

## ***Executive summary***

Access to the Bering Sea and Aleutian Island crab fisheries is regulated through the allocation of harvest share privileges (or shares). Holders of long term shares, known as quota shares (QS), receive an annual allocation of individual fishing quota (IFQ), representing a privilege to harvest a certain number of pounds of crab during that year. Under the program, 97 percent of the QS pool was initially allocated to holders of limited entry permits under the previous management program. These QS are known as "owner" QS. Under the management program, these owner QS are transferable to any person who meets a minimum sea time requirement; thereafter, holders of these owner shares may maintain those holdings without any further or continuing qualification. At its December 2011 meeting, after receiving a report reviewing the first 5 years of fishing under the current crab management program, the Council directed staff to analyze alternatives to establish active participation requirements for the acquisition of owner shares and retention of those newly acquired owner shares.<sup>1</sup>

### **Purpose and need statement**

The Council has adopted the following the problem statement for this action:

*The Bering Sea/Aleutian Islands (BSAI) Crab Rationalization Program is a comprehensive approach to rationalize an overcapitalized fishery. Conservation, safety, and efficiency goals have largely been met under the program. Provisions that allow for absentee ownership of crab harvest shares support long-term investment by persons or corporations with little or no involvement in the prosecution of the fisheries and limit the amount of quota available for active participants. This action is intended to ensure that ownership of quota transitions to persons who are actively involved in the prosecution of the fisheries.*

### **Alternatives**

#### **Alternative 1: No action**

No action, status quo.

#### **Alternative 2: Active Participation - Eligibility criteria for purchase of owner shares**

To be eligible to permanently transfer and retain Catcher Vessel Owner or Catcher Processor Owner Quota Shares (QS), the QS holder or an individual that is at least a 10, 20, or 33% (options) share holder when the QS is held by a partnership or corporation must meet one of the following requirements:

- a. hold 5, 10, or 20% (options) ownership of a vessel with participation in a rationalized Bering Sea/Aleutian Islands crab fishery in any of the previous 2 to 4 seasons, or
- b. provide documentation of participation as a captain or crew in a rationalized crab fishery (verified by a signature on a fish ticket or crew members' affidavit) for at least 1, 2, or 4 (options) fishing trips in a rationalized Bering Sea/Aleutian Islands crab fishery in any of the 3 or 4 (options) previous seasons.

### **Analysis of Alternatives**

#### **Status quo**

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<sup>1</sup> As a part of its deliberations in the development of alternatives, the Council specified that the action would not affect existing share holdings, but would apply only to shares acquired after implementation of the action.

Under the status quo, five provisions qualify individuals or entities to acquire owner shares (see Taable ES-10), which require some connection to fishing; however, these liberal rules allow persons with no direct connection to the Bering Sea and Aleutian Islands crab fisheries to acquire owner QS.

**Table ES-1. Eligibility to acquire owner QS.**

Type	Qualification requirement
Individuals and entities	recipient of an initial allocation of QS
Individuals	150 sea time in a U.S. fishery
Entities	owner of 20 percent or more of the entity with 150 days sea time in a U.S. fishery
Community entities	Entities holding rights of first refusal to PQS
CDQ groups.	Any CDQ group

Source: 50 CFR 680.41

Although specific data are not available to fully evaluate the extent to which holders of owner QS have ownership interests in vessels active in the fisheries, a substantial number of vessel owners are known to have considerable QS holdings. In addition, some share of QS holders are actively fishing on crab fishery vessels; however, a number of QS holders, also with substantial holdings, are believed to have no activity in the fisheries through either vessel ownership or as crew. If the current rules governing share acquisition and use are maintained, it is likely that the QS in the fisheries will continue to be held by a mix of persons with and without active participation (through ownership of an active vessel or activity as a crewmember on such a vessel). Although it is possible for persons with no connection to the fisheries (i.e., no vessel ownership or crew experience) to acquire QS, it is likely that most QS purchasers and holders will have some participation (historical or active) as knowledge of the fishery is important to investment decision making. Over time some portion of these QS holders may choose not to continue to maintain that vessel ownership or crewing activity, while maintaining their share holdings.

