

## EXECUTIVE SUMMARY

In 2001, Congress directed the Council to conduct an analysis of several different approaches to rationalizing the BSAI crab fisheries (see Consolidated Appropriations Act of 2001 (Pub. L. No. 106-554)). In response, the Council adopted the following purpose and need statement to guide it through the process of considering rationalization alternatives for the fisheries:

*Vessel owners, processors and coastal communities have all made investments in the crab fisheries, and capacity in these fisheries far exceeds available resources. The BSAI crab stocks have also been highly variable and have suffered significant declines. Although three of these stocks are presently under rebuilding plans, the continuing race for fish frustrates conservation efforts. Additionally, the ability of crab harvesters and processors to diversify into other fisheries is severely limited and the economic viability of the crab industry is in jeopardy. Harvesting and processing capacity has expanded to accommodate highly abbreviated seasons, and presently, significant portions of that capacity operate in an economically inefficient manner or are idle between seasons. Many of the concerns identified by the NPFMC at the beginning of the comprehensive rationalization process in 1992 still exist for the BSAI crab fisheries. Problems facing the fishery include:*

- 1. Resource conservation, utilization and management problems;*
- 2. Bycatch and its' associated mortalities, and potential landing deadloss;*
- 3. Excess harvesting and processing capacity, as well as low economic returns;*
- 4. Lack of economic stability for harvesters, processors and coastal communities; and*
- 5. High levels of occupational loss of life and injury.*

*The problem facing the Council, in the continuing process of comprehensive rationalization, is to develop a management program which slows the race for fish, reduces bycatch and its associated mortalities, provides for conservation to increase the efficacy of crab rebuilding strategies, addresses the social and economic concerns of communities, maintains healthy harvesting and processing sectors and promotes efficiency and safety in the harvesting sector. Any such system should seek to achieve equity between the harvesting and processing sectors, including healthy, stable and competitive markets.*

In June of 2004, after deliberating at several meetings, the Council took final action adopting its preferred alternative for rationalizing the fisheries. As a part of that action, the Council requested this comprehensive review of the first five years of the program. The analysis examines five years of fishing under the program. The change to any share-based management system requires participants to modify their behavior. Some changes evolve over time, as participants adapt to the program. While some aspects of this transition (such as fleet consolidation) occurred immediately on implementation of the program, others, such as the joint fishing of allocations in cooperatives, have occurred more gradually. In considering the assessment of the program in this document, it should be noted that the fishery continues to evolve as participants learn to operate under the program and adapt to the changes it has brought on.

### **Description of the management**

Prior to the rationalization program, the major Bering Sea and Aleutian Islands crab fisheries were managed under the License Limitation Program, a limited entry program under which licenses were allocated to harvesters based on historic participation. A guideline harvest level (GHL) for each fishery set target catch for the fishery. Managers monitored harvests by in-season reports and attempted to time the closure of a fishery with completion of the harvest of the GHL. Harvests exceeded the GHLs in some years, however, because in-season monitoring could not keep pace with harvests during the short seasons.

Over time, managers improved in their abilities to monitor catch in season, limiting the extent of these GHL overages. Since the seasons in most of the BSAI crab fisheries do not conflict, most participants were active in several of the fisheries, moving from one fishery to another. However, stock declines in the Bristol Bay red king crab and the Bering Sea *C. opilio* led to seasons lasting only a few days or weeks. Consequently, equipment was often idle for several months of the year.

The rationalization program allocates catch shares in the large crab fisheries in the Bering Sea and Aleutian Islands, specifically the following:

- Bristol Bay red king crab
- Bering Sea *C. opilio* (snow crab)
- Eastern Bering Sea *C. bairdi* (Tanner crab) – East of 166° W
- Western Bering Sea *C. bairdi* (Tanner crab) – West of 166° W
- Pribilof blue and red king crab
- St. Matthew Island blue king crab
- Western Aleutian Islands (Adak) golden king crab – West of 174° W
- Eastern Aleutian Islands (Dutch Harbor) golden king crab – East of 174° W
- Western Aleutian Islands (Adak) red king crab – West of 174° W

To address the concerns of various stakeholders in these fisheries, the Council developed a “voluntary three pie cooperative” program intended to protect the interests of the harvest sector, the processing sector and defined regions and communities. Each program fishery is managed with a total allowable catch (TAC), which sets a specific catch limit, instead of a GHL. Although the change to a TAC may be largely semantic, it signifies a change to more precise catch management.

Harvesting quota shares (QS), revocable privileges to harvest a specific percentage of the annual TAC, were allocated in each program fishery. Approximately 97 percent of the QS (referred to as “owner QS”) in each program fishery were initially allocated to license holders based on their catch histories, while the remaining 3 percent of the QS (referred to as “C shares” or “crew QS”) were initially allocated to captains based on their catch histories in the fishery. The annual allocations, which are expressed in pounds, are referred to as individual fishing quota (IFQ). QS are designated as either catcher vessel QS or catcher processor QS, depending on whether the vessel giving rise to the privilege processed the qualifying harvests on board. C share QS may be acquired by persons with recent participation on a vessel in the fishery and, under a recent amendment, will require that their holders demonstrate continued active participation in a program fishery (or for recipients of an initial allocation, continued active participation in State or Federal fisheries in or off Alaska).

Catcher vessel owner IFQ are issued in two classes, Class A IFQ and Class B IFQ. Class A IFQ are issued for 90 percent of the catcher vessel owner IFQ in a program fishery. Crab harvested using these IFQ must be delivered to a processor holding unused individual processing quota (IPQ). In addition, Class A IFQ are subject to regional share designations, whereby harvests are required to be delivered within an identified region. In most program fisheries, regionalized shares are either North or South, with North shares designated for delivery in areas on the Bering Sea north of 56° 20' north latitude and South shares designated for any other areas, including Kodiak and other areas on the Gulf of Alaska. In the Western Aleutian Islands (Adak) golden king crab fishery, the designation is based on an east/west line to accommodate a different distribution of activity in that fishery. Share designations are based on the historic location of the landings and processing that gave rise to the shares. The delivery restrictions of Class A IFQ are intended to add stability to the processing sector by protecting processor investment in program fisheries and to preserve the historic distribution of landings and processing between regions. To provide harvesters with additional market leverage for negotiating prices for landings of crab, Class B IFQ are issued for the remaining 10 percent of the catcher vessel owner QS in a program fishery and may be delivered to any processor (except a catcher processor) in any location.

QS and IFQ are transferrable under the program, subject to limits on the amount of shares a person may own or use. IFQ transfers after a delivery to cover overages are allowed. The program also allows harvesters to form harvest cooperatives. Cooperatives receive the annual IFQ allocated to their members. Formation of cooperatives is intended to facilitate production efficiency by aiding harvesters in coordinating share transfers and harvest activities and deliveries to processors, as catch is monitored at the cooperative level. Harvesters within a cooperative may transfer IFQ freely without notice to managers since those IFQ are directly allocated to the cooperative and are counted against the cooperative's allocation. IFQ transfers between cooperatives are administered through NOAA Fisheries. After the fifth year of the program, leasing of QS (or equivalently, the sale of owner IFQ - defined as the use of IFQ on a vessel in which the owner of the underlying QS holds less than a 10 percent ownership interest and on which the underlying QS holder is not present) is allowed only among harvest cooperatives.

To ensure that future share holders in the fishery have fishing background, to acquire shares in the fishery an individual is required to be a US citizen and to have at least 150 days of sea time in US commercial fisheries in a harvest capacity. An partnership or corporation is eligible to purchase shares only if it is at least 20 percent owned by a US citizen with at least 150 days of sea time in US commercial fisheries in a harvest capacity and is at least 75 percent U.S. owned, allowing it to document a vessel. Initial recipients of QS and CDQ groups are exempt from these eligibility criteria.

“Individual use caps” are imposed on the use and holdings of harvest shares in order to prevent excessive consolidation of shares under the program. Different caps apply to owner share holdings and C share holdings. In addition, the six groups participating in the Community Development Quota program – a program intended to benefit Bering Sea coastal communities - are subject to higher share caps. “Vessel use caps” limit the amount of owner IFQ that may be harvested by a single vessel. Vessel use caps do not apply to cooperatives, thereby providing an additional incentive for cooperative participation (see Table 1-1).

**Table 1-1 Harvest share use caps as percent of the respective quota share pool.**

Fishery	Owner share		C share use cap**	Vessel use cap*
	Individual use cap*	CDQ group use cap*		
Bristol Bay red king crab	1	5	2	2
Bering Sea <i>C. opilio</i>	1	5	2	2
Eastern Bering Sea <i>C. bairdi</i>	1	5	2	2
Western Bering Sea <i>C. bairdi</i>	1	5	2	2
Pribilof red and blue king crab	2	10	4	4
St. Matthew Island blue king crab	2	10	4	4
Eastern Aleutian Islands golden king crab	10	20	20	20
Western Aleutian Islands golden king crab	10	20	20	20
Western Aleutian Islands red king crab	10	20	20	20

\* as a percentage of the owner share pool.

\*\* as a percentage of the C share pool.

To protect processor investments in the fisheries, the program also created processing quota shares (PQS), which are allocated to processors based on processing histories. PQS are a revocable privilege to receive annual allocations of individual processing quota (IPQ), which authorize the acceptance of deliveries of a portion of the annual TAC from a program fishery. IPQ is issued for 90 percent of the catcher vessel owner IFQ pool, corresponding to the 90 percent allocation of owner IFQ issued as Class A IFQ. As with

owner QS and Class A IFQ, PQS and IPQ are designated for processing in a region. To protect independent vessel owners and processors that are not vertically integrated, processor harvest share holdings are also limited by a cap on vertical integration. To promote efficiency, processing shares are transferable, including leasing of PQS (or equivalently, the sale of IPQ) subject to a use cap that prohibits any person from holding or using in excess of 30 percent of the processing shares in a fishery. An exception allows consolidation of processing (but not share holdings) beyond the caps in fisheries and regions that pose particular economic challenges to processors. To provide a period of general stability for processors and communities to adjust to the program a two-year "cooling off period" was established during which processing shares could not be relocated from the community where the historical processing occurred that led to the allocation (the community of origin). In addition, a right of first refusal was granted to community groups and CDQ groups from communities with significant crab processing history on the sale of any processing shares for use outside of the community of origin. Exceptions to the right allow a company to consolidate operations among several commonly owned plants to achieve intra-company efficiencies and the temporary lease of shares outside of the community of origin.

Catcher processors participate in both the harvest and processing sectors and therefore have a unique position in the program. Catcher processors are allocated catcher processor QS and issued corresponding catcher processor IFQ. These shares carry both a harvest privilege and an accompanying onboard processing privilege. A person holding catcher processor shares may either harvest and process crab onboard under the allocation or choose not to process harvested crab, instead delivering their catch to any other processor.

An arbitration system serves several important purposes in the program, including dissemination of market information to facilitate negotiations, the coordination of matching Class A IFQ held by harvesters to IPQ held by processors, and a binding arbitration process to resolve terms of delivery. A "market analyst" and a "formula arbitrator," jointly selected by the harvesting and processing sectors, develop a market report and price formula, which specifies an ex vessel price as a portion of the first wholesale price, to be used by participants to guide their delivery negotiations. Neither the market report nor the formula price are binding, but are intended to provide information concerning the market and the price that might be generated by a binding arbitration proceeding. Matching of Class A IFQ with IPQ is facilitated through a process of share commitments and dissemination of information concerning available shares. Once shares are matched, parties unable to negotiate terms of delivery (which may include the price) may use the arbitration system to resolve those terms.

To ensure predictability and fairness, the arbitration system sets forth standards to be followed by formula arbitrators and contract arbitrators. Although different standards apply to the formula arbitrator and the contract arbitrator, the differences between the standards are very limited and do not substantively change the general approach to be applied. The regulations provide that both the non-binding price formula and contract arbitrator's decision must establish a price that preserves the historical division of revenues in the fishery while considering several listed factors (such as quality, product innovations, the interest of maintaining the financial health of the harvesting and processing sectors, and the timing and location of deliveries).

The program also made changes in the allocations under the CDQ program, broadening that program to include the Eastern Aleutian Islands (Dutch Harbor) golden king crab fishery and the Western Aleutian Islands (Adak) red king crab fishery and increasing the allocations in all crab fisheries covered by the CDQ program from 7.5 to 10 percent of the TAC. These changes in the CDQ allocations are intended to further facilitate fishing activity and economic development in rural Western Alaska communities. The CDQ allocations are managed independently from the program and are not subject to IPQ and regional landing requirements. The program also made an allocation of 10 percent of the Western Aleutian Islands

(Adak) golden king crab fishery to the community of Adak This allocation to Adak is thought to be appropriate because that community was excluded from the CDQ program because of its history as a military community.

The rationalization program includes a low interest loan program to assist eligible captains and crew in purchasing QS. The program implementation was delay for the first 5 years of the program, but funding of loans is expected to begin in the near future. "Sideboards" impose limits on the activity of crab vessels in other fisheries to protect participants in those fisheries from a possible influx of activity that could arise from vessels that exit the program fisheries or are able to time activities in the program fisheries to increase participation in other fisheries. An economic data collection program, to help the Council and NMFS assess the success of the program and develop future management actions was included in the program. The data collection is currently being modified to eliminate redundancies with other data collections and eliminate the collection of inaccurate data.

### Harvest sector privileges

Prior to implementation of the rationalization program, NOAA Fisheries managed the Bering Sea and Aleutian Island crab fisheries under the License Limitation Program (LLP), whereby vessels assigned a transferrable LLP license could participate in those fisheries designated by the license. Licenses were initially allocated based on historic participation with species-area (fishery) endorsements (see Table 1-2). Licenses were issued by vessel type (catcher vessel or catcher processor) and specified a maximum vessel length (MLOA). Since licenses could carry multiple species-area endorsements, the total number of licenses was not additive.<sup>1</sup>

**Table 1-2 LLP licenses in the Bering Sea and Aleutian Islands crab fisheries (2005).**

LLPs	Bristol Bay red king crab	Bering Sea <i>C. opilio</i> and <i>C. bairdi</i>	Pribilof red and blue king crab	St. Matthew Island blue king crab	Aleutian Island red king crab	Aleutian Island golden king crab	Catcher processor
Licenses endorsed for							
also endorsed for							
Bristol Bay red king crab	270	264	110	168	28	25	26
Bering Sea <i>C. opilio</i> and <i>C. bairdi</i>		273	109	169	30	27	27
Pribilof red and blue king crab			118	77	15	8	2
St. Matthew Island blue king crab				170	26	19	13
Aleutian Island red king crab					30	8	4
Aleutian Island golden king crab						28	9

Source: NMFS RAM Division.

A moratorium on entry, established in 1995, limited speculative entry into the fisheries while the LLP was being developed and approved. Nevertheless, the fisheries remained heavily overcapitalized. Further, the limited access management increased the incentive for all license holders to participate in the fisheries because a person could not receive a return without participating. Some participants allege that financial pressures of boat payments ensured their participation, as revenues from the fisheries were their primary source of income from their vessels. Participants also likely remained in the fisheries to reinforce their stake in any future history-based allocation. In the years leading up to implementation of the rationalization program, few licenses were transferred. First, entry to the crab fisheries was costly because it required the purchase of an LLP permit and a properly configured vessel from which to fish. Secondly, the continuing overcapitalization, together with the historically low GHIs for the Bering Sea *C. opilio* fishery, in particular, made the crab fisheries economically unattractive for potential new entrants.

When the program was implemented, NOAA Fisheries made initial allocations of owner QS to persons holding LLP licenses. Since most licenses were held by corporations, aggregation of license holdings by

<sup>1</sup> Exceptions to the LLP license requirement included vessels that do not exceed 32 feet LOA in the BSAI and certain vessels constructed for, and used exclusively in, CDQ fisheries.

owner name typically will not reflect actual common control of QS holdings. In addition, complex corporate ownership patterns prevent a complete assessment of the level of concentration of ownership beyond relying on the named owner for this report. Consequently, levels of consolidation of owner shares exceed those represented in the following discussion.

Approximate 250 persons received allocations of owner QS in the largest fisheries – the Bristol Bay red king crab and the Bering Sea *C. opilio*, as well as in the Bering Sea *C. bairdi* fisheries. The largest allocations in these fisheries exceeded 2 percent of the QS pool. In the St. Matthew Island blue king crab and the Pribilof blue in red king crab fisheries, 136 persons and 112 persons received allocations of owner QS, respectively, with the largest allocations exceeding 4 percent and 3 percent of the respective QS pools. Initial allocations were made to 15 persons in each of the Aleutian Islands golden king crab fisheries, with the largest allocation in the Eastern fishery exceeding 20 percent of the pool and the largest allocation in the Western fishery exceeding 40 percent of the pool. In the Western Aleutian Island red king crab fishery, 30 persons received an initial allocation, with the largest allocation exceeding 40 percent of the pool. Catcher processor allocations were less than 10 percent of the pool in all fisheries, except the two Western Aleutian Island fisheries, in which catcher processors received approximately 40 or more of the QS allocated.

The initial crew QS allocations showed a pattern similar to initial allocations of owner QS allocations across the program. Since fewer persons qualified for initial allocations of C share QS, holdings were more concentrated than initial owner QS holdings. In most cases, the initial allocations of C share QS were more evenly distributed among initial recipients. In each of the three largest fisheries, fewer than 200 persons receive an initial allocation of C shares, with the largest allocations less than 2 percent of the respective C share QS pools. In the St. Matthew Island and Pribilof fisheries, 72 and 40 persons received initial allocations, respectively, with the largest allocations exceeding 3 percent and 4 percent of the respective pools. In the Eastern Aleutian Islands golden king crab fishery, 13 persons received initial allocations, with the largest allocation making up less than 13 percent of the C share QS pool. Initial allocations of C share QS in each of the two Western Aleutian Island fisheries were made to fewer than 10 people, with the largest allocations exceeding 40 percent of the respective pool.

In the first five years of the program, substantial portions of the harvesting QS pools were transferred. Transfers of shares in some fisheries sum to over 50 percent of the QS pool, while transfers in the two largest fisheries (the Bristol Bay red king crab and Bering Sea *C. opilio* fisheries) sum to in excess of 20 percent of the respective QS pools. As with other data concerning owner share holdings, transfer data can be misleading. In some cases, transfers are changes in the name of the holder. In other cases, the transfer might reflect a change in structure of the share holding entity (such as the addition of a new partner or a change in corporate ownership). Yet, a change in corporate or partnership ownership structure will not be recorded, if the named entity holding shares remains unchanged.

Share holdings distribution data in the Bristol Bay red king crab, Bering Sea *C. opilio*, and both Bering Sea *C. bairdi* fisheries suggest that owner quota share holdings have become slightly more concentrated since the initial allocation. In each of these fisheries, the maximum holding increased to a level that exceeds the individual cap applicable to most holders, as a result of CDQ groups, who are subject to separate higher share holdings caps, have increased their holdings in the fisheries. Although some QS holders have consolidated holdings in the fisheries, the number of owner quota share holders increased or has stayed near constant since the initial allocation in all of the fisheries.

The current distribution of C share quota share holdings shows larger changes from the initial allocation than that of owner shares. Persons have consolidated holdings, acquiring shares to the individual cap in the Bristol Bay red king crab, Bering Sea *C. opilio*, and both Bering Sea *C. bairdi* fisheries. Approximately 20 fewer persons and 40 fewer persons hold shares in each of these fisheries than held

shares at the initial allocation, respectively. Although active participation requirements did not apply for the first three years of the program and the exemption of cooperative members from the requirements continues to apply, some holders may have divested as they have lost their connection to the fisheries. C share holders might also be more likely to divest of their share holdings, since those holdings are a relatively small portion of the overall QS pool, limiting the annual income that might be derived from those shares. Holders of owner QS who no longer enter a vessel into the fishery may be more likely to maintain their share holdings, as the flow of income from those shares is likely to be substantially greater, since those shares make up a much larger share of the QS pool.

Limits on vertical integration included in the program are intended to prevent PQS holders from acquiring a substantial share of the QS pool. In addition, PQS should decrease the incentive for processors to acquire harvest shares, as PQS holdings ensure access to a portion of the landings in the fishery. These factors appear to have limited the degree of vertical integration in the fisheries. IFQ allocations under a rule that restricts the allocation of Class B IFQ to PQS holders suggest that slightly less than 20 percent of the Bristol Bay red king crab QS pool is held by PQS holders and their affiliates. A similar portion of the Bering Sea *C. bairdi* catcher vessel owner pool is subject to PQS affiliation, while slightly less of the Bering Sea *C. opilio* catcher vessel owner pool is subject to PQS affiliation. In the two Aleutian Island golden king crab fisheries almost no QS are held by persons with affiliations with PQS holders in that fishery (although a few of the QS holders have affiliations with holders of PQS in other fisheries).

### The Harvest Sector

A precipitous decline in the fleets in all fisheries occurred on implementation of the program (see Table 1-3). In the Bristol Bay red king crab fishery, the fleet contracted to less than one-third its pre-rationalization size. In the Bering Sea *C. opilio* fishery, the contraction was of smaller magnitude because this fleet had contracted to some degree prior to implementation of the program, as GHFs in the fishery were at historic lows in the years preceding the program. Despite the fleet consolidation, average vessel catches in the large fisheries currently parallel those of seasons prior to 2000, when either fewer vessels were participating in the crab fisheries or one or more of the major fisheries had a relatively high harvest (see Figure 1).

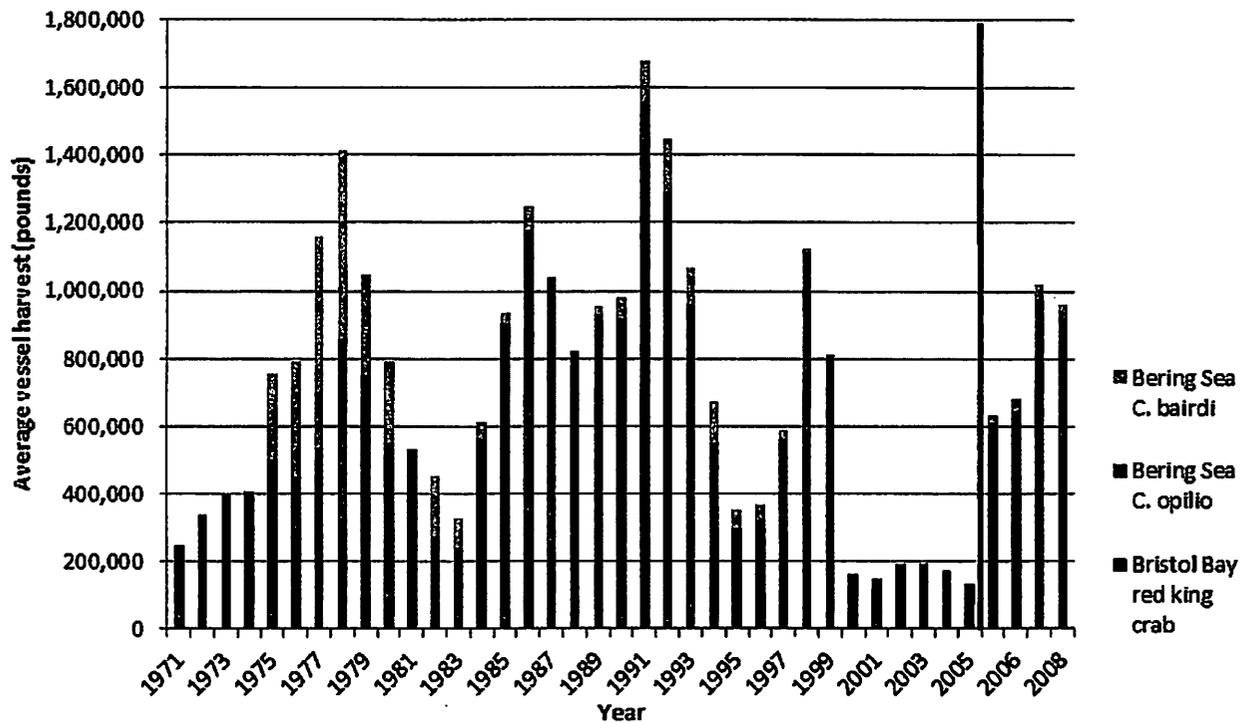
Table 1-3. Total catch and vessel participation in fisheries open preceding and subsequent to program implementation in 2005/6.

Fishery	Seasons	Average total catch	Average number of vessels participating
Bering Sea <i>C. opilio</i>	2001-2005	24,511,160	189
	2005/6 - 2009/10	43,710,333	74
Bristol Bay red king crab	2001-2004	11,144,469	243
	2005/6 - 2009/10	16,260,196	78
Eastern Aleutian Islands golden king crab	2001/2-2004/5	2,910,091	19
	2005/6 - 2009/10	2,721,660	5
Western Aleutian Islands golden king crab	2001/2-2004/5	2,643,870	7
	2005/6 - 2009/10	2,272,224	3

Sources: ADFG fishtickets prior to 2005 and NMFS RAM catch data (for 2005-2006 through 2009-2010)  
Notes: Catch as a percent of IFQ allocations for 2005-2006 through 2009-2010 seasons.

Fleet consolidation in the program fisheries was the result of owners and operators making business decisions to idle boats in order to remove excess capacity from the fisheries. Leasing of quota, and the accompanying retirement or sidelining of excess capital, has taken place to the degree but more quickly than most predicted. A few factors likely contributed to the substantial consolidation that occurred in the

first years of the program. Consolidation was stimulated by the cooperative structure under the program. Cooperatives created the framework for and led to the development of harvesting associations. These strengthening relationships, in turn, created an environment ripe for consolidation of harvesting. In addition, it is likely that a portion of the fleet active prior to implementation of the program only remained in the fishery because of the impending rationalization program. Owners of these vessels quickly removed their vessels once the program was implemented.



Source: ADFG Annual Management Report 2008-2009.

Notes: Harvests for seasons overlapping two calendar years are attributed to one of the two years, to avoid double counting catches from a single fishery in the same year. Harvest per vessel is sum of average vessel's harvest in each fishery.

**Figure 1. Approximate annual average vessel harvests in the Bristol Bay red-king crab, Bering Sea *C. opilio*, and Bering Sea *C. bairdi* fisheries (1971 through 2008-2009).**

In the first five years of the program, participants have harvested most of the issued IFQ. In each year in the two largest fisheries – the Bristol Bay red king crab and Bering Sea *C. opilio* fisheries – catches have exceeded 99 percent of the IFQ allocation. Lower portions of the IFQ were harvested in the *C. bairdi* fisheries, as well as the St. Matthew Island blue king crab fishery, as participants have reported that those fisheries have been particularly difficult to prosecute because of low catch rates. This complication seems to have been resolved in the Eastern *C. bairdi* fishery as most of the TAC was harvested in the 2009-2010 season. The St. Matthew Island fishery opens in October, one month later than its historical September opening. Some participants attribute low catch rates in the fishery to the later opening under current regulations. Crab are thought to migrate offshore and be more dispersed in October which may contribute to lower catches. Reduced fleet size due to consolidation may also have contributed to low total catch relative to the TAC during the 2009-2010 season. Harvest of the Western Aleutian Islands golden king crab fishery in some years has been reported to be economically challenging because of low market prices for golden king crab and limited processing capacity in the West region (where 50 percent of the catcher vessel owner IFQ is required to be landed). The 2009-2010 harvest of nearly the entire IFQ allocation suggest that a recent amendment creating an exemption to the regional landing requirement (by agreement

of QS holders, PQS holders and the communities of Atka and Adak) will resolve the processing capacity issue in the fishery.

While most participants have managed to harvest close to their full allocations, a few IFQ holders have exceeded their IFQ allocations in the first five years of the program. Overages have averaged approximately 30,000 pounds per year aggregated across all fisheries (or less than 5,000 pounds per fishery each year). These overages average slightly more than 4 one-hundredths of a percent of the TAC. Cooperative membership likely plays a role in reducing the number of overages, since IFQ attributable to QS of several different holders are aggregated at the cooperative level. Cooperative held IFQ is fished as a pool by members with no overage until the entire cooperative allocation is fully harvested. The ability of harvesters to avoid overages is also aided by permissible discarding. Under the program, harvesters are permitted to discard crab without charge against IFQ. So, when a harvester estimates that available IFQ are fully used, any catch in remaining deployed gear may be discarded. Lastly, in the most recent season an amendment to the program has permitted harvesters to engage in post-delivery transfers to avoid overages.

Overall, fleet consolidation in the fisheries has tended to distribute catch to larger vessels. The fleet consolidation has led to all but 2 of approximately 15 vessels less than 85 feet in length dropping out of the fisheries. In addition, vessels less than 100 feet in length have disproportionately left the fleet. While vessels greater than 125 make up slightly less of the fleet than vessels greater than 100 feet and less than 125 feet, catches of the larger vessels have increased. This pattern has occurred consistently across all fisheries in the program. The resulting fleet is generally made up of larger vessels than the prerationalization fleet, while continuing to maintain diversity.

Short term transfers under leases and cooperative fishing arrangements are the primary means by which QS holders in the crab fisheries have achieved fleet consolidation under the rationalization program. Favorable lease rates have made quota leasing (inside and outside of cooperatives) particularly attractive under the rationalization program. High lease rates have likely contributed greatly to consolidation under the program. Lease rates fluctuate across seasons and are believed to vary across the fleet. Currently lease data are poor and do not support direct analysis of lease quantities or prices. Intra-cooperative transfers of IFQ are not administered or fully tracked by managers, limiting available information concerning these transfers. Anecdotal evidence suggest that lease rates in the Bristol Bay red king crab fishery have been as high as 70 percent of the ex vessel price, while Bering Sea *C. opilio* lease rates have exceeded 50 percent of the ex vessel price in some cases. In the Bering Sea *C. bairdi* fisheries lease rates are said to have fluctuated from approximately 20 percent to 35 percent of the ex vessel price. The lower rate in this fishery is likely a reflection of the fact that these fisheries have had relatively lower catch rates and low TACs. Lease rates in the Eastern Aleutian Islands golden king crab fishery are said to be approximately 50 percent of the ex vessel prices, while lease rates in the Western Aleutian Islands golden king crab fishery are said to be approximately 20 percent to 25 percent of the ex vessel price. The low lease rate in the Western Aleutian Islands fishery likely has resulted from the high operating costs and low ex vessel price in that remote fishery. In the one year of fishing in the St. Matthew Island blue king crab fishery, lease rates are said to have been approximately 30 percent to 35 percent of the ex vessel price.

Most QS holders have elected to join cooperatives, with almost all IFQ held by cooperatives since the third year of the program. The degree of consolidation of harvest activity is also shown by the relatively large share of the IFQ held by a relatively small number of cooperatives in the fisheries. By the 2007-2008 (the third year of the program), Bristol Bay red king crab and Bering Sea *C. opilio* fisheries, fewer than 20 cooperatives held in excess of 98 percent of the IFQ, with a single cooperative holding in excess of 20 percent of the IFQ in the Bristol Bay fishery. In the fifth year of the program, independent harvesters consolidated several cooperatives that had previously participated collectively in the arbitration system into a single cooperative. This cooperative held in almost three-quarters of the IFQ pool in the all

fisheries except the Western Aleutian Island golden king crab fishery. The extent to which harvests of allocations are managed collectively varied within and across cooperatives, but has increased substantially over time. Although most cooperatives have continued to allow individual members to arrange the harvest of their shares, management of harvests at the cooperative level has increased. This relinquishing of individual management of the harvest of shares not only contributes to consolidation of IFQ harvests, but also has allowed for better coordination, to reduce the disruption of unanticipated circumstances.

High operating costs in the first few years of the program also contributed to the high amount of leasing (and rapid consolidation of fishing). Fuel prices increased by more than 50 percent during the 2005-2006 season. Several participants also reported increases in insurance costs, in part, because many now purchase cargo insurance to cover the quota landings committed to IPQ holders and lease payments committed to other quota holders. In the face of exceptionally favorable quota lease rates and high operational costs many participants elected to lease their quota holdings. Although fuel costs have stabilized, they have remained high. In addition, consolidation within cooperatives continued as cooperative members become more comfortable with cooperative management of their quota. The result of these factors has been greater consolidation of IFQ harvests. During the 2007-2008 season, the number of vessels participating in the Bristol Bay red king crab fishery fell to 74 despite a TAC increase of 31 percent from the previous year. In the Bering Sea *C. opilio* fishery, an approximately 70 percent increase in the TAC in the third year stimulated the reentry of vessels. This increase, however, only returned the fleet to a size of 78 vessels, its size in the first year of the program. As a result, the average vessel harvest in the fishery increased by more than 50 percent, despite the increase in the number of vessels.

Comparing vessel activities before and after implementation of the program in the two largest fisheries brings to light further changes in the fleet dynamics. Under the rationalization program, both the median and largest vessel annual harvests in the Bristol Bay red king crab fishery have been more than double the levels (in pounds and as a percent of the total catch) of the years immediately preceding implementation of the program. The mean and median vessel harvest in the fishery grew consistently in the first three years of the program, before declining in the two most recent years. The largest harvests have fluctuated, both in pounds and as a percent of the total harvests. In the first year of the program, the largest vessel harvests in the Bering Sea *C. opilio* fishery greatly exceeded the largest harvests in years immediately preceding rationalization. Since the 2005-2006 season, average vessel harvests have increased considerably, largely from higher TACs beginning in the third year of the program.

Prior to the rationalization program, TACs were typically harvested and seasons closed in less than one month in all of the program fisheries, except the Western Aleutian Islands golden king crab fishery. In the Bristol Bay red king crab fishery, seasons lasted less than one week, while in both the Bering Sea *C. opilio* and the Eastern Aleutian Islands golden king crab fisheries seasons lasted for less than one month. Although the Western Aleutian Islands golden king crab fishery lasted several months, its seasons also shortened progressively leading up to implementation of the program.

The allocation of exclusive harvest shares allowed the seasons in the fisheries to be extended substantially. Currently season limits are imposed for biological reasons. With this new latitude to schedule harvest activity, participants have dispersed catch substantially with deliveries distributed over a period of several months. Deliveries remain most concentrated in the Bristol Bay red king crab fishery and the St. Matthew Island blue king crab fishery, as the seasons in those fisheries are only four months and four and one-half months, respectively, substantially shorter than the season in other fisheries, and markets tend to be strongest near the year's end leading up to the holidays.

The extension of fishing over a longer period and consolidation of fishing effort has substantially changed the number and volume of deliveries. The average number of deliveries per vessel has doubled in most program fisheries.<sup>2</sup> In addition, the average amount of crab delivered has increased. Prior to the rationalization program, in most fisheries vessels made a single delivery after a fishery closing. Under the rationalization program, almost all vessels make multiple deliveries in a season, fishing closer to the vessel's capacity prior to making deliveries. In general, deliveries average near or more than 100,000 pounds in each fishery, with the exceptions of the Bering Sea *C. bairdi* and St. Matthew Island blue king crab fisheries, which have had relatively low catch rates.

Under the rationalization program, since allocations are exclusive, participants do not need to race to prevent others from preempting their catch. To improve returns from the fisheries, participants have an incentive to reduce costs. The most obvious means of reducing costs is fleet consolidation, which is demonstrated by the removal of vessels from the fisheries. Stacking quota on fewer vessels can save on costs not only of capital, but also on maintenance, insurance, crew, fuel, and other variable input costs. In addition, several participants in the fisheries have reported that the exclusive allocations have allowed them to reduce vessel speed to conserve fuel without risking loss of catch.

The pot usage and pot catches in the fisheries suggest vessels are using the flexibility provided by exclusive allocations and extended seasons, as well as more liberal regulations on pot sharing, to save on operating costs in the fisheries. In the first five years of the program, the number of registered pots per vessel remained constant or increased in all fisheries, while the total number of registered pots in each fishery declined or remained constant. Prior to implementation of the program, pot limits constrained pot usage in some fisheries. Those limits were relaxed under the rationalization program, allowing vessels to choose the number of pots to use to increase operational efficiency. Some vessels are reported to have increased their pot holdings through acquisitions of used pots, which are reported to be readily available in the market. In addition, pot sharing arrangements are reported to be common. In most fisheries, these practices have led to the pulling of each pot more times each season. Vessels are believed to have increased soak times through slowing the pace of fishing and allowing pots to fish during periods when deliveries are made. These increased soak times are believed to have contributed to the increased catch per unit effort observed in most fisheries in the first five years of the program. A different effect has arisen in the Aleutian Islands fisheries where increased soak times (and an accompanying increase in catch per unit effort) has reduced the number of pulls per pot.

The greatest effect on crew arising from the rationalization program was the loss of crew positions brought on by consolidation in the fisheries. Crew sizes are generally unchanged since implementation of the program, so vessel participation provides a direct estimate of the number of crew that have left the fisheries. Assuming six crew members per vessel, approximately 975 fewer crew (including captains) were employed in the Bristol Bay red king crab fishery on average in each of the first five years of the rationalization program, in comparison to the 2000 to 2004 season average; approximately 675 fewer crew were employed in the Bering Sea *C. opilio* fishery on average in each of the first five years of the program, when compared to the 2001 to 2005 season average.<sup>3</sup>

<sup>2</sup> In some instances, multiple deliveries are suggested by multiple fish tickets across multiple days in a single delivery.

<sup>3</sup> Note that these estimates are based on an assumption of 6 persons per crew (including captain). Crab Economic Data Reports suggest that average crews are approximately 5 persons; however, these surveys may have some biases. For years prior to implementation of the program, the surveys requested average crew size. Subsequent to the implementation the survey requests the number of paid crew per fishery. Both suggest that average crews are slightly less than 6 persons.

Although these job losses are substantial, one must also consider the terms of employment in the prerationalization fisheries in assessing the magnitude of the loss. Prior to implementation of the program, few crab deck jobs, fully supported a crewmember. Because of the low total catches and high number of vessels in the fisheries in years leading up to the rationalization program, most crew worked only a month or so in the crab fisheries. Crew typically worked other jobs (including crew jobs in other fisheries) throughout the remainder of the year. In addition, since pay was a share of the vessel's net revenues in the derby, pay was subject to risk. The relatively short tenure of crab crew jobs was attractive to many crew who were able to negotiate (or take) short periods away from other employment to fish crab. Notwithstanding their relatively short term, for many deck crew, their crab fishing jobs were reported to have provided important contributions to annual income. Particularly in the case of crew from remote communities with few job opportunities, replacing income from lost crab crew jobs is reported to be problematic.

Since crew compensation arrangements vary across the fleet, changes in crew share payments can be best assessed by examining the change in payment amounts and change the percentage of gross vessel revenues paid to crew before and after the implementation of the program. Available data suggest that mean and median crew payments as a percentage of gross vessel revenues declined by approximately one-third under the rationalization program (see Table 1-4). Although this decline is substantial, on average, the increase in revenues from consolidation (i.e., increase in average vessel harvest) more than compensated for additional deductions, charges, and decrease share percentages. In general, this additional compensation came at the cost of greater crew efforts harvesting those additional pounds. Even in 2006, when Bering Sea *C. opilio* prices were particularly low, the average crew earned substantially greater compensation than in the years preceding rationalization, with the exception of 1998, when harvests from the Bering Sea *C. opilio* fishery were substantially greater than for any other year for which data are available. Although data for these vessels suggest total annual crew compensation on each vessel has increased, a progressive decline in the crew share percentages from approximately 24 percent of gross revenues in the first full calendar year of the program to slightly less than 21 percent in the fourth calendar year is also evident. The long run effect of this trend is uncertain.

**Table 1-4. Harvest, captain pay, crew pay, and percentage of gross vessel revenues paid to crew by vessels participating in both the Bristol Bay red king crab and Bering Sea *C. opilio* fisheries (1998, 2001, 2004, 2006-2009).**

Year	Number of vessels	Vessel revenues		Captain pay		Crew pay (excluding captain)		Percent of gross to crew (including captain)	
		Mean	Median	Mean	Median	Mean	Median	Mean	Median
1998	151	1,034,471	983,861	123,019	116,947	249,953	232,979	35.9	35.3
2001	143	435,583	369,474	50,310	43,426	97,279	87,042	34.1	34.3
2004	162	620,513	583,453	72,301	69,625	148,010	135,224	35.7	35.5
2006	56	1,367,208	1,244,964	98,025	96,090	195,317	185,298	24.0	24.2
2007	55	2,210,463	1,958,662	144,081	145,564	300,238	283,862	23.0	22.4
2008	61	2,729,428	2,646,745	179,973	176,911	385,464	365,392	22.6	22.4
2009	57	2,256,501	2,090,932	141,269	138,993	308,668	272,565	21.5	20.9

Source: Crab Economic Data Reporting.

Notes: 2005 omitted, as Bering Sea *C. opilio* fishery prosecuted as limited entry derby and Bristol Bay red king crab prosecuted as share-based fishery. Excludes any vessels on which crew were paid in excess of 75 percent of the vessel's gross revenues. Adjusted for inflation using CPI-U to 2009 dollars.

Most vessel owners assert that the decline in crew shares as a percentage of gross revenues is simply a reflect the change in vessel owner net revenues arising from the costly acquisition of shares to harvest. Many crew are said to have received full crew share on IFQ initially allocated to the vessel owner; however, in some cases vessel owners are reported to deduct IFQ value from revenues prior to paying crew, even for shares received in the initial allocation. Changes in crew compensation relative to pounds harvested by a vessel reinforce the conclusion that quota costs are a major contributor to declines in the percentage of gross vessel revenues paid to crew.

An additional factor to consider in assessing crew compensation under the rationalization program is the change in daily compensation. If only fishing, transiting, and offloading days are considered, crew appear to suffered a decline in daily compensation under the rationalization program; however, such an approach assumes that crew work no additional days in preparation for a season or at the end of a season. If each crewmember is assumed to work an additional 10 days on the vessel and gear, the conclusion is far less clear, with crew daily compensation in a similar range to prerationalization daily pay. This relative equivalence (or ambiguity) arises from several competing effects. Prior to the program, crews spent few days fishing, so days spent on vessel and gear work made up a greater share of their time. Since the program was implemented, vessels have stacked substantially greater catches on the remaining active vessels increasing the revenue base on the average vessel. These two factors, on average, counterbalance the effect of quota royalties (or the reduced share of gross revenues paid to crew) that has diminished crew pay.

#### **The processing sector**

Prior to implementation of the rationalization program, processor entry to the crab fisheries was not subject to limit. With the implementation of the rationalization program, participation in program fisheries by processors is limited by PQS and IPQ allocations yielded annually by those PQS. Initial allocations of processor quota shares were substantially more concentrated than harvester quota share allocations under the program because fewer processors than vessels were active in the fisheries during the qualifying period. As in the harvest sector, concentration of initial allocations of processing privileges varied across fisheries. The Aleutian Islands fisheries, which had the least participation during the qualifying period, were the most concentrated. The Bristol Bay red king crab, Bering Sea *C. opilio*, and Bering Sea *C. bairdi* fisheries, which had the most participants during the qualifying period, were the least concentrated. The regional distribution of shares differed with landing patterns that arose from the geographic distribution of fishing grounds and processing activities. In the Pribilof red and blue king crab fisheries, most historic processing occurred in the Pribilofs, resulting in over two-thirds of the processing allocations in those fisheries being designated for processing in the North region. Most processing in the St. Matthew Island blue king crab fishery occurred on floating processors near the fishing grounds in the North region. The Bering Sea *C. opilio* fishery allocations are split almost evenly between the North and South regions; while less than 5 percent of the Bristol Bay red king crab PQS is designated for North processing. All qualifying processing in the Eastern Aleutian Island golden king crab fishery occurred in the South region, resulting in all processing shares in that fishery (and in the Western Aleutian Islands red king crab fishery, which was based on the same history) being designated for processing in the South region. All processing allocations Western Aleutian Islands golden king crab fishery were split evenly with half required to be processed in the West region and half undesignated, which can be processed anywhere. Bering Sea *C. bairdi* processing shares are also undesignated.

During the first five years of the program, transfers of PQS total over 20 percent the PQS pool in 5 fisheries and over 50 percent of the pool in one fishery. As with harvester shares, the extent to which these transfers represent actual market transfers is uncertain, as some restructuring of processing interests occurred. In addition to the transfers of PQS, substantial leases of annual quota (IPQ transfers) occurred in the first five years of the program. In most fisheries, between 20 percent and 35 percent of the IPQ are transferred annually. As with PQS transfers, in some cases, these leases represent shifting of shares

within a corporate structure that may not reflect a true lease; yet, true leasing of interests occurred. Despite the number of transfers, PQS holdings are currently only slightly more concentrated than at the time of the initial allocation.

In the years leading up to the rationalization program, 20 or fewer processors participated in the largest crab fisheries. The largest three processors in these fisheries processed less than 15 percent of the fisheries' landings in each year. Processing distributions by community show that Dutch Harbor shore plants attracted a majority of landings in the Bristol Bay red king crab fishery and slightly less than a majority in the Bering Sea *C. opilio*. The remainder of landings was divided primarily among Akutan and St. Paul and floaters in the Bering Sea and King Cove and Kodiak on the Gulf. In the two Aleutian Islands golden king crab fisheries, participation fluctuated between 2 and 7 processors during the years leading up to implementation of the program. Dutch Harbor and Adak supported virtually all of the processing in those fisheries.

Under the rationalization program, a large portion of the processing (and raw crab purchasing) is vested in the holders of processing shares. To achieve efficiencies in processing, holders of processor shares have used custom processing arrangements to process substantial portions of the landings in the fisheries. Under these arrangements, a share holder contracts for the processing of landings of crab, while retaining all interests and obligations associated with the landed and processed crab. Because of the prevalence of these arrangements, both plant activities and buyer activities must be considered. Since the rationalization program, the number of processing plants participating in the Bristol Bay red king crab fisheries and the Bering Sea *C. opilio* fisheries have declined to approximately 10. The average processing by the top 3 plants in both fisheries increased to approximately 20 percent of the fishery. Ten or fewer plants participated in processing in the Bering Sea *C. bairdi* fisheries in each year of the program, with processing slightly more concentrated than in the two largest fisheries. Five or fewer processors participated in the Eastern Aleutian Island golden king crab and Western Aleutian Island golden king crab fisheries in the first five years of the program, limiting the information that may be released concerning processing in those fisheries. Only two plants participated in the St. Matthew Island blue king crab fishery in the one year that fishery was open since implementation of the program. These last three fisheries have relatively small TACs which limit processing opportunities.

In the first two years of the program, a large portion of the IPQ pool was subject to the "cooling off" provision, which required processing to occur in the community of the processing history that led to the allocation of the underlying PQS. Consequently, few changes in the distribution of processing of Class A IFQ/IPQ landings occurred in the first two years of the program. Also, entities representing the community in which processing occurred historically are granted a right of first refusal on certain transfers of the PQS and IPQ for use outside the community. This right is relatively weak because intra-company transfers are exempt from the right and the right lapses, if the IPQ are used outside of the community for a period of years. Limited information is available concerning the lapse of rights of first refusal, as no obligation to report a lapse exists. To date, rights of first refusal on PQS are believed to have lapsed in only a few instances (see Table 1-5). Most notably, the right has lapsed with respect to the shares arising from historic processing in St. George. The St. George harbor and its entrance were damaged by a storm in 2004. In the first two years of the program, that damage was found to have prevented processing in St. George. As a consequence, under the terms specified by the rationalization program the rights of first refusal would have lapsed. However, representatives of Aleutian Pribilof Island Community Development Association, the holder of the right, reached agreements with holders of these PQS to protect the interests of St. George. In another case, PQS were acquired by that right holder. In addition, the holder of the rights on behalf of the City of Kodiak and Kodiak Island borough has also acquired PQS through a negotiated arrangement with original holder of those PQS. In at least one other case, a right holder has consented to an acquisition of PQS by another entity despite its right.

**Table 1-5 Initial and current distribution of rights of first refusal by community.**

Fishery	Region	Right of first refusal boundary	Percentage of initial PQS pool	Percentage of current PQS pool
Bristol Bay red king crab	North	None	0.0	0.0
		St. Paul	2.5	2.5
	South	Akutan	19.7	19.7
		False Pass	3.7	3.7
		King Cove	12.7	7.4
		Kodiak	3.8	0.2
		None	3.4	12.2
		Unalaska	50.7	50.7
Bering Sea <i>C. opilio</i>	North	None	1.0	16.0
		St. George	9.7	0.0
		St. Paul	36.3	30.9
	South	Akutan	9.7	9.7
		King Cove	6.3	6.3
		Kodiak	0.1	0.0
		None	1.8	2.0
		Unalaska	35.0	35.0
Eastern Aleutian Island golden king crab	South	Akutan	1.0	1.0
		None	0.9	7.8
		Unalaska	98.1	91.2
Pribilof red and blue king crab	North	None	0.3	0.3
		St. George	2.5	0.0
		St. Paul	64.8	67.3
	South	Akutan	1.2	1.2
		King Cove	3.8	3.8
		Kodiak	2.9	2.9
		Unalaska	24.6	24.6
St. Matthew Island blue king crab	North	None	64.6	64.6
		St. Paul	13.8	13.8
	South	Akutan	2.7	2.7
		King Cove	1.3	1.3
		None	0.0	0.0
		Unalaska	17.6	17.6

Source: RAM PQS data, 2009-2010

Despite the end of the cooling off period and the ease with which the right of first refusal may be avoided, a large share of the processing of IPQ landings are believed to have continued to be made in the community benefiting from the right. Three factors likely contribute to this distribution of processing. First, in many cases, the shore-based processing capital used to develop the history leading the PQS allocation continues to be used for processing in by the initial recipient of the PQS allocation. The regionalization of PQS strictly limits the movement of processing across regional boundaries. In addition, to date, most processors have acknowledged a community interest in processing of landings using their IPQ, and report that they have continued to process those landings in the community of origin. Whether this acknowledgement of community interests will persist is not known.

Little information concerning the extent of processing in specific communities can be released because of the limited number of processors that participate in the crab fisheries. No clear trend is apparent in the landings of Class B IFQ and C share IFQ in the Bristol Bay red king crab fishery, as landings in Dutch Harbor and Akutan (communities associated with approximately 65 percent of the Class A IFA) have fluctuated between landings have between approximately 60 percent and approximately 85 percent of the annual landings of those shares in the first 5 years of the program. Those two communities, however,

have attracted between 65 percent and 90 percent of the annual Class B IFQ and C share IFQ landings in each of the first five years of the program (well in excess of the approximately 45 percent of the Class A IFQ associated with those communities on the initial allocation.

As with harvesters one of the primary changes in operations under the rationalization program is the distribution of landings among processors and throughout the season. Prior to the rationalization program in the two largest fisheries, deliveries were concentrated in very short periods – typically one week or less in the Bristol Bay red king crab fishery and fewer than 20 days in the Bering Sea *C. opilio* fishery. Under the rationalization program landings are distributed over a substantially longer time period. In the Bristol Bay red king crab fishery, most landings continue to be concentrated in a relatively short period in the fall; however, the processing season is several weeks long. In the North region of the Bering Sea *C. opilio* fishery, the days between a processor's first and last deliveries has fluctuated since implementation of the program. From the outset, processors operating in the North expressed a strong preference for concentrating deliveries in a short period of time, but several factors, including general lack of familiarity with use of cooperative fishing practices, ice in the vicinity of plants, and a fire at one plant have contributed to extending processing over a period of between two and three months. In the fifth year, harvesters made a coordinated effort to complete landings in the North region early in the season, resulting in processing being completed in one and one-half months. In the South region in the Bering Sea *C. opilio* fishery, landings were distributed across a noticeably longer period, when compared to prerationalization years. This distribution of landings over time is less costly to South region processors, which process landings from groundfish fisheries (i.e., pollock and cod) during the *C. opilio* season. In the Eastern Aleutian Islands golden king crab fishery in the first five years of the program, processors generally distributed their processing over a period of between two and three months. Since most of the processors in this fishery also participate in the groundfish fisheries, the distribution of landings across a greater period of time is of less importance. The average days between first and last delivery in the Western Aleutian Islands golden king crab fishery differs year to year since the rationalization program was implemented. To a large extent, this extended period has arisen from circumstances related to operations at the Adak plant, the only plant operating in the West region in four of the first five years of the program. Its operator held little IPQ, and often had protracted negotiations for custom processing and leasing arrangements. In the fifth year, the operator of the plant declared bankruptcy and was unable to process any landings from the fishery. NOAA Fisheries adopted an emergency rule (after receiving a recommendation from the Council) allowing an exemption from the West region landing requirement for all shares in the fishery. Subsequently, the Council adopted an amendment that would allow for an exemption on the agreement of QS holders, PQS holders, and the communities of Adak and Atka.

Clearly, the largest effect of the program on processing operations has arisen from the extended seasons in the fisheries. In some cases (particularly in the South region), processors have operated fewer crab lines and reduced peak operating crews. Use of fewer lines reduces both labor and capital costs associated with opening, configuring, and maintaining lines. Reductions in peak crews allow processors to save on transportation costs associated with bringing in crew for the short crab seasons. In some instances, savings on overtime labor may also be realized. In the North region, these savings are less available as plants in that area typically process only crab during the periods when the crab fisheries are open. In North plants, concentrating processing activity into a short period is needed to achieve efficiencies. With processing consolidated in fewer plants, the processing season is substantially longer, but operations are conducted in a manner similar to before implementation of the program.

Scheduling deliveries around available processing windows is critical to processor efficiencies. The importance and the success of processors in scheduling deliveries have varied across time, location, and fisheries. At times in the first year of the program, harvester/processor relationships were particularly strained by attempts of both sectors to dictate scheduling of deliveries. Although some conflicts have continued to arise, most delivery scheduling issues have been resolved to the satisfaction of both parties.

In the case of processors in the North region, scheduling of deliveries is critical to maintaining processing efficiencies under the program. Harvesters are generally sensitive to these circumstances and put some effort into cooperating with processors' operational schedules. In the 2009-2010 season, harvesters put substantial effort into coordinating landings in the North region soon after the New Year. Although this effort was primarily motivated by a desire to use the North region IFQ prior to ice conditions developing in vicinity of St. Paul, North region processors benefited from the consolidation of landings that reduced down times for processing crews. Processors in the South have more latitude to move labor among crab and groundfish species production. Despite this greater flexibility, delivery scheduling occasionally causes tension between the sectors.

The lengthening of seasons and greater distribution of landings across those seasons has reduced peak staff levels in plants in the South during the Bristol Bay red king crab and Bering Sea *C. opilio* processing seasons. Although these changes in delivery patterns, at times, mean less overtime for staff, in some instances, they may allow longer term employment, particularly for crews that work in both groundfish and crab fisheries. In addition, processors may be able to secure better trained or more suitable crews, as short term employment requirements decline. These changes can improve safety and performance in plants. In the North region of the Bering Sea *C. opilio* fishery, processing patterns have changed under the extended seasons, but processing labor works under terms and conditions similar to those prior to rationalization. Processors attempt to concentrate deliveries to achieve efficiencies. This scheduling means plants operate at set capacity for a period of time with employees working relatively long hours and earning substantial overtime pay. Although the seasons last a few months (as opposed to a few weeks) work is short term with all employees brought in exclusively for the crab season. In some cases, these employees are relatively long term employees of the processor who work in other plants. In others, they are short term employees hired exclusively for crab processing. In the other program fisheries, most processing is done by crews that work in both groundfish and crab fisheries, with crews shifting among different species production as demands arise. These crews tend to be longer term employees, working several months for the processor. The change to rationalization has had little effect on processing workers active in these fisheries, but to the extent that rationalization has allowed fisheries to be prosecuted that might otherwise have been closed (e.g., the two Bering Sea *C. bairdi* fisheries) processing workers have benefited from additional employment.

#### **CDQ group and Adak community group participation in program fisheries**

Community development quota (CDQ) groups and the community group representing Adak annually receive 10 percent of the TAC of each of the program fisheries prior to allocations being made under the program. Both before and after implementation of the rationalization program, CDQ groups made substantial investments in the program fisheries. Three CDQ groups hold PQS directly. CDQ groups and the Adak community group have acquired PQS interests recently and may also have indirect holdings of PQS. Share holdings of these groups vary by fishery, with the most substantial holding in the Western Aleutian Island golden king crab fishery, where a single group holds almost 30 percent of the PQS. Five of the six CDQ groups had direct holdings of QS during the 2009-2010 season and the sixth has indirect holdings through partnerships and joint ventures. Others are also known to have indirect holdings. Direct holdings alone show that CDQ groups have substantial interests in most program fisheries. The Adak community group has no direct QS holdings in the program fisheries. CDQ holdings are greatest in the Eastern Aleutian Islands golden king crab fisheries, in which CDQ interests are approximately 30 percent of the QS. CDQ groups also directly hold in excess of 10 percent of the QS in both of the major fisheries (the Bristol Bay red king crab and the Bering Sea *C. opilio* fishery).

CDQ groups may, and do, harvest their allocations using vessels of both operation types (catcher vessel and catcher processor). In addition, CDQ groups have integrated harvest of their allocations with program fishery allocations. In the Bristol Bay red king crab fishery, the portion of the annual CDQ harvests landed with harvests from the program fishery allocations has fluctuated between approximately 15

percent and almost 70 percent. In the Bering Sea *C. opilio* fishery, between 25 and 40 percent of the annual CDQ harvests are landed with harvests from the program fisheries. In the other program fisheries, much of the CDQ landings data cannot be revealed because of confidentiality limitations.

#### **Ex vessel prices and terms of delivery**

Ex vessel pricing structures have changed under the rationalization program. To assess how changes in pricing structure have affected negotiations and pricing, the section begins with a brief discussion of pre-rationalization delivery terms (including ex vessel pricing). After that discussion, this section describes delivery terms under the rationalization program, including those terms for Class A IFQ landings and Class B and C share IFQ landings.

In the years leading up to implementation of the rationalization program, harvesters in the Bristol Bay red king crab and Bering Sea *C. opilio* fisheries coordinated most price negotiations. The Alaska Marketing Association (AMA), a harvester organization, would solicit price offers from each processor until a price offer acceptable to its members was received. Since deliveries were unrestricted, once an acceptable offer was received from a processor all other processors usually matched that offer in order to maintain market share. Prices generally remained constant over the short seasons, with minor variations across processors to create incentives for deliveries. Historically, the Aleutian Island golden king crab fisheries had longer seasons and far fewer participants than the Bristol Bay red king crab and Bering Sea *C. opilio* fisheries. Traditionally, harvesters in these fisheries negotiated prices independently with some price variation throughout the season.

Several aspects of the structure of the program have affected delivery terms and pricing under the program. The different catcher vessel IFQ types (Class A IFQ v. Class B and C share IFQ) may bring different prices because of the different limitations on use of those shares and the effects of the arbitration program on Class A IFQ landing prices. The arbitration system serves several important purposes in the program, including dissemination of market information to facilitate negotiations, the coordination of matching Class A IFQ held by harvesters to IPQ held by processors, and a binding arbitration process to resolve terms of delivery. The arbitration process begins with the two sectors (harvesters and processors) jointly selecting a "market analyst," who produces a market report, a "formula arbitrator," who develops a price formula specifying an ex vessel price as a portion of the first wholesale price, and a pool of "contract arbitrators," who preside over any binding arbitration proceedings. Neither the market report nor the formula price has any binding effect. Rather, they are intended to provide baseline information concerning the market and a signal of a reasonable price.

To ensure predictability and fairness, the arbitration system sets forth standards to be followed by formula arbitrators and contract arbitrators. As set out, the standards applicable to the two different arbitrators are both intended to "establish a price that preserves the historical division of revenues in the fishery" while considering several factors. The findings of both arbitrators should be based on the historical division of "first wholesale revenues between fishermen and processors in the aggregate based on arm's length first wholesale prices and ex-vessel prices, taking into consideration the size of the harvest each year." Within the context of this primary standard, the arbitrator is directed to take into account the listed factors (which include product developments, quality, delivery timing, operational efficiencies, and financial stability).

The price formula, in part through its effects on binding arbitration proceedings, has largely driven the pricing of Class A IFQ landings in the fishery. Since 90 percent of the annual owner IFQ allocation (or approximately 87 percent of the annual catcher vessel allocation of IFQ) is made up of Class A IFQ, the distribution of benefits between harvesters and processors under the rationalization program has in large part depended on the distribution of benefits from landings of Class A IFQ

Data distinguishing ex vessel prices by IFQ type, as well as anecdotal evidence, suggest that harvesters have been able to gain a premium on landings of Class B and C share IFQ catch over landings Class A IFQ catch. These premiums vary across participants and time, averaging between 5 cents and 10 cents per pound. Premiums are thought to fluctuate with market conditions, which vary within and across years. When crab product markets are particularly weak, processors are thought to be generally less willing to buy crab to add to existing inventories. In addition to anecdotal and collected price information, other sources of evidence suggest that harvesters have developed competition for Class B and C share IFQ landings. In many cases, harvesters have been able to make deliveries of crab harvested exclusively with Class B and C share IFQ. In addition, buyers of Class B and C share IFQ catches and the extent to which buyers purchase larger portions of the Class B and C share IFQ catches than Class A IFQ catches suggest that some processors are competing for landings of Class B and C share IFQ catch.

### **Production from the fisheries**

One of the goals of the crab rationalization program is to increase the value of production from the fisheries. Some product development has occurred since the program began. A few processors and brokers have attempted to develop live and fresh crab markets in the U.S. and abroad. Processors, including catcher processors, have also produced more whole frozen crab, a small but possibly growing market. In addition, at least one processor has processed crab by breaking down sections into single legs prior to cooking to increase value and recovery. These market developments have generally focused on red king crab, the crab that is best suitable for development of new high-end markets. While these attempts to develop new markets are encouraging to some observers, overall the progress in market development has been slower than in most fisheries undergoing rationalization.

A few characteristics of the Bering Sea and Aleutian Islands crab fisheries have likely slowed product innovation. First, the requirement that all crab harvested in BSAI fisheries be processed live was in effect before the rationalization program began; consequently, the opportunities to make product quality improvements were less than those commonly observed in the transition to share-based management in other fisheries. Secondly, the distance to markets and less reliable air service in remote processing locations pose challenges to processors attempting to innovate with products with relatively short shelf lives, such as live crab and fresh crab. Thirdly, development of new product forms, such as more heavily processed products, may require significant outlay of capital or increases in labor, which may be more costly in remote Alaska communities where most of the crab from program fisheries is processed. Finally, the recent market price for shellfish sections has been so high that processors may have little incentive to produce anything else. The higher price received for value added products, such as meat, may not offset the yield loss of those products. In addition to fishery-specific factors that may hinder product developments, those developments may be constrained by certain aspects of the arbitration program.

### **Entry opportunities**

Entry into the fisheries under the LLP occurred primarily in two ways. Some persons with access to considerable capital were able to enter through the purchase of an LLP license and vessel. The nature of the fisheries increased the risk associated with entry. In brief derby seasons of a few days or weeks, poor catch rates and vessel breakdowns could result in no or little revenues for the season. New entrants dependent on revenues from the fisheries for their vessel payments faced greater risks under this derby management as they competed with others for a share of the GHL.

An alternative method of entry was open to some captains and crew in the fisheries. The typical progression in the fisheries was for crewmembers to work their way up to become skippers. With most vessels employing approximately 5 deck crew, the opportunity for advancement to skipper was limited. Some long term captains who sought to enter the fisheries were able to convince the vessel owner/license holders they worked for to sell them an interest in the operation. Persons entering the fishery in this manner typically had strong long term relationships with their employers (i.e., the vessel owners) and

shared in the oversight of annual maintenance and upkeep of the vessel. This progression from skipper to vessel owner was available only to a few skippers, who had strong relationships with a vessel owner who was interested in sharing an interest in the vessel.

Since the crab fisheries were greatly overcapitalized on implementation of the rationalization program, any absence of entry to the fisheries to date should be fully expected. The restructuring of harvest privileges under the rationalization program has changed the nature of entry opportunities substantially. Entry can occur through the purchase of harvesting QS without ownership of an interest in a vessel or a supporting license. Annual IFQs can then be fished liberally through leasing arrangements. Since QS are divisible, gradual entry into the program fisheries is permitted. The cost of entry is determined by QS prices, which depend on TACs, crab markets and other factors.

The market for crab QS has tended to be less fluid than that for sablefish or halibut QS because crab QS holdings are more concentrated with a relatively smaller number of known participants in the market. Since much of the share concentration resulted from the initial allocation of QS, the thin market is largely a reflection of the historic distribution of interests in the fisheries. The more industrial nature of the fishery, with larger investments in vessels, has also contributed to concentration of interests. With this concentration, few transactions take place and most transactions for owner QS have tended to be large, requiring substantial access to capital. Until the most recent year, the annual average priced transaction for owner QS (based on available price information and the average transfer size) exceeded \$300,000 in the Bering Sea *C. opilio* fishery and the Bristol Bay red king crab fishery. While full scale entry requires ownership of a vessel in addition to quota acquisition, cooperative harvest of IFQ and leasing create an opportunity for a more gradual entry without a vessel. This method of entry has created greater entry opportunities than existed under LLP management. Alternatively, the separation of accessible harvest privileges from vessel ownership allows persons to enter by purchasing a vessel without QS. Through the leasing market such a person can access IFQ without substantial QS holdings; however, such an approach to entry to the fishery is relatively high risk and may have little return.

C share QS, which make up 3 percent of the total QS pool, have also opened new avenues for small scale entry by eligible crew. C share QS typically sell for less than owner QS, in part, because of the active participant requirements applicable to C shares. The relatively low caps on C share QS holdings and the small percentage of the total harvest share allocation made up of C shares limit the ability of persons to consolidate large C share QS holdings. As a result, C share transfers must be of relatively small amounts of QS, which are likely to be more affordable, particularly to crew, who may have less access to capital. Available transfer information from the first five years of the program suggests that the average transfer in each fishery is for approximately one-hundredth of the QS pool and is valued at less than \$50,000.

Unlike the harvest sector, entry to the processing sector was not limited under the LLP. As a result, processor participation fluctuated greatly in the years leading up to the implementation of the rationalization program. In the early 1990s, more than 50 processors operated in the Bristol Bay red king crab and Bering Sea *C. opilio* fisheries. Under lower GHIs in the late 1990s and early 2000s, processing participation dropped to fewer than 20 plants in those fisheries.

Both prior to and since implementation of the rationalization program, entry to the processing sector as only a crab processor was very challenging. Processors that also process groundfish are able to keep plants operating for a greater period of time, spreading capital costs across larger scale production. Consequently, entry to the processing sector is affected by a processor's potential to enter groundfish fisheries and secure a portion of that production. With groundfish processing fully capitalized, entry opportunities in the crab processing sector are also limited. In addition, to the extent that other management programs (such as the AFA Bering Sea pollock cooperative program, Bering Sea and Aleutian Island cod sector allocations, and the Amendment 80 cooperative program) directly or indirectly

limit the ability of processors to enter those fisheries, entry to the crab fisheries is more constrained, regardless of the limits on entry created by the crab management program. Share holdings data suggest that a few processors have entered the fisheries, since implementation of the program, in some cases with development of substantial holdings. In at least one case, the entrant has not processed landings directly, the lease of those shares has supported processing by an entering processing platform.

### **Management and enforcement**

The system of share-based fishing established by the program includes several fishing privileges and obligations that must be overseen by NOAA Fisheries managers and enforcement agents. These requirements present extensive and unique challenges to NOAA Fisheries Restricted Access Management and Office of Law Enforcement. The several sets of accounts authorizing fishing and processing activities must be monitored. Using plant observers and electronic reporting, landings can be attributed to the appropriate accounts. Overall, managers and enforcement believe that fishing and processing activities are in compliance with the allocation of privileges for those activities as intended by the program.

Some aspects of the program have effectively created systems of self monitoring that have relieved monitoring and enforcement burdens. The arbitration system is administered through a series of contracts that are subject to civil enforcement by the participants in that system. The system of harvest cooperatives has also reduced monitoring burdens by consolidating annual IFQ allocations into fewer accounts, effectively shifting a portion of the oversight of those accounts to harvest sector share holders.

Under the Council motion adopting the program, NOAA Fisheries collects fees to pay for the costs of management (including enforcement) arising out of the program. These costs are the incremental costs that are incurred due to the implementation of the program. The fee is split equally between harvesters and processors, with processors responsible for collecting the fee and making payment to NOAA Fisheries. Catcher processors, who catch and process their catch, pay the full amount. Fees are limited to no more than 3 percent of the ex vessel value of the fishery in a crab fishing year. Although NOAA Fisheries cannot adjust the fee percentage at the end of a season, regulations require that any debit or credit to the fee collection account must be carried forward and applied toward the fee percentage calculations for future years. In some years, fee collection has exceeded costs, allowing, NOAA Fisheries to reduce the fee percentage below 3 percent and even and remove the fee in its entirety in one year.

### **Fishing vessel safety**

Historically, the BSAI crab fisheries have been considered to be the most dangerous in Alaska, especially those crab fisheries that take place in the winter months where cold temperatures, high winds, poor weather, icing conditions and high seas have been contributing factors to crew and vessel losses. The combination of environmental conditions, onboard stowage of crab gear and launching and retrieving of the gear, and minimal safety regime create numerous safety hazards for this fleet. In addition to the safety issues inherent with operations, fleet economics and fishery resource management issues also created safety concerns. Throughout the 1990s, a major fisheries management problem with the Bering Sea crab fleet was that despite efforts to limit overcapacity through the LLP, the catching power within the fleet greatly exceeded the available amount of crab, resulting in an extremely competitive "race for fish" in what was already a high-risk operating environment. From August 1990 through March 1999, 73 people died in the BSAI crab fisheries as a result of capsizing, sinking, man overboard (MOB), and industrial accidents, such as being struck or crushed by crab pots. When taking into account changes in workforce size, variations in season length and number of vessels participating in the fishery, workers participating in BSAI crab fisheries were experiencing an astronomical fatality rate of 770 fatalities per 100,000 full time fishermen.

In 1999, the safety program developed for the BSAI crab fleet, known as the “At the Dock Stability and Safety Compliance Check” (SSCC) was established. Under the program, the USCG reviewed vessel loading and stability issues with the master and checked for overloading. Vessels found to be without stability reports, overloaded, or having missing, outdated, or inoperable primary life saving equipment (i.e. immersion suits, liferafts, EPIRBs) would be issued captain of the port orders and not allowed to get underway until the safety discrepancy was corrected. From October 1999 through January 2005, SSCCs identified 1 or 2 crab vessels every season that were improperly loaded and required those vessels to reduce the number of pots on board. Additionally, compliance checks found a significant number of vessels with outdated or improperly installed primary life saving equipment. Since the establishment of the SSCC, a total of ten lives have been lost, representing a significant improvement over the 1990 – 1999 time period, where the fleet lost an average of eight fishermen annually. Other changes that occurred prior to rationalization that lessen risk and improve safety include the pre-staging of helicopters during the two major crab seasons and the ability to delay openings up to 48 hours to allow bad weather pass if the USCG’s ability to conduct search and rescue missions are significantly impaired. In addition, starting in September 2005 (simultaneously with the rationalization program), vessels participating in the BSAI crab fisheries are now required to have a current and valid USCG safety decal before vessel registration is issued to participate in the fishery. However it is important to note that, a dockside exam does not focus on vessel seaworthiness but only on the required survival equipment on board the vessel. Vessel operators are also now required to call the USCG 24 hours prior to leaving port when carrying pot gear so that the USCG can confirm they have a decal and participated in the SSCC before they depart.

One of the primary arguments for the rationalization program was to improve safety of the fleet. Although fatalities of the BSAI crab fishery declined significantly since October 1999, prior to the implementation of the program, rationalization programs can improve operational safety through reducing risk. In the years leading up to the rationalization program, crews in the fisheries would actively fish crab for only a few days or weeks each year. Under the rationalization program, most crews are active in the crab fisheries for a period of months providing crew with more (and more regular) experience deploying and hauling gear. Maintaining a consistent crew better maintains vessel management, improves efficiency and safe operating procedures, crew become more familiar with the vessels operation, other crew, deck rotation. The extended seasons under the program also have allowed captains to slow fishing. Slowing down the pace allows for crew to get more (and more regular) rest than in the derby fishery. A less fatigued crew is less likely to have accidents. Anecdotally fishermen have said that they work fewer hours in a single day allowing for more time to sleep and they are not staying up 3 or 4 days straight.

Rationalization has led to a consolidation of the fishing fleet allowing for vessels that are more fully capable of operating in their chosen service of fishing in the Bering Sea in the winter. Prior to implementation, many vessels fished to maintain historic interests in the crab fisheries. The overall poor profitability of the highly capitalized fisheries with relatively low TACs may have economically forced some owners to postpone needed vessel maintenance. Fleet contraction resulted in the removal of many of these marginal vessels from the fleet. The consolidation of the fleet resulted in an increase in the average vessel size, as smaller vessels were disproportionately removed from the fisheries. Larger vessels lend themselves to a larger work platform and may be able to handle the weather conditions more easily and are more fully capable of operating in their chosen service.

The rationalization program has resulted in several improvements in efficiency that can allow for reduced risk in the fishery. For instance, individual allocations and spreading the season out allows more flexibility in choosing to stay in port if weather is predicted to be poor. Anecdotally fishermen say that they delay going out if the weather is bad. They are also more likely to suspend fishing on grounds during periods of bad weather. These secure fishing privileges, together with flexible transfer rules for cooperatives, are said by some participants to allow them to move vessels off the grounds when weather is turning bad. With the end to the race for fish, participants also put less emphasis on catching power,

reducing the incentive to overload vessels. Stability and safety compliance checks (which were performed on over 70 percent of the fleet in the years 2007 through 2009) found vessels were carrying fewer pots than their stability instructions allowed.

While the rationalization program has provided some opportunities for improved safety, some aspects of the fishery may continue to pose safety risks. Participants continue to desire to minimize days at sea to reduce operational costs. The work ethic of individuals who have been historically employed largely because of their ability to work fast for long periods of time persists. The effect of these factors on fishing practices may subside over time, but currently are still valued and exist within the fleet. In the first couple of years of the program, harvesters raised concerns that rigid delivery dates established by processors were resulting into a “race” to meet pre-established delivery schedules and in some cases were becoming a detriment to safety; however, over the last few years, efforts have been made by both harvesters and processors to address this issue. Regional landing requirements have also limited the flexibility of captains to take sea conditions into account when deciding where to deliver crab, particularly in the North region, where ice conditions are known to create a barrier to deliveries. This issue should be addressed through the development of a satisfactory provision for emergency relief from regionalization to alleviate risks associated with regional landing requirements.

The rationalization program has clearly demonstrated the ability to improve safety by making foundational changes which increase fishing time, reduce an emphasis on catching power, allow large, more efficient and safer vessels to remain in the fishery, and improve crew experience. These are areas that are typically difficult to control through Coast Guard safety regulations. In order to maintain the progress made in saving lives and reducing risk, hazards to the fleet must continue to be monitored and addressed. In addition, safety effects of the rationalization program should also continue to be monitored and addressed appropriately.

#### **Biological management issues**

Catch in excess of the harvest targets was difficult to prevent in the derby-style fisheries that predated the crab rationalization program. Even with good in-season assessment and catch reporting, catches can change rapidly. Since the implementation of the crab rationalization program, the total allowable catch (TAC) for these target fisheries has never been exceeded. Deadloss in the Bristol Bay red king crab and the Aleutian Islands golden king crab fisheries has decreased post-rationalization, compared to the seasons immediately preceding implementation of the program. In the Bering Sea *C. opilio* fishery, the rate of deadloss is comparable to that which occurred in the two most recent years before rationalization. In the first year of fishing after being closed for more than 10 years, deadloss in the St. Matthew Island blue king crab was slightly more than 2 percent of catch. Since deadloss is counted against IFQ allocations, this deadloss presents no biological risk.

High grading is the sorting through legal crab for the most valuable (typically the largest and cleanest) crab, and discard of the remaining legal crab to ensure that only the highest-priced portion of the catch is landed and counted against the IFQ. During the first year under rationalization in the Bristol Bay red king crab fishery, the number of legal male crabs captured during the fishery and subsequently discarded was dramatically higher than discard rates in previous years, and represented approximately 20 percent of legal male red king crab caught. ADF&G reacted to the 2005-2006 discard issue by downwardly adjusting the TAC determination for the 2006-2007 season, thus resulting in an economic penalty for the share holders in that season. In an effort to address the biological concerns harvesters, processors, and cooperative members agreed to improve retention of legal size crab to the level of the pre-rationalized fishery in the years 1999-2004, and to reduce bycatch of females and sublegal males. In addition, beginning in the 2006-2007 season, most harvesters and processors changed their pricing structure to reflect their support for a full retention policy, and moved to a single price that does not distinguish for shell condition, in order to remove the incentive to high grade. As discarding of legal males did not occur

on a similar scale in 2006-2007, no further downward adjustment was made for the 2007-2008 season (Vining and Zheng 2008). No adjustment has been made since. High grading and discard rates have not been an issue, other than the 2005-2006 Bristol Bay red king crab season.

Experimental studies have shown that longer soak times, in conjunction with the required pot escape mechanisms, are likely to increase the proportion of legal versus non-legal crabs caught in the fishery (Barnard and Pengilly 2006). Soak times in the Bristol Bay red king crab fishery and the Bering Sea *C. opilio* fisheries have lengthened since the program was implemented. Catch per unit effort have increased to some extent, but catches of sublegal and female catch under the rationalization program remain within the range of bycatch levels from previous years.

Mortality is also caused by ghost fishing of lost crab pots. Mortality of crab caused by ghost fishing is difficult to estimate with precision given existing information, but studies have shown that unbaited crab pots continue to catch crabs, and pots are subject to rebaiting due to capture of other fish and crab, until biodegradable mesh gives way. The impact of ghost fishing on crab stocks remains unknown. Pre-rationalization, it has been estimated that 10 percent to 20 percent of crab pots were lost each year, although lack of observer coverage precluded accurate recording. In the first five years of the program, estimates indicate that lost pots represent less than 5 percent of registered pots in the Bristol Bay red king crab, St. Matthew Island blue king crab, Aleutian Island golden king crab, and Bering Sea *C. opilio* fisheries. Pot losses have ranged from 6 percent and 14 percent of registered pots in the *C. bairdi* fishery. One factor that may affect the rate of lost gear in these latter fisheries is the longer fishing season. Longer soak times mean that the time between setting and retrieving the gear is extended, and combined with the three to four month season, increase the risk of a change in the weather and unforeseen encroachment of sea ice preventing the vessel from successfully retrieving its gear.

Discussion Paper  
Rights of first refusal  
Bering Sea and Aleutian Islands crab fisheries  
December 2011

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<sup>1</sup> corresponding to a portion of the harvest share pool. These processor shares were allocated to processors based on their respective processing histories. To protect community interests, holders of most processor shares were required to enter agreements granting community designated entities a right of first refusal on certain transfers of those shares. Since implementation, community representatives and fishery participants have suggested that some aspects of the rights of first refusal may inhibit their effectiveness in protecting community interests. To address these concerns, the Council developed an amendment package that included the following measures:

- 1) the lapse of the right after three consecutive years of use of the individual processing quota (IPQ) outside the community or if a community entity elects not to exercise the right on a transaction to which it applies;
- 2) the relatively short period of time allowed for exercising and performing under the right;
- 3) the requirement that the right apply to all assets involved in a transaction, which could include assets outside the community; and
- 4) the limited protection to community interests by the right of first refusal.

At its February 2011 meeting, the Council elected to delay further action on the package to allow stakeholders to work together to further develop acceptable solutions (including those under consideration in the amendment package) to issues with the rights of first refusal. The Council will consider suggestions of stakeholders to further this action at this meeting.

This paper includes the purpose and need statement and alternatives proposed by the Council for this action. In addition, the paper concludes with a brief discussion of notices and the lack of information concerning the state of rights of first refusal (including whether those rights have been triggered by a transfer or have lapsed under their terms). This discussion is included at the suggestion of stakeholders to facilitate the potential development of an alternative to address those information concerns.

### **Purpose and Need Statement**

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

*The Bering Sea/Aleutian Islands crab rationalization program recognizes the unique relationship between specific crab-dependent communities and their shore-based processors, and has addressed that codependence by establishing community “right of first refusal” agreements as a significant feature of the program. These right of first refusal agreements apply to the Processor Quota Shares initially issued within each community, and are entered into and held by Eligible Crab Community Organizations on behalf of each respective community.*

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<sup>1</sup> Processor shares include both Processor Quota Shares (PQS), which are long term privileges to receive annual allocations of Individual Processor Quota (IPQ), and IPQ. Annual IPQ are the specific poundage of crab landings authorized exclusively for the holder in that year.

*To date, there have been several significant Processor Quota Share transactions, resulting in Eligible Crab Community Organizations now owning between 20 percent and 50 percent of the PQS<sup>2</sup> in each rationalized fishery. However, the ability of the right of first refusal to lapse may diminish the intent to protect community interests. Also, limiting the time period to exercise the right may conflict with the ability to exercise and perform under the right of first refusal. In addition, some communities, when exercising the right of first refusal may have no interest in purchasing assets located in another community and feel the right of first refusal contract should exclude any such requirement.*

## **Alternatives**

The Council has identified the following three actions:

### **Action 1: Increase a right holding entity's time to exercise the right and perform as required.**

#### Alternative 1 – status quo

- 1) Maintain current period for exercising the right of first refusal at 60 days from receipt of the contract.
- 2) Maintain current period for performing under the right of first refusal contract at 120 days from receipt of the contract.

#### Alternative 2: Increase an entity's time to exercise the right and perform.

- 1) Require parties to rights of first refusal contracts to extend the period for exercising the right of first refusal from 60 days from receipt of the contract to 90 days from receipt of the contract.
- 2) Require parties to rights of first refusal contracts to extend the period for performing under the contract after exercising the right from 120 days from receipt of the contract to 150 days from receipt of the contract.

### **Action 2: Increase community protections by removing the ROFR lapse provisions.**

#### Alternative 1 – status quo

- 1) Maintain current provision under which the right lapses, if IPQ are used outside the community of the entity holding the right for three consecutive years.
- 2) Maintain current provision, which allows rights to lapse, if the PQS is sold in a sale subject to the right (and the entity holding the right fails to exercise the right).

#### Alternative 2 – Strengthen community protections under circumstances where ROFR may lapse.

Require parties to rights of first refusal contracts to remove the provision that rights lapse, if the IPQ are used outside the community for a period of three consecutive years.

Require that any person holding PQS that met landing thresholds qualifying a community entity for a right of first refusal on program implementation to maintain a contract providing that right at all times

### **Action 3: Apply the right to only PQS or PQS and assets in the subject community.**

<sup>2</sup> The Council should consider revising this clause to state that community organizations “hold substantial portions of the PQS in each rationalized fishery.” Although it is possible that organization holdings reach these levels in some fisheries, in some cases holdings are indirect. In addition, some organizations hold PQS on which they have never held a right of first refusal. Given these circumstances, the statement as written may not be fully accurate or may be misconstrued by readers. A more general statement may address these concerns.

Alternative 1 – status quo

The right of first refusal applies to all assets included in a sale of PQS subject to the right, with the price determined by the sale contract.

Alternative 2: Apply the right to only PQS.

Require parties to rights of first refusal contracts to provide that the right shall apply only to the PQS subject to the right of first refusal. In the event other assets are included in the proposed sale, the price of the PQS to which the right applies shall be determined by a) agreement of the parties or b) if the parties are unable to agree, an appraiser jointly selected by the PQS holder and the entity holding the right of first refusal.

For any transaction that includes only PQS, the community entity may request that an appraiser value the PQS. If the appraiser's valuation differs from that of the contract, the right of first refusal shall be at the price determined by the appraiser.

The appraiser shall establish a price that represents the fair market value of the PQS, but may adjust the price to address any diminishment in value of other assets included in the PQS transaction subject to the right.

Timeline for appraisal and performance<sup>3</sup>

From the date of receipt of the sale contract by the community entity:

Within:

10 days: community may request an appraiser

20 days: jointly selected assessor chosen, or if the parties do not agree on a single assessor, then each party chooses an assessor

40 days: if no single assessor is chosen, the two assessors will choose a third assessor

From the date of selection of the assessor (or assessors) by either method:

Within:

60 days: the assessor(s) establish a price

120 days: notification of community entity of intent to exercise ROFR

180 days: community representative must perform under the contract

The cost of the assessor will be paid equally by the PQS holder and the community entity. If a third assessor is chosen, the PQS holder and community entity will pay their chosen assessor and divide equally the cost of the third assessor.

**Action 4: Require community approval for IPQ subject to the right to be processed outside the subject community.**

Alternative 1 – Status quo

Intra-company transfers of PQS and IPQ outside the subject community are permitted without requiring the PQS holder to notify the community entity that holds the right.

Alternative 2 – Require community consent to move IPQ outside the community

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<sup>3</sup> Note that the timeline for the appraisal process is reformatted from the December 2010 motion for clarity. No substantive modifications were made.

Require the PQS holder to obtain written approval from the community prior to processing IPQ subject to the right (or formerly subject to the right), at a facility outside the subject community.

### **Discussion of notices and information under the right of first refusal**

As developed in regulation, rights of first refusal are administered through contractual arrangements between right holders and PQS holders. Contracts under the regulation should require the PQS holder to provide notice to the right holder of a transfer that triggers the right. Rights on PQS transfers are triggered by a transfer of PQS, unless the person acquiring the PQS enters a contract with the right holder perpetuating the right and agrees to use 80 percent of the PQS in the community in 2 of following 5 years. A right is triggered by a transfer of IPQ, if more than 20 percent of the PQS holder's community based IPQ (on a fishery by fishery basis) has been processed outside the community by another company in 3 of the preceding 5 years. In addition, rights lapse, if the IPQ are used outside of the community for a period of 3 consecutive years.

In addition, regulations include certain provisions intended to ensure that transferors and transferees comply with rights of first refusal obligations. Specifically, 680.41(i) provides, in part:

- (8) In the case of an application for transfer of PQS or IPQ for use outside an ECC that has designated an entity to represent it in exercise of ROFR under paragraph (l), the Regional Administrator will not act upon the application for a period of 10 days. At the end of that time period, the application will be approved pending meeting the criteria set forth in this paragraph (i).
- (9) In the case of an application for transfer of PQS for use within an ECC that has designated an entity to represent it in exercise of ROFR under paragraph (l), [t]he Regional Administrator will not approve the application unless either the ECC entity provides an affidavit to the Regional Administrator that the ECC wishes to permanently waive ROFR for the PQS or the proposed recipient of the PQS provides an affidavit affirming the completion of a contract for ROFR....

The first provision applies when the right would be triggered and is intended to provide a window of time for the right holder to act to prevent the transfer, if the right is to be exercised. The second provision applies when the right is not triggered and is intended to provide ensure that the right is maintained with the new PQS holder or is waived by the right holder.

Given the structure of the rights, it would be appropriate for right holders to ensure that their contracts include reporting by a PQS holder concerning the use of IPQ and any PQS and IPQ transfers. Yet, even if those reports are required by contract, the Council and NOAA Fisheries may have little or no information concerning the operation and effectiveness of rights. The Council could consider modifying reporting requirements to aid right holders in monitoring the use of shares subject to the right and improve information available to the Council for assessing the effects of the rights. If the Council wished to pursue additional reporting requirements, it could include an alternative in the amendment package to require PQS holders to provide the following notices:

- 1) To the right holder, a notice of all transfers of IPQ or PQS that are subject to the right (regardless of whether the PQS holder believes the right applies to the transfer) (*as a required contract provision*);
- 2) To NMFS as a part of any application to transfer PQS subject to the right to any party other than the right holder, either:

- a. A certification of the transferor of the PQS that the right holder was provided with 90 days notice of the right and did not exercise the right during that period (in which case the PQS may transfer and the right will no longer apply); or
  - b. A certification of the new PQS holder and the right holder that a contract has been entered establishing the right with respect to the new PQS holder or that the right holder has elected to waive the right with respect to the new holder.<sup>4</sup>
- 3) To NMFS, as a part of the annual application for IPQ (and copied to the right holder), a statement as to whether the right has lapsed as a result of use of the IPQ outside of the community for 3 consecutive years; and
  - 4) To the right holder annually, the location of use of IPQ that are subject to a right and whether the IPQ were processed by the PQS holder (*as a required contract provision*).

The first notice requirement would be used to ensure that right holders are informed concerning the holder of PQS that are subject to the right of first refusal. The second notice would be used to prevent transfers from being processed without either providing the right holder with notice that the right applies and adequate time for exercising or perpetuating the right. The third notice would ensure that NMFS has notice of whether the right has lapsed as a result of the shares being used outside the community. The last notice would provide the right holder with information for determining both whether the right has lapsed and whether the right applies to the transfer of IPQ.

The development of these notices is likely to be complicated by enforcement and confidentiality issues. Specifically, the Council and NMFS will need to consider whether delaying transfers and withholding IPQ issuances for failure to complete required notices is appropriate (or whether some other penalty is more appropriate). Confidentiality issues could also arise to the extent a notice requires a PQS holder or IPQ holder to reveal landings information. These issues will need to be explored should the Council wish to proceed with the development of some of these notice requirements.

---

<sup>4</sup> It should be noted that this second certification is similar to the existing requirement for transfers of shares for use inside the community.

**To: North Pacific Fisheries Management Council**

**Fax # 907-271-2817**

**From: Fish Heads, An Advocacy Group for Coastal Communities**

**Re: C-4 (a) BSAI Stakeholder reports (5 Year Review Issues)**

Thank you for continuing to examine the BSAI Crab rationalization program. We believe your focus on the three related issues: **excessive lease fees, crew compensation and active participation** is correctly aimed as you consider modifications to the program to ensure both the resource and our coastal communities remain healthy.

**To this end we suggest:**

1. A sunset date be imposed on non-participating owners after which they must divest to on board owners.
2. A minimum 25% of net profits to active on board fishermen.
3. A vessel cap be implemented to avoid overfishing in hot spots and unnatural fleet constriction.

Thank You

Terry Haines  
Executive Director  
Fish Heads



Steven K. Minor  
Executive Director

T 360-440-4737  
F 206-801-5803  
steve@wafro.com

November 28, 2011

Mr. Eric Olson  
Mr. Chris Oliver  
North Pacific Fishery Management Council

Re: Agenda Item C-4(b), Crab Program Binding Arbitration

Gentlemen,

The BSAI Crab Program Binding Arbitration system is not meeting Congressional and Council objectives; and has unfairly shifted almost all risks to the processing sector, and nearly all financial gains to the holders of QS/IFQ.

This is easily summarized by examining the share of quasi-rents under the current price formulas on page 2.

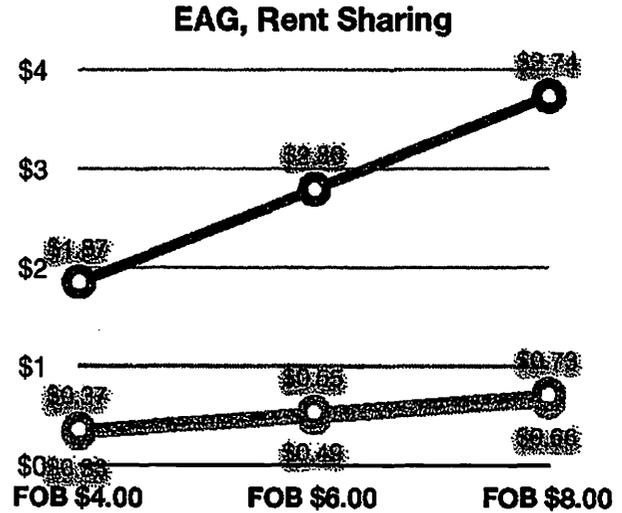
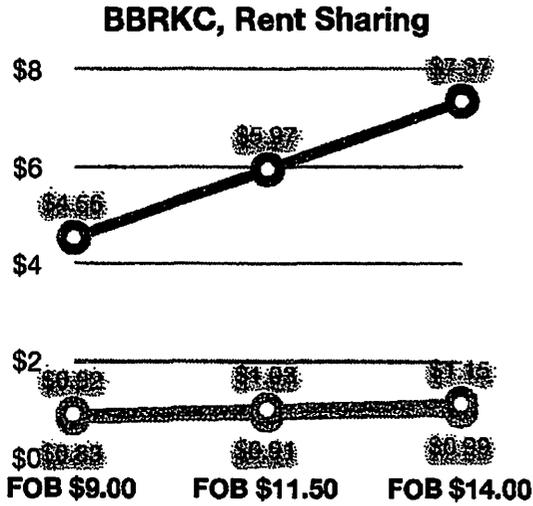
We believe there is an issue regarding the implementing regulations as they pertain to the arbitration system and lengthy season agreements ("LSA"). The current regulations allow for LSA to include arbitration proceedings any time during the "crab fishing year." That time frame allows for final price arbitrations to occur long after the subject crab has been harvested, processed and sold. That event was not contemplated by the Council and has resulted in unfair advantages to holders of arbitration individual fishing quota ("IFQ"). The more correct interpretation should have allowed LSA's to include dates for arbitrations to occur during the subject crab fishing "season."

Our analysis is included in a letter already submitted to NMFS, beginning on page 4. We request the Council to begin a regulatory amendment process to address this unintended inequity as soon as possible.

Sincerely,

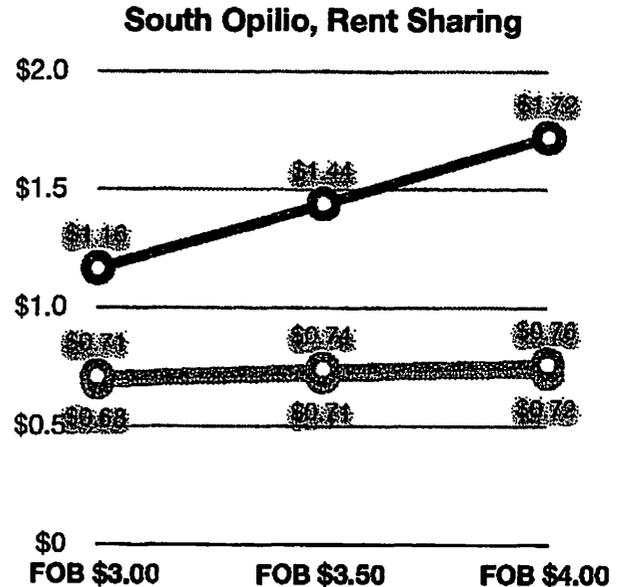
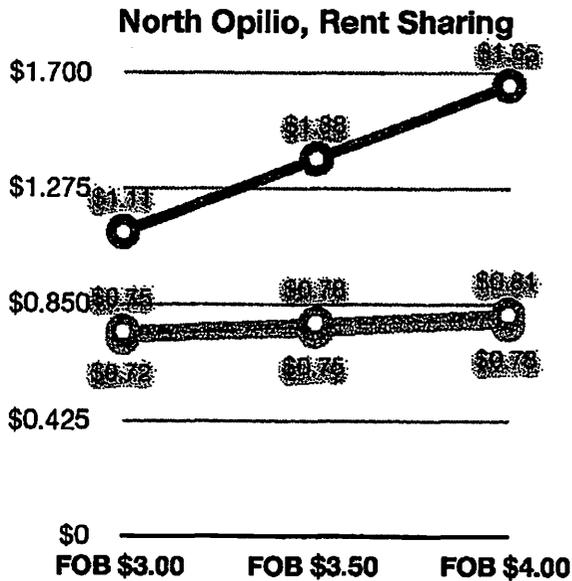
Steven K Minor

Price Formulas under the Current Binding Arbitration System



- Gross to Harvester, Round Pounds
- Gross to Shorebased Processor, Round
- Gross to Floating Processor, Round

- Gross to Harvester, Round Pounds
- Gross to Processor, Round
- Gross to Floating Processor, Round





1201 Third Avenue, Suite 4800  
Seattle, WA 98101-3099  
PHONE: 206.359.8000  
FAX: 206.359.9000  
www.perkinscoie.com

L. John Iani  
PHONE: (206) 359-6689  
FAX: (206) 359-7689  
EMAIL: JIani@perkinscoie.com

August 9, 2011

Mr. Glenn Merrill  
National Marine Fisheries Service  
Alaska Region  
Juneau, AK

**Re: Crab Rationalization-Lengthy Season Agreements**

Dear Glenn:

We are writing on behalf of the North Pacific Crab Association and have identified a problem with the regulations implementing the Crab Rationalization program as prescribed by the U.S. Congress and the North Pacific Fishery Management Council ("Council"). We believe there is an issue regarding the implementing regulations ("the regs") as they pertain to the arbitration system and lengthy season agreements ("LSA"). The current regulations allow for LSA to include arbitration proceedings any time during the "crab fishing year." That time frame allows for final price arbitrations to occur long after the subject crab has been harvested, processed and sold. That event was not contemplated by the Council and has resulted in unfair advantages to holders of arbitration individual fishing quota ("IFQ"). The more correct interpretation should have allowed LSA's to include dates for arbitrations to occur during the subject crab fishing "season."

The crab rationalization regulations provide for LSA's timing at section 680.20 (h)(3)(iii)(B) as follows:

(B) A Lengthy Season approach allows a committed IPQ holder and a committed Arbitration IFQ holder to agree to postpone negotiation of specific contract terms until a time during the crab fishing year as agreed upon by the Arbitration IFQ holder and IPQ holder participating in the negotiations. The Lengthy Season approach allows the Arbitration IFQ holders and IPQ holder involved in the negotiation to postpone Binding Arbitration, if necessary, until a time during the crab fishing year. If the parties reach a final agreement on the contract terms, Binding Arbitration is not necessary.

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Perkins Coie LLP

Mr. Glenn Merrill  
August 9, 2011  
Page 2

The inclusion of "crab fishing year" did not happen until the final rule was published. Allowing for the entire period encompassed by the crab fishing year has resulted in arbitration dates occurring long after the relevant IFQ and IPQ have been harvested, processed and sold into the market. That result has allowed the arbitration IFQ holder to assert price demands that unfairly subject the IPQ holder to changes in the market that occurred long after the subject crab was sold.

The use of "crab fishing year" in the final rule directly conflicts with the NMFS discussion of the final rule contained in the federal register. That discussion correctly states that the LSA approach at p. 10177 Fed. Reg. Volume 70, No. 40:

Arbitration System... (b) a lengthy season approach that allows parties to postpone binding arbitration until sometime during the season;...

"During the season" is the correct timing reference and is far different from the crab fishing year that is contained in the final rule. That seasonal time frame is also consistent with the NMFS response to comments which also preceded the publishing of the final rule. In response to Comment 139 contained on p. 10209 Fed Reg Volume 70, No. 40 NMFS clarified:

"NMFS is revising this portion of the regulations at Section 680.20(a)(3) to clarify that if Arbitration IFQ holders choose to use the Arbitration System, they may enter into open negotiation prior to, and during the crab fishing season...."

The "crab fishing year" is a defined term in section 680.2 Definitions:

Crab fishing year means the period of July 1 of one calendar year through June 30 of the following calendar year.

By including that defined term in the LSA timing regulation, NMFS has effectively allowed for price negotiations to occur any time during the 12 month period in which the subject crab was harvested, processed and sold. Clearly substantial changes in the marketplace (well beyond the control of the IPQ holder) can take place that would unfairly disadvantage the IPQ holder in an arbitration proceeding.

Mr. Glenn Merrill  
August 9, 2011  
Page 3

We believe the inclusion of "crab fishing year" in the final rule was not intended to provide such a result and that a more appropriate term for the LSA timing regulation should be "during the season." We would greatly appreciate NMFS reviewing the record and we look forward to discussing the need for a regulatory amendment to reflect the original intent for the arbitration system.

Very truly yours,



L. John Latt

cc: Steve Minor - NPCA

Date: November 21st, 2011

To: Eric A. Olson, Chairman  
Chris Oliver, Executive Director  
North Pacific Fishery Management Council  
605 West 4<sup>th</sup> Avenue, Suite 306  
Anchorage, Alaska 99501-2252

From: Scott Campbell

Re: Agenda item C-4 BSAI Crab Stakeholder reports (5-year review issues)

Following is a letter to the Council written by myself regarding the Crab Stakeholders report agenda item as well as a letter written by my son and recently published in the Wall Street Journal.

Sincerely,

A handwritten signature in cursive script that reads "Scott Campbell". The signature is written in black ink and includes a stylized flourish at the end.

Scott Campbell, Owner and Manager  
F/V Seabrooke

I started crab fishing in 1973 and have made a lifetime career as a Bering Sea crab fisherman.

My son started crab fishing with me when he was 15. He describes the pre rationalization days as intense, thrilling, treacherous and incredibly dangerous. There are a few more things I remember that need to be added to the list. Frustration, disappointment, and downright continued fear of failure. In the last few years before rationalization the seasons just kept getting shorter and shorter. It got to the point where it didn't matter how many days of preparation went into getting your boat and gear fine tuned and ready for the season, how skilled you were at fishing, how nice of a boat you had, or even if you had a top notch crew. Success or failure largely depended on the decision you made on where you set your gear on opening day and whether you were lucky enough to choose a spot where 30 to 40 other boats weren't planning on setting also. There was literally no time to recover from making a wrong choice on such a short few day season. Every boat on the grounds was an enemy that threatened your survival and chance to have a successful season. All crab caught was kept highly secret and information was not shared. Our biggest ally was bad weather as it would slow things down enough to buy you a few extra hours of fishing time if you were lucky enough to make it through the storm. A lot of us weren't. Most of the fishermen that fished through the pre rationalization days, lost at some point in time, fathers, sons, brothers, friends and careers. The pressures of trying to catch as much crab as quick as you could, took its toll on everybody. Fatigue would start taking over and rob you of good judgment and mistakes would be made and at times lives lost. This always seemed like a very heavy price to pay to call yourself a crab fisherman. A lot of us had to look for land jobs in between season just to try and survive and earn enough money for a plane ticket to get back for the next season. Our boats also suffered as a lot of the fleet did not get the maintenance needed and were being fished that way with the hopes of making the repairs after the next seasons revenues came in but the problem was that there wasn't ever quite enough left after paying the crew, expenses, insurance, and boat payments at the end of the season. The repairs did not get made in most cases and just got carried over into the next season with the hopes it would get better. It didn't get better until crab rationalization was put into play. There was simply too many boats for the amount of resource we were being given to catch. In 2000 I sold my interest in the Arctic Lady and bought the Seabrooke. Around this time my son decided he wanted to make a career out of crab fishing in the Bering Sea. My heart sank and I did my best to discourage his choice and convince him to go off to college pursue a different career choice. I didn't want him to be faced with the extreme dangers, frustrations and disappointments associated with these short marathon type seasons. He was determined to become a fisherman and boat owner so I finally gave in and in 2003 sold him an interest in the boat and he became my partner. For the next two years it was a struggle to survive but we made it through it. In 2005 when rationalization came in we were still very apprehensive of the program but after the first rationalized crab season the benefits became very apparent. The marathon race for fish was over. Over the next few years we seen a huge change in the mind set of the fishermen. It was no longer a marathon race against each other. We all started talking to each other and working together sharing information on where we had seen juvenile and female crab so these areas could be avoided for bycatch, initiated gear sharing, increased our soak times to reduce handling and pot hauls and allow small crab to clean out of the gear. Rationalization also allowed us to slow the pace on deck so we could handle the crab better and touch them one time and get them back into the water quickly and unharmed. Most of the boats now have hydraulic sorting tables with overboard chutes with water to get

the crab quickly back into the ocean. We as an industry have also helped fund survey and research projects. We have become good stewards of our resource and have common long term goals of sustainability for the future generations. Rationalization has stabilized the crab fisheries that was about to fall off a cliff and doomed to fail under the old derby style system. I would ask that you please allow crab rationalization to go forward unaltered so we as an industry can continue to protect the resources and the safety of our families, friends, and crews that go to sea to make their livings.

Sincerely,



Scott Campbell Sr, Owner and Manager

F/V Seabrooke

## **Making the "Deadliest Catch" Less Dangerous**

**By Scott Campbell, Jr.**

*Scott can be seen on the "Deadliest Catch" TV show. He is captain of the Seabrooke and catches king crab and snow crab. When he is not fishing in Alaska, he lives in Walla Walla, Washington.*

Many people think I'm crazy for making a living by catching crabs in Alaska. Battling 20-foot waves in icy conditions and hauling heavy equipment is part of the job description. My dad, a lifelong fisherman, tried to get me to pick a safer career.

A fireman came up to me and told me he wouldn't want my job, which was hard for me to believe.

Recently the Bureau of Labor Statistics released data about deaths on the job in 2010. Once again fishing topped the list of deadliest jobs in the United States because fishermen faced a fatality rate 33 times the average worker.

Catching crab in the Bering Sea can be treacherous. But most people don't know that it's actually gotten a lot less deadly than it used to be since 2005 when fishing regulations changed dramatically.

The old fishing regulations forced fishermen to race against the clock. To control overfishing, the government set a cap on how many crabs fishermen could collectively catch and we had to stop when that limit was reached. In some years, that meant we had seasons as short as three days. Like in a car race, boats used to line up for the minute the season began.

This intense race was thrilling but it was also incredibly dangerous. Crabbers worked around the clock, sometimes in terrible weather. There was no time to go back and forth to the docks, so some boats would be overloaded with too many crab pots, making them unstable. The result of this dangerous catch is that from 1990 to 2005, an average of 5 crabbers died a year.

Part of my finger was cut off during a violent storm when I got knocked off of my feet and landed on an air compressor. I decided against going to the hospital to have it stitched back on because I knew the fishing season could end any day and my crew had mortgages to pay. I nearly lost my hand after developing a nasty infection.

If that accident happened today, there wouldn't be nearly as much pressure to keep fishing. Since August 2005, we fish under a much better system called "catch shares." Now regulators divide up how much crab the fleet can catch among individual fishermen. We can fish at our own pace during significantly longer seasons. Tighter Coast Guard requirements have also improved safety.

I believe catch shares have saved lives in Alaska because crabbing deaths are much less common now.

Since we switched to catch shares, one commercial crabber has died in the Bering Sea/Aleutian Islands. He was a good friend of mine who worked on my boat. His tragic death happened on a very calm day at sea, which is a reminder that fishing is still a very risky job even with longer seasons. But fishing shouldn't be made any more dangerous than it has to be.

Catch shares have impacted safety in other fisheries. A poll showed more than 85% of Alaska halibut fishermen – who at one point had just a couple of 24-hour windows in a year to catch halibut - found fishing safer under catch shares. The number of search and rescue cases for fishermen in the Alaska halibut and black cod catch share program was 2 in 2010 and 3 in 2009, down a lot from the last two years before the switch to catch shares (26 in 1993 and 33 1994).

Catch shares have brought other benefits too. Because we aren't in such a race against the clock, we're able to get more young and female crabs we don't keep back into the ocean unharmed. Fishermen are earning more and the jobs now are more stable because we have much more time to catch crab. We can plan better because we know in advance how much crab we're allowed to catch.

Crabbing before and after catch shares is like night and day.

There are just a couple dozen catch share programs in the U.S., which may contribute to the fact that fishing remains so deadly.

**November 21, 2011**

**Mr. Eric Olson, Chair  
North Pacific Fishery Management Council  
605 West 4<sup>th</sup> Avenue, Suite 306  
Anchorage, Alaska 99501-2252**

**Re: Agenda Item C-4 (a) Crew compensation/active participation/excessive lease rates**

**My name is Monte Colburn and I fish on the crabber *F/V Wizard*. I have been fishing crab in the Bering Sea for 25 years. The only seasons I've missed in the last 25 years were red crab in 2004 and opilio in 2005, because I was running a supply vessel after the grounding of the *Selendang Ayu* outside of Dutch Harbor. In that time I have worked on deck, been a relief skipper, and I've also run boats as the primary skipper. I currently hold "C" shares that I earned as part of the initial allocation. I have also bought "C" shares since the program was put into place. I have recently been pre-qualified for a loan under the NMFS Crew Loan Program. I'm hoping to take advantage of this Program to buy more quota, either more "C" shares or "A" shares.**

**Now that I have financing in place I want to make sure that I'm able to buy quota as blocks become available for sale. I can keep an eye on Dock Street Brokers and other brokerage websites and hope that I can take advantage when shares are advertised on those sites. But in my experience most quota sales take place "over dinner at Chinooks" and active fishermen/crew don't always know when there's quota available or at what price. Or the seller isn't willing to break the quota block into smaller, more affordable "chunks" that crew can afford. Under the approach that ICE is talking about, active fishermen and crew will be notified that quota is for sale and they will know the terms up front. At least 10% will be made available specifically to crew who qualify under the "C" share requirements. The remaining 90% will be open to both crew and individuals qualifying as "active" in the fishery. Both the 10% to crew and the 90% to crew/active fishermen will be subject to a right of first offer (RoFO). This right will make sure that crew and active fishermen get the first shot at any quota that becomes available. And this approach also breaks quota blocks into manageable chunks that crew and active fishermen can afford instead of keeping it locked up in big, expensive blocks. I'm confident that with my financing in place and first shot at a portion of future quota sales I'll be able to increase my holdings and make a bigger investment in the future success of the crab fishery.**

**As a crewmember on a vessel that leases much of its quota I have an interest in keeping lease rates at a reasonable level. But I don't believe it's the Council's place to decide what "reasonable" is. There isn't another fishery the Council manages where they tell participants what lease rates they can and can't charge. In the past Bristol Bay Red King crab lease rates have been as high as 75%. This past year the majority of the industry voluntarily reduced lease rates to 65% for red crab and 50% for**

opilio. At these rates, vessels were able to pay their bills and still make healthy profits. Crew shares are up and everyone is making money. I think the approach where the industry voluntarily caps lease rates at 65% for red crab and 50% for opilio, then reports back to the Council on compliance, is the way to go. In the future if the Council sees that lease rates are getting too high, they can step in. But for now we should give the voluntary approach a chance. It has worked this year and there's no reason to expect it won't keep working. I also don't think the Council should be mandating the crew receive a set percentage of gross revenues. As long as there has been fishing there has been wage negotiation between captains and crew. These are private contractual agreements and it's not really the place of the government to get involved. Even with the quota for red crab down this year, captains and crewmembers are making a very decent living.

And finally, I'm not in favor of any type of vessel use cap within cooperatives. The whole point of forming cooperatives is having the ability to stack quota on the safest and most efficient vessels. This brings down overall operating costs and increases safety. By putting vessel use caps in place you will force more boats to go fishing, but these will be less efficient and not as safe. The cost of catching crab will go up and crew will be no better off than before. And besides, many vessels have re-rigged to participate in other fisheries or do other things. And many boats have been "moth-balled" for so long they're not really fit to fish crab. So if the Council makes it so that more boats have to go fishing, where are these extra boats going to come from?

At this time, I encourage the Council to not take any formal action and I thank the Council for listening to what I have to say.

Sincerely,



Monte Colburn  
F/V Wizard



Mark Gleason, Executive Director  
5470 Shilshole Ave NW Suite #505  
Seattle, WA 98107  
(831) 419-6993  
[markhgleason@gmail.com](mailto:markhgleason@gmail.com)  
<http://alaskaberingscraabbers.org/>

Date: November 21st, 2011

To: Eric A. Olson, Chairman  
Chris Oliver, Executive Director  
North Pacific Fishery Management Council  
605 West 4th Avenue, Suite 306  
Anchorage, Alaska 99501-2252

From: The Alaska Bering Sea Crabbers

Re: Agenda item C-4 BSAI Crab Stakeholder reports (5-year review issues)

Following are comments regarding the Alaska Bering Sea Crabbers (ABSC) efforts to address the issues raised during the Crab 5 Year Review by the Council at the December 2010 meeting. The Alaska Bering Sea Crabbers represents approximately 70% of the harvesters fishing crab in the Bering Sea. Following, you will find:

- A concise one page document titled "Alaska Bering Sea Crabbers Stakeholder Report on 5 Year Review Issues, One Page Talking Points" which provides bullet points summarizing the ABSC Stakeholder Report for quick reference.
- An Executive Summary document titled "Alaska Bering Sea Crabbers Stakeholder Report on 5 Year Review Issues, Executive Summary" which is a 5 page executive summary of the full Stakeholder Report.
- The full ABSC Stakeholder Report titled "Alaska Bering Sea Crabbers Stakeholder Report on 5 Year Review Issues" providing detailed information regarding the ABSC efforts and solutions consisting of 22 pages.

Sincerely,

Mark Gleason, Executive Director  
Alaska Bering Sea Crabbers

Edward Poulsen, Advisor  
Alaska Bering Sea Crabbers

Joe Sullivan, Legal Counsel  
Alaska Bering Sea Crabbers

Jim Stone, President  
Alaska Bering Sea Crabbers

**Alaska Bering Sea Crabbers Stakeholder Report on 5 Year Review Issues  
One Page Talking Points**

**From December 2010 NPFMC Problem Statement:**

*"Program stakeholders, as well as the Advisory Panel, have identified several problem areas, including issues of equitable crew compensation, quota lease rates and active participation...the Council strongly encourages crab rationalization stakeholders to work together within the industry to craft solutions to the concerns"*

- **Crab Industry Workgroup formed to address concerns of NPFMC**
  - Consists of quota share (QS) holders, vessel owners, captains, & crew
  - This approach represents collaborative, good faith effort of all parties
- **Active Participation**
  - "Controls" already exist to discourage "speculative" QS purchases
  - Right of First Offer (RoFO) on QS sales involving ICE members is an additional "control" to incentivize active participation
    - 10% of QS made available to crew ("C" share eligibility criteria)
      - 15 days to exercise RoFO
    - Remaining 90% of QS (plus anything left over from initial 10% QS offering) offered to "active" fishermen and crew
      - "Active" includes crew and vessel owners with fishing boats operating in Alaskan waters (State/Federal)
      - 5 days to exercise RoFO
    - If no sale executed, QS offered broadly under original terms
    - If terms change, would trigger re-initiation of RoFO process under new terms
    - ICE would maintain lists of crew and "active" fishermen and monitor QS sales through NMFS RAM database
      - RoFO compliance enforced via ICE membership agreement, liquidated damages assessment, and possible expulsion from ICE
      - Limited exemptions to RoFO requirement
- **Crew Investment Opportunities**
  - RoFO process described above
  - NMFS Crew Loan Program in place to assist with financing
- **Crew Pay/Leasing**
  - Individual voluntary cap on lease rates (65% BBR and 50% BSS) initiated in 2011-2012...will be in place for 2012-2013 as well
  - Cooperative member agreements to cap lease rates would trigger anti-trust concerns, thus not viable
  - Annual reporting to ensure compliance with voluntary efforts
- **Conclusion-** The Council tasked industry to address the concerns raised in the 5 Year Review. The private sector solution described here does that. It allows for proper oversight while avoiding unnecessary and overly burdensome direct government intervention. This approach is legally permissible, financially realistic, and equitable for all stakeholders.

## **Alaska Bering Sea Crabbers Stakeholder Report on 5 Year Review Issues Executive Summary**

From December 2010 NPFMC Problem Statement:

*"Program stakeholders, as well as the Advisory Panel, have identified several problem areas, including issues of equitable crew compensation, quota lease rates and active participation...it will take some additional time for Council members to more fully evaluate the five year review and assess oral and written public testimony to determine whether or not additional Council action is needed. In the meantime, the Council strongly encourages crab rationalization stakeholders to work together within the industry to craft solutions to the concerns identified. Stakeholder solutions will be considered by the Council should a formalized five year review amendment package be developed."*

### **Crab Industry Workgroup**

The workgroup was formed shortly after the December 2010 North Pacific Fishery Management Council (NPFMC, or "the Council") meeting. The group, which includes vessel owners, quota share (QS) holders, and crew, has formally met 8 times since its inception, including a Crab Crew Workshop sponsored by Alaska Bering Sea Crabbers on May 3, 2011 in Seattle. The purpose of this workshop was to inform crewmembers of quota share purchase opportunities as well as a discussion and presentations from lenders regarding possible financing options. The most recent meeting of this group was held on November 21, 2011 in Seattle. The purpose of this meeting was to provide interested crew with the proposal described by this Executive Summary. The majority of the ideas contained within this 5 Year Review document reflect the ideas developed collectively over the course of these 8 meetings, as well as through numerous informal meetings, telephone calls, and email correspondence.

### **Inter Cooperative Exchange (ICE) & Alaska Bering Sea Crabbers (ABSC)**

ICE is the FCMA (Fishermen's Cooperative Marketing Act) Cooperative that negotiates price with the processing sector as well as coordinating harvest activities among Co-op members. The Alaska Bering Sea Crabbers (ABSC) is a separate entity, consisting of all ICE members, that engages in the public policy arena on behalf of its members. The members of ICE/ABSC are of the opinion that changes to the ICE membership agreement and other voluntary measures are the most effective means to address the policy questions described in the December 2010 NPFMC Problem Statement. The hope is that through private contractual agreements and voluntary measures, rather than direct government intervention via the Council, industry stakeholders may find solutions internally. The following paragraphs provide a brief summary of the proposed solutions.

### **Active Participation**

There is a concern that individuals or entities will purchase crab QS as an investment tool without any intention of actually owning a vessel or actively participating in the fishery. At this time the industry is not aware that this type of

speculative QS purchasing has occurred. Nonetheless, the concern is plausible and the industry feels it worthwhile to address this possibility before it becomes a reality. An additional concern is that current QS holders have little incentive to have an ownership stake in an active vessel due to their ability to simply lease quota onto existing active vessels. There are multiple "controls" in place already that would discourage this type of speculative investment. These include the requirement to have 150 days sea time in order to purchase crab QS (or a minimum 20% partner that meets this requirement); the fact that there are a limited number of entities that initially qualified to hold QS which may be offered for sale, and; the fact that these limited number of entities may have pre-existing liabilities associated with them. However, changes proposed by ICE would add additional layers of "control."

For fishing year 2012-2013, ICE is proposing a change to its membership agreement that would provide preferential access ("Right of First Offer," or RoFO) for qualified crew and those individuals meeting the definition of "active," whenever crab QS currently held by ICE members is offered for sale. Both active crewmembers (as defined by the Crab Rationalization "C" share eligibility criteria) and vessel owners meeting the following criteria would be considered "active." An "active" vessel owner would be defined as a person that holds a direct or indirect ownership interest in a Commercial Fishing Vessel that is either commercial fishing, tendering, or acting as a research vessel in support of fisheries off the coast of Alaska, as of a specified date each year. Those meeting the definition will submit to ICE a request to be designated "qualified crew" or "active." ICE will maintain a list of all active vessel owners and crewmembers for the purposes of initiating the RoFO process.

When an ICE member wishes to sell crab QS they will be required to offer for sale 10% to active crew. Once crew is notified of the QS offering, they will have 15 days to exercise the "right" by committing to purchase all or a portion of the QS offered for sale. At the expiration of this 15-day period, the remaining 90% of the QS (plus any remaining portion of the 10% initially offered to crew) will be offered for sale to those meeting the "active" criteria. As previously mentioned, crew would also qualify as "active" under the definition provided here with respect to the RoFO process. Upon notification of the 90% QS offering, qualified active fishermen and crew would then have an additional 5 days to exercise their "right" by committing to purchase all or a portion of the QS offering. If the right was not exercised the crab QS could then enter the market place at the price described at the initiation of the RoFO process. If the QS holder seeks to reduce or otherwise modify the asking price or purchase terms, the crab QS would then be subject to a new RoFO process according to the new terms. This process would continue until either all of the crab QS is sold or the holder removes it from the market. Of course, the QS holder may bypass the RoFO process altogether by negotiating directly with crew and active fishermen and ultimately executing a sale consistent with the terms described in the RoFO process.

Several exemptions are made to the RoFO process. These are in the event the QS offering is part of a court-ordered asset liquidation as in a foreclosure; when the QS is part of the sale of a fishing vessel or fishing business whereby the business would

no longer be financially viable if the QS were to be "peeled off" and sold separately, or; in the event there is some type of partnership "re-structuring" whereby one or more partner(s) in a business intend to "buy out" one or more of their current partner(s) in the business. Of particular note is the fact that no exemption exists in the case of QS being passed to an heir in the event the original QS holder passes away. The expectation is that the heir would either become active in the fishery or divest themselves of the QS holding consistent with the RoFO process described herein.

When considering the methods to encourage active participation some options were considered but ultimately abandoned as being too disruptive to current business practices and cooperative relationships (i.e. forcing existing QS holders to become "active" or divest themselves of quota) or inappropriate as to their interference with expected future business relationships (i.e. mandating a minimum percentage standard for vessel ownership).

ICE would track all QS transfers through routine queries of the existing NMFS RAM database. ICE further anticipates a program of annual voluntary reporting to ensure that "active" participants be given preferential access to QS via the RoFO process. ICE would also enforce compliance with the terms described above through its annual membership agreement. If it were determined that ICE members were attempting to "game" the system by complying with the letter of the agreement but not the intent, the agreement could be modified appropriately. Furthermore, ICE members found to be in breach of the agreement face the prospect of liquidated damages and/or possible expulsion from ICE. At this point in time ICE believes that there is widespread support for this approach both within ICE and among non-ICE coops and is unaware of any meaningful opposition.

### **Crew Investment Opportunities**

The concern with regard to crew investment opportunities is that crew are not afforded sufficient notice and/or access to QS when it becomes available for purchase and that they may not have sufficient access to capital to undertake a QS purchase. Under the terms of the original BSAI Crab Rationalization Program, 3% of the original QS were reserved for active captains and crew as "C" shares. Prior to the December 2010 Council meeting there was some discussion of a possible "compensated reallocation" of QS whereby some amount of CVO ("A" shares) would be converted to "C" shares and purchased by qualified captains and crew. This approach was deemed too disruptive to the Rationalization Program due to the complications that would arise under this approach with respect to Processor QS (PQS) and the "share matching" requirement. As such, the Council requested industry provide a "private solution" to the concerns expressed. Under the ICE proposal, existing CVO ("A" share) QS would be offered (at minimum 10% of any QS sale) to active crew under the RoFO process described in the preceding section. The remaining 90% of any QS sale involving ICE members would also be offered for sale to active fishermen, including crew, according to the RoFO process described in the preceding section. This preferential access afforded to crew would address the

concern regarding access to available QS. After much delay, the National Marine Fisheries Service (NMFS) has initiated a crew loan program as of 2011. There is an expectation that this program would be the primary financing means employed by crew wishing to purchase QS under this RoFO process. This would address the second concern that crew may not have access to capital to execute the purchase of QS when it becomes available.

As mentioned in the previous section, ICE would modify its membership agreement to ensure that crew would be afforded preferential access to QS when ICE members wish to offer it for sale. ICE members in breach of the membership agreement may face the prospect of liquidated damages and/or expulsion from ICE. ICE would also summarize active crew investments in QS as part of its annual reporting requirement. At this time, ICE believes the approach outlined above enjoys wide support within ICE and among non-ICE coops and is not aware of any meaningful opposition.

### **Crew Pay/Leasing**

The concern expressed by the Council is that excessive lease rates on QS has resulted in a slow erosion in terms of the percentage of gross revenues paid to crew. Discussions within the Crab Industry Workgroup have determined that this issue generally applies to a subset of vessels and is mainly confined to Bristol Bay Red king crab. More specifically, this issue seems to be disproportionately applicable to "new entrants" or those vessels that were purchased after the implementation of the Rationalization program. Most vessels that were initially issued QS do not charge lease fees on their initial issue QS. However, many vessels considered "new entrants" were purchased with very little (if any) initial issue QS, but rather the intention all along has been to participate in the fishery via the QS lease market. Industry believes the investment made by these new entrants is important in terms of the jobs these vessels provide and is evidence that there are still profits to be made even when an active QS lease market exists. Without these new entrants, it is likely that the QS these vessels fish would have been fished on more established vessels and would likely have resulted in more consolidation than has occurred to date. In order for many of these vessels to "attract quota" they have had to offer higher lease rates than might otherwise be expected. This is the primary reason lease rates have reached levels deemed by some as "excessive." Exacerbating this situation is the fact that red king crab has seen significant price increases over the last few years, thus adding additional upward pressure on lease rates.

In an effort to dampen the observed lease rate increases, some ICE members voluntarily capped lease rates at 65% for Bristol Bay red king crab and 50% for Bering Sea opilio/snow crab in fishing year 2011-2012. Initially, it was the intention of ICE to make this part of the membership agreement for 2012 and beyond. However, legal issues related to anti-trust have recently come to light and it is clear that the industry as a whole can not mandatorily cap lease rates or set crew pay standards. As such, an agreement among cooperative members to do so is no longer viewed as a viable approach. However, a large majority of ICE members have

of First Offer (ROFO) process when they wish to sell crab quota share. Members meeting the active definition from all cooperatives signing this agreement would have a right of first offer to purchase 90% of this quota share (the other 10% is specifically set aside for crew to be discussed later).

A summary of some of the key definitions in regard to what constitutes active are as follows:

**"Active Fisherman"** means a person that (i) holds a direct or indirect ownership interest in a Commercial Fishing Vessel as of the Annual Record Date; (ii) provides ICE or its agent with the information and documents that ICE requests as evidence of such ownership interest; and (iii) is named on the "Active Fisherman" list that ICE maintains.

**"Commercial Fishing Vessel"** means a vessel not less than twenty-nine feet in length overall that has been employed in commercial fishing in state waters or in the Federal Fishery Conservation Zone during the twelve (12) month period prior to the Annual Record Date. For purposes of this definition, a vessel that is employed as a tender or research vessel in support of commercial fishing shall be considered a Commercial Fishing Vessel.

**"Crab Crewmember"** means an individual whom (i) meets the Crab Rationalization Program "C" share recent participation requirements as of the Record Date, as the same may be amended from time to time; (ii) did not receive catcher vessel owner ("CVO") or catcher processor owner ("CPO") QS at initial allocation; and (iii) is named on the Crab Crewmember list that ICE maintains.

As reflected in the definitions above, Inter-Cooperative Exchange (ICE) will maintain a list of those crew and vessel owners who meet the definition for active. When quota share is made available, those on the active list will be notified and the ROFO process will begin.

The ROFO process begins when a QS holder, who is a member of a ROFO participating cooperative, wishes to sell his QS. The QS holder is required to sell 10% to active crew (described under the crew investment opportunity section) and 90% to either active crew or vessel owners as defined above. The QS holder would determine the price at which he wishes to sell which would be communicated to all ROFO holders. ROFO holders would have 15 days to commit to purchasing the QS at the requested price. If there are no commitments, the QS is free to be purchased outside of the ROFO process. If there is an over commitment of purchasers, the QS is split pro-rata based on commitments. If the quota does not find any commitments either through the ROFO process or outside the ROFO process, the QS holder may wish to pull his QS off the market (which ends the process) or reduce his requested price. If the price is reduced, the QS then goes back through the ROFO process at the new reduced price and restarts the 15 day commitment period. This process continues until either all the QS is sold or the QS holder pulls the QS off the market.

There are several exemptions which are provided for transferring QS.

First, an exemption is made in connection with a foreclosure of a security interest or pursuant to a court order. This exemption is necessary as this agreement could complicate court proceedings.

Second, an exemption is made in connection with the sale of a Bering Sea or Aleutian Islands crab fishing vessel, or as part of the sale of an entire commercial fishing business. This exemption makes sense because, in essence, the purchaser will be active after completing the transaction as he is buying both QS and a vessel.

Finally, exemptions are made for both related parties and inter-company transfers. This is to prevent the ROFO process from disrupting partnership restructuring where it could disrupt an ongoing fishing operation by triggering the ROFO process and resulting in the vessels QS being sold outside of the operation.

It is important to note that there is specifically no exemption for cases where QS holding entities who do not meet the active standard can pass along the QS to heirs upon death of the entities owners. It would be expected that in these cases, if the heirs intended to own the QS, they would need to become active.

Having gone through all of this, it is anticipated that at the end of the day, many transactions will occur outside of the ROFO process. It is anticipated that many QS holders would simply find an individual or entity that is active, either through personal knowledge or a broker, and sell directly to them. ABSC will be asking members to provide documentation on these sales and will be following up with audits to ensure compliance.

#### **Other options considered and disregarded:**

The industry considered measures that would force quota share holders to become active. This was deemed too disruptive to existing business and cooperative relationships. Some vessels are very dependent upon leasing quota share from entities that are not currently active. Forcing these non-active entities to become active may have the perverse result of putting undue pressure on the non-active entities harvesting partner to sell a portion of the vessel to him to maintain an active participation standard. The harvesting partner may not really be interested in selling a portion of the vessel to him, but may feel he has little choice as he would likely lose the quota otherwise. In addition, it would be expected that under this approach, further consolidation in the industry would occur and those larger players would be the "winners" accumulating more quota while the smaller players would be "losers".

The industry also considered including a standard for a certain minimal amount of vessel ownership (i.e. 5% or 10%) in order to be deemed active. Industry felt this was inappropriate as it likely would interfere with expected future business arrangements. It is anticipated that in the future, crab QS holders will likely partner together in ownership of vessels and own the vessel pro-rata based on the QS they hold individually. An arbitrary standard in terms of vessel ownership would be inappropriate under this model, particularly when there is a strong history of many minority shareholders owning vessels, including skippers at fairly small levels (i.e. 5-10% or less). If a group of QS holders decides to purchase multiple vessels, it could be that some individuals own 5% of 2 or 3 vessels. Arbitrary standards simply would create a roadblock for this sort of positive trend. It should also be pointed out that the likelihood of "sham" ownership is reduced through reporting and if abuses are discovered, membership agreements can be modified.

Finally, the industry considered several definitions for commercial fishing vessel. It was decided that vessels below 29 feet should not be included in the active definition. Considerations were made to not include any limit, but it was felt this would be too easily abused. Length limits greater than 29 feet were also considered but the industry felt that this would exclude Bristol Bay salmon fishermen. There has been a history of driftnetters moving into crab and vice versa. By having a vessel limit greater than 29 feet would make it much more difficult for these fishermen from being able to enter the crab fishery in the future.

adopted the individual voluntary approach. This is in conjunction with strongly higher ex-vessel prices resulting in a very profitable year for vessels and crew. In fact, it is widely assumed that crab crew in the Bering Sea are among the highest, if not the highest paid crew, of any fishery in the country. A majority of ICE members have indicated their intention to continue with this voluntary approach for fishing year 2012-2013 and into the foreseeable future.

As with the active participation and opportunities for crew investment issues, ICE intends to survey its members and provide the Council with annual reports concerning lease rates and crew compensation. Unfortunately, by definition, there really is no enforcement mechanism for an individual voluntary approach such as the one outlined above. However, in the future, if the Council becomes concerned that lease rates are increasing to levels beyond those deemed equitable, the Council will still have the option to examine the issue again and take formal action if it feels the need to. This in itself is pressure enough for industry.

Industry feels this individual voluntary lease cap is the most viable approach. Agreements among cooperative members to adopt lease rate caps would trigger anti-trust concerns, as previously described. An approach whereby crew was paid a fixed percentage of gross revenues would put "new entrants" who rely heavily on leased QS at a disadvantage and would likely force many of them out of the industry.

### **Conclusion**

At its December 2010 meeting the Council requested industry report back with options to address the concerns raised during the 5 Year Review. Specifically the Council requested options for addressing active participation, crew compensation, and excessive lease rates. The industry responded by forming the Crab Industry Workgroup. This workgroup has formally met 8 times in the last year. In addition, there have been countless informal meetings, phone discussions, and email correspondence. The approach for dealing with each of the issues identified has been summarized in this document. A more detailed description of each approach is contained in the full *Outline of Analysis for 5 Year Review*. Industry feels it has done what the Council asked of it in December 2010. While this approach may not be perfect, it is the product of a good faith effort on the part of all participants. It reflects what is legally permissible, financially realistic, and equitable to all concerned parties. It is the product of a collaborative effort between QS holders, vessel owners and operators, and crew. And it represents a non-regulatory approach to what is considered by many, a problem best addressed through a private sector solution.

## Alaska Bering Sea Crabbers Stakeholder Report on 5 Year Review Issues

### **Introduction:**

The North Pacific Fishery Management Council requested industry to provide solutions to issues perceived from the 5 year review of the crab program.

This document provides proposed solutions to these concerns including why industry feels these solutions are appropriate, the anticipated results of the solutions and background of how we embraced these solutions.

### **December crab 5 year review motion:**

The North Pacific Fishery Management Council passed the following motion during the December, 2010 meeting:

*"The Council appreciates the work of the Council and NOAA Fisheries staff, as well as that of Mike Downs, AECOM, Inc., Commander Chris Woodley, USCG and Jennifer Lincoln, National Institute of Occupational Safety and Health, in preparing the five year review of the crab rationalization management program for Bering Sea and Aleutian Island crab fisheries. The five year review demonstrates that many aspects of the Bering Sea and Aleutian Islands crab rationalization management program seem to be working well for the stakeholders. For example, participants have adapted to the complications of