be addressed by the Council unless of course they are granted a monopoly, in which case they need not compete for raw material. If ADAK expects to recover a full overhead or indirect cost contribution from brown king crab then they fail to understand the commodity nature of the crab business these days. Westward has never been able to consistently allocate full indirect costs (e.g total indirect costs / pounds processed) to this product line. That has not kept us from paying competitive prices to fishermen or taking the normal market risk.

Of course it is just such a monopoly that ADAK seeks:

"The real fix is to get rid of PQS for all AI king crab delivered west of 174, and to maintain regional landing requirements."

Mr. Chris Oliver  
Executive Director  
North Pacific Fishery Management Council

*Their objection to the current system apparently is that they have to compete. In ADAK's view competition for custom processing-benefits only the PQS owner.*

**"The only real beneficiary of competition to be the low cost service provider to the PQS owner is the PQS owner."**

*In truth, as is supposed to be the case, competition for custom processing will primarily benefit the harvester. As we can see, the current lack of competition for custom processing in the west region has resulted in below market prices being paid to fishermen and the Adak Community forgoing any royalty on its quota. Obviously more competition, not less, is required.*

#### Excessive Shares

*At page 3 of their letter, ADAK opines that:*

*one WAG PQS holder chose not to apply for WAG IPQ this year. The result is there was a pro-rata reallocation of IPQ, 90% of which went to Westward. So, now one company owns 90%, or three times the excessive-share cap, of WAG IPQ.*

*This outcome is totally inconsistent with the whole concept of excessive share caps.*

**If 90% of a limited access privilege isn't excessive, what is?"**

*The hyperbole here is obviously intended and inflammatory. In fact, Westward owns no more of the WAG PQS than it did upon the initial issuance of shares. When Royal Aleutian Seafoods declined to apply for brown crab IPQ, the RAM division simply followed regulatory procedures to ensure that adequate IPQ was issued to match with IFQ "A" shares and provide for the TAC to be harvested.*

#### Conclusion

*Westward, the industry and the former owners of the Adak facility supported the Council's west designation of 50% of WAG during the development of the crab rationalization plan, believing at the time that business arrangements would evolve to insure that all the TAC was harvested. The processing or use caps ultimately applied to the region and ADAK's unwillingness to compete at industry standard levels have now caused harm to harvesters who count on this product. If ADAK insists that the only solution is the establishment of a monopoly in their favor, the Council should act to protect competition for this product by either raising the use cap for this region or removing the west designation.*

*Thank you for your time and consideration of these remarks.*

Sincerely,  
WESTWARD SEAFOODS, INC.

  
F. Gregory Baker  
President

Cod is the only significant un-rationalized federal fishery in the BSAI, and thus the likely dumping ground for excess processing capital resulting from consolidation in the Opilio fishery.

Over 80% of the wholesale value processed in Adak in 2007 has come from P. cod.

Every other rationalized fishery since AFA has incorporated provisions to protect participants in un-rationalized fisheries from excess steel resulting from consolidation.

We request the Council adopt, and NMFS implement, processing sideboards on both the PQS holders and the floating processing vessels that previously processed northern region opilio if they consolidate their IPQ use through custom processing or otherwise.

At a minimum, the sideboard should restrict participation in processing of federally managed P. cod harvested by catcher vessels in the Aleutian Island management area between January 15<sup>th</sup> and March 21<sup>st</sup> of a fishing year.

PSQ for North Region Opilio was initially allocated to 12 recipients. The Crab Plan allowed massive consolidation of processing facilities. The new MSA provision exempting custom processing from the use caps, intensifies the potential for consolidation. The Crab Committee was told only one floater and one shoreplant will operate in St. Paul in the upcoming opilio season.

Initial Recipients of PQS for North Region Opilio - Source NMFS RAM Website							
FISHERY	REGION	QUOTA UNITS	ROFR	HOLDER	CITY	STATE	
BSS	N	154,971,913	ST PAUL	TRIDENT SEAFOODS CORPORATION	SEATTLE	WA	
BSS	N	56,082,037	ST PAUL	ICICLE SEAFOODS, INC.	SEATTLE	WA	
BSS	N	53,950,239	ST PAUL	YARDARM KNOT, INC.	SEATTLE	WA	
BSS	N	47,604,363	ST PAUL	UNISEA, INC.	REDMOND	WA	
BSS	N	34,233,514	ST PAUL	NORQUEST SEAFOODS, INC.	SEATTLE	WA	
BSS	N	17,100,952	ST PAUL	PETER PAN SEAFOODS, INC.	SEATTLE	WA	
BSS	N	56,976,258	ST GEORGE	SNOPAC PRODUCTS, INC.	SEATTLE	WA	
BSS	N	39,810,978	ST GEORGE	PETER PAN SEAFOODS, INC.	SEATTLE	WA	
BSS	N	79,006	UNALASKA	MALEZI SEAFOODS	ALBANY	GA	
BSS	N	6,067,852	None	PETER PAN SEAFOODS, INC.	SEATTLE	WA	
BSS	N	3,532,639	None	BLUE DUTCH, LLC	SEATTLE	WA	
BSS	N	403,398	None	YARDARM KNOT, INC.	SEATTLE	WA	

The period January 15<sup>th</sup> to March 21<sup>st</sup> reflects the opilio season dates from the qualifying years used to allocate PQS.

TABLE 9 TO PART 680.

—INITIAL ISSUANCE OF CRAB PQS BY CRAB QS FISHERY

Bering Sea snow crab (BSS)

3 years of the 3-year period beginning on:

- (1) January 15, 1997 through March 21, 1997;
- (2) January 15, 1998 through March 21, 1998; and
- (3) January 15, 1999 through March 22, 1999.

## Option 2

Adak is more dependent on cod than Dutch Harbor is dependent on pollock.

If the Council believes in protecting shorebased processing in small communities is good for Alaska, then we've asked for some protection for our cod fishery from surplus floating processing capital being dumped in our backyard.

If the Council doesn't believe in protecting shorebased processing in our community, and choses to ignore our prior dependence on brown crab, then at least until NMFS can change the SSL restrictions in the AI, let buy BS pollock.

Either way is fine with us, but be consistent. Don't protect Dutch Harbor and leave Adak to deal with predatory competitors.

The American Fisheries Act authorizes NMFS to allow a new shoreside processor to buy BS pollock upon the recommendation of the Council.

Adak is willing to compete with Dutch Harbor on an even playing field. Therefore we will submit an application to be approved as an AFA authorized shorebased processor under staff tasking for action at the December Council meeting, consistent with the provisions of 679.4(1)(5)(v).

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### *AFA 208(f)(2)*

*Upon recommendation by the North Pacific Council, the Secretary may approve measures to allow catcher vessels eligible under subsection (a) to deliver pollock harvested from the directed fishing allowance under section 206(b)(1) to shoreside processors not eligible under paragraph (1) if the total allowable catch for pollock in the Bering Sea and Aleutian Islands Management Area increases by more than 10 percent above the total allowable catch in such fishery in 1997, or in the event of the actual total loss or constructive total loss of a shoreside processor eligible under paragraph (1)(A).*

The process for approving a shoreside processor to buy BS AFA pollock from AFA inshore catcher vessels was published in the Federal Register Vol. 67, No. 250 Rules and Regulations on Monday, December 30, 2002.

The preamble explains the process as follows:

#### **Approval of Additional AFA Inshore Processors**

Paragraph 208(f)(2) of the AFA provides that:

Upon recommendation by the North Pacific Council, the Secretary may approve measures to allow catcher vessels eligible under subsection (a) to deliver pollock harvested from the directed fishing allowance under section 206(b)(1) to shoreside processors not eligible under paragraph (1) if the total allowable catch for pollock in the Bering Sea and Aleutian Islands Management Area increases by more than 10 percent above the total allowable catch in such fishery in 1997, or in the event of the actual total loss or constructive total loss of a shoreside processor eligible under paragraph (1)(A).

To implement this provision of the AFA, the final rule provides a mechanism for the Council recommend that NMFS issue AFA inshore processor permits to inshore processors that are otherwise ineligible under the AFA. In the event that the BSAI pollock TAC exceeds 1,274,900

mt (10 percent above the 1997 combined BSAI TAC of 1,159,000 mt), or in the event of the actual total loss or constructive loss of an AFA inshore processor, the Council may recommend that an additional inshore processor (or processors) be issued AFA inshore processing permits.

The Council's recommendation to NMFS must identify

- (1) the processor (or processors) that would be issued AFA inshore processing permits,
- (2) the type of AFA inshore processing permit(s) to be issued (restricted or unrestricted), and the duration of any such permit(s).

The Council may recommend any length of duration for permits issued under this provision, from a single fishing season to the duration of the AFA. Or the Council may recommend that any such permits remain valid as long as the criteria that led to their issuance remain in effect (i.e., TAC remains above 1,274,900 mt).

The regulations at 679.4(l)(5)(v) provide the details of the approval process.

(v) Authorization of new AFA inshore processors.

If the Council recommends and NMFS approves a combined BSAI pollock TAC that exceeds 1,274,900 mt for any fishing year, or in the event of the actual total loss or constructive loss of an existing AFA inshore processor, the Council may recommend that an additional inshore processor (or processors) be issued AFA inshore processing permits.

(A) Timing of Council action.

At any time prior to or during a fishing year in which the combined BSAI pollock TAC exceeds 1,274,900 mt, or at any time after the actual total loss or constructive total loss of an existing AFA inshore processor, the Council may, after opportunity for public comment, recommend that an additional inshore processor (or processors) be issued AFA inshore processor permits.

(B) Required elements in Council recommendation.

Any recommendation from the Council to add an additional inshore processor (or processors) must include the following information:

(1) Identification of inshore processor(s).

The Council recommendation must identify by name the inshore processor(s) to which AFA inshore processor permits would be issued;

(2) Type of AFA inshore processor permit(s).

The Council recommendation must specify whether the identified inshore processor(s) should be issued a restricted or unrestricted AFA inshore processor permit.

(3) Duration of permit.

The Council recommendation must specify the recommended duration of the permit. Permit duration may be for any duration from a single fishing season to the duration of section 208 of the AFA. Alternatively, the Council may recommend that the permit be valid as long as the conditions that led to the permit remain in effect. For example, the Council could recommend that a permit issued under this paragraph remain valid as long as the combined annual BSAI pollock TAC remains above 1,274,900 mt. or a lost AFA inshore processor is not reconstructed.

(4) Council procedures.

The Council may establish additional procedures for the review and approval of requests to authorize additional AFA inshore processors. However, such procedures must be consistent with the Magnuson-Stevens Act, the national standards, and other applicable law.

(5) Action by NMFS.

Upon receipt of a recommendation from the Council to authorize additional AFA inshore processors, NMFS may issue an AFA inshore processor permit to the identified inshore processor(s) of the type and duration recommended by the Council, provided the Council has met the requirements identified in paragraphs (l)(5)(v)(B)(1) through (4) of this section, and the owner(s) of the identified inshore processor has submitted a completed application for an AFA inshore processor permit that is subsequently approved.