Private interests that hold QS are likely to be a mix of vessel owners, active crew, and inactive persons. Most persons acquiring QS are likely to either be active in the fisheries at the time of their purchase (through vessel ownership or crewing on a vessel) or already hold shares in the fisheries. Over time, a portion of the active share holders are likely to become inactive, either retiring from crewing or selling their vessel ownership interests to others. Share holders are also likely to cycle out of the fishery, selling their shares to others who either are active in the fishery or already hold shares. CDQ groups are likely to increase their QS holdings by continuing to acquire QS to advance both to advance their community development objectives and further their interests in fisheries in general. As is the case currently, all CDQ groups are very likely to be active through vessel ownership.

Under this cycle of share holdings, most share holders will have reasonably good information concerning fishery operations that will allow them to make reasonable decisions concerning the use of their shares. These decisions should ensure that share holders obtain competitive returns from shares (either through harvesting the shares through their own activity or through lease payments), as well as achieve relatively full harvest of those allocations.

Shares are likely to trade at a free market price, unaffected by the sea time requirement, the only qualification needed for private share acquisition. That minimal requirement can be met relatively easily, as many persons nationwide meet that the requirement. In addition, CDQ groups, who are relatively well financed, tend to favor Bering Sea and Aleutian Island fishery investments over other investments, as these fishery investments can aid in meeting their community development objectives. As a result, CDQ groups may be willing to pay premium prices for investments in the crab fisheries, further ensuring that share prices are not reduced by the regulatory limit on private acquisitions.

The current rules for qualification for owner QS acquisition are relatively simple and inexpensive to administer. The sea time requirement is administered through certification of the recipient, who is required to provide specific fishing information, which is subject to some verification. Typically, fishery openings and closings are reviewed to ensure that fisheries were open during identified participation periods. In addition, any suspect information may be given additional review. As a single, one-time qualification, information does not need to be submitted for each application, only once for each individual or entity acquiring QS. This simple qualification allows NOAA Fisheries to maintain an individual or entity qualification indefinitely, without requiring additional qualification information for future acquisitions. Consequently, administration costs of the existing rule are relatively low.

#### **Alternatives to change eligibility to acquire and retain owner shares**

The proposed action would require a person to meet an ongoing active participation requirement to acquire and maintain holdings of owner QS.

Under the Council motion, individual's that wish to acquire and hold QS may satisfy the active participation requirement by holding a 5 percent, 10 percent, or 20 percent ownership interest in a vessel that participated on one of the rationalized crab fisheries in 1 of the 2 or 4 preceding seasons. Partnership or corporate held shares would subject to a similar requirement, under which an individual with a 10 percent, 20 percent, or 33 percent interest in the share holding entity would be required to also hold a 5 percent, 10 percent, or 20 percent interests a vessel that participated in a rationalized crab fishery in 1 of the 2 or 4 preceding seasons. For the 2010-2011 and 2011-2012 seasons, fewer than 110 vessels would meet the more liberal landing threshold, which requires one landing in the four preceding years, while fewer than 100 vessels would meet the more stringent landing threshold, which requires one landing in the preceding two years.

If vessel and share ownerships were structured to maximize the number of individuals and entities independently<sup>2</sup> qualified to hold shares, over 400 individuals and entities could independently meet the most stringent proposed threshold. As of the 2011-2012 season 321 individuals and entities held owner QS, approximately 90 fewer than the maximum number of individuals and entities that could meet the threshold independently. While it is unlikely that vessel ownership structures would independently qualify the maximum number of owner QS holders, overlapping ownership structures could qualify a substantially larger number of owners. For example, a single individual that owns a 25 percent interest in a participating vessel would be qualified, and could also qualify several different companies that he or she holds the requisite interest in. Particularly if the ownership threshold is set relatively low – such as requiring only a 10 percent interest of the vessel owner in the share holding company – it is possible that a single vessel could qualify partners in several different entities to hold a relatively large amount of owner QS. In any case, the underlying structure would seem to allow for the qualification of a very large number of entities to hold owner QS.

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<sup>2</sup> As used here, independently means that no overlapping interests in QS holdings exists between any qualified individuals and entities. In other words, each entity's qualification is satisfied by a different person meeting the vessel ownership standard.

In general, any revision of share holding eligibility to require a vessel ownership is likely to have a substantial effect on the distribution of QS holdings in the fisheries.<sup>3</sup> If only vessel owners (or persons affiliated with vessel owners) are permitted to hold QS, it is likely that vessel owners will gain influence over QS acquisitions and the distribution of QS in the fishery. With each new partnership, it is likely that a portion of the QS will be removed from broader circulation, becoming associated with the vessel (or vessels) controlled by the owner (or ownership group). Over time, it may be expected that concentrations of QS in the fisheries will be associated with the 100 active vessels in the fisheries and be subject to decisions of the owners (and ownership groups) that control those vessels. If QS holdings consolidate into entities associated with the active vessels in the fishery, it is likely to decrease the potential for small amounts of QS to come on to an open market accessible to these crewmembers.

It will remain possible for a person to enter the fishery by acquiring a vessel and leasing quota, but it may also be even more difficult to make such an entry. Since QS holdings will require a vessel ownership relationship, it is likely that a person acquiring a vessel to enter the fishery would need to acquire a substantial amount of QS (or entice holders of substantial amounts of QS to sever an existing relationship with another vessel owner and lease share to be harvested on the entering vessel) to enter the fishery.

In considering the specific operation of the options, it should be noted that for an individual to hold owner QS that person would need to meet the same standard that a single shareholder in a partnership or corporation would need to meet. In other words, an individual owning an active vessel could buy owner QS or could qualify a partnership or corporation to hold owner QS (despite between 66 and 90 percent of the owners of that partnership or corporation having no connection to the fisheries other than their share holdings). A few consequences of this structure are worth considering. First, an individual must make a substantial investment in a vessel to qualify to hold QS. Second, corporate owners may be largely passive, despite a shareholder who meets the corporate ownership threshold also owning an active vessel. Consequently, control of the owner QS may be vested in persons with no active engagement in the fisheries.

As an alternative to qualifying through vessel ownership, an individual or corporation may be eligible to acquire and retain owner QS through participation in the fisheries as a crewmember. Individuals can qualify through verified participation in 1, 2, or 4 trips in one of the previous 3 or 4 years. A partnership or corporation could qualify if an owner with more than a 10, 20, or 33 percent interest in the entity meets the threshold crew participation requirement. Based on landings in the years preceding the 2011-2012 season between 83 and 100 vessels would meet the different trip thresholds. Increasing the trip threshold to four has the greatest effect on the number of vessels that meeting the trip threshold, as between 95 and 100 vessels meet the one and two trip thresholds, while fewer than 90 vessels meet the four trip threshold under either the three or four year window. Again, it should be noted that comparing these data to annual participation levels suggests that some vessels come and go from the fisheries each year. In recent years, vessels in the crab fishery have employed between 5 and 6 unique crewmembers (including captains) annually on average (see Table 13). Assuming that each vessel that meets the threshold qualified the average number of unique crewmembers, between approximately 450 and 600 crewmembers would meet a threshold for the 2011-2012 season, depending on which threshold is applied.

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<sup>3</sup> It should be noted that these changes may take some time to manifest themselves, as the proposed action would apply only to new QS acquisitions. Existing holders who liberally lease their shares through existing arrangements with vessel owners will have no need to restructure their holdings or leasing arrangements as a result of this action. Consequently, the transition of QS holdings to active persons (as defined by the action) and resulting effects may not be realized for several years.

While a relatively large number of individuals are likely to meet the qualification to acquire owner QS, it is possible that a large number of these individuals may not have access to funding to purchase QS. Priced transactions of owner QS have averaged in excess of \$150,000 in every year in the Bristol Bay red king crab and Bering Sea *C. opilio* fisheries and exceeded \$1.0 million in one year in the Bering Sea *C. opilio* fishery. Many active crew work on crab vessels as their primary source of income. From 2006 through 2010, mean and median annual compensation of captains on vessels that participated in both the Bristol Bay red king crab and Bering Sea *C. opilio* fisheries ranged from approximately \$100,000 to approximately \$185,000. During the same time period, mean and median compensation for the remaining crewmembers ranged from approximately \$40,000 to \$90,000.

Although a large number of the crew meeting the qualification may not have access to funding to purchase owner QS, they may be able to access funds by forming partnerships and corporations with persons with access to funding who do not meet the active participation qualification, particularly under options that allow the active individual to have a relatively small share of the ownership interest in the QS holding entity. While these minimal stake arrangements may resolve a funding issue for active crew, they will have consequences. As with the vessel ownership thresholds, the Council should consider the potential for active individuals to have very little control over the entity's QS, if the active individual needs to only hold a relatively small interest in that entity.

From the standpoint of crewmembers, the highest annual trip requirement (four trips in a year) could be problematic. If a vessel fishes a relatively small allocation in one fishery, it is possible that the vessel may make only two or three trips in a year. Despite relatively consistent annual participation, such a vessel's harvest may not be adequate to qualify a crewmember to acquire and retain owner QS. In addition, to the extent that a crewmember may attempt to use their qualification to develop partnerships with persons with better access funding for QS acquisitions, potential partners may be reluctant to enter QS purchase arrangements with crew that work on vessels that harvest small amounts of quota despite their consistent annual participation.

The effects of this action on QS holders and holdings are likely to be realized over many years. Under its terms, the eligibility criteria for maintaining owner QS only apply to shares acquired after the action is implemented. As such, current share holders would not be required to comply with any active participation requirements to maintain their holdings. Share holders that currently lease their holdings (not owning an interest in an operating vessel) are likely to continue to lease their shares. In addition, it is possible that some of the owner QS holders that have maintained ownership interests in active vessels could divest of their interest in a vessel and lease their annual allocations to others. Exempting existing share holdings from the action have the dual effects of not disrupting business plans of current share holders and phase in the active participation requirement over what could be a very extended period of time.

A notable aspect of the action alternatives in their current form is that CDQ groups and other entities that hold rights of first refusal on behalf of communities cannot qualify to acquire owner QS. To be eligible a corporation or partnership must have an individual owner that meets either the vessel ownership or crew eligibility criteria. By their structure, CDQ groups and community entities have no specific individual owners. This disqualification would occur despite several CDQ groups directly owning vessels that actively participate in the fisheries. Although CDQ groups and other crab community entities may not meet the eligibility criteria specified in the alternatives as currently specified, qualifying CDQ groups and other crab community entities either directly or through a modification of the proposed active participation requirements is likely consistent with the Council's intention for the action, as most CDQ

groups and other crab community entities maintain direct or indirect interests in active vessels in the fisheries to pursue their community development objectives.

#### Interactions of the qualifying provisions

The proposed action's two means of eligibility to acquire owner QS are likely to interact. Persons eligible through vessel ownership qualification are likely to dominate the market for owner QS. Vessel owners are likely to have more assets and access to capital to fund QS acquisitions. Vessel owners are also more likely to be viewed as more appealing business partners, as they have greater business experience with investments and operations. While some individuals meeting the crew qualification are likely to have similar qualities and skills, the majority of active crew are likely to be less experienced in business. In addition, qualifying only as a crewmember could pose some risk, as injuries or loss of job could result in a loss of eligibility. While some risk is also inherent in vessel ownership, qualification through a partnership with an established vessel owner is likely to be viewed as a more stable and reliable means of qualification. These factors may constrain opportunities for crew that might be interested in acquiring owner QS through partnerships with others.

Actions that decrease the pool of individuals and entities eligible to acquire owner QS have the potential to decrease competition for those shares. The proposed action will limit eligibility to acquire owner QS by requiring that an individual QS holder have, or entity QS holder have an individual owner who has, either an ownership interest in an active crab vessel or be active as a crewmember on a crab vessel. Even without eligibility requirements, persons with crew and vessel ownership interests are the most likely to invest in the fisheries. These people have the most knowledge of the fisheries and the business opportunities that they present. The alternatives also provide for substantial investments by persons who do not own a vessel ownership or crew, but partner with someone who does own a vessel or crew on a vessel. These means of indirectly qualifying allows for substantial capital to come into the fisheries by persons who do not actively participate in the fisheries. These avenues should ensure that any price effect of the active participation requirements is relatively minor.

Rules establishing active participation requirements for acquisition and retention of owner QS will require NOAA Fisheries to monitor vessel and crew participation and integrate those participation records with vessel ownership and QS holdings information and corporate and partnership ownership information. The burden associated with this monitoring will vary with each case, but could be very high. Vessel owner eligibility would require submission of vessel ownership and participation records for a period of years, which would be similarly compared to vessel participation records. To verify continuing eligibility to hold owner QS, owner QS holders will likely need to submit information concerning their qualifications on an annual basis (either as a part of their annual IFQ application or separately), since the requirements are applied over a period of years. In addition, the timeline for submitting applications and appealing administrative decisions will need to be reviewed, once the Council has fully specified its alternatives (defining the intended consequences of failing to comply with the active participation requirements).

The action alternative would require that individuals and entities meet eligibility requirements to acquire owner QS. The timeline for applications and filing of appeals will need to be given additional scrutiny as this action proceeds. As currently defined by the motion, verification of active participation would require review of ownership records for vessels and QS holding entities. Depending on the structure of the requirements and the consequences for failing to meet those requirements, the action could create a substantial and costly burden for managers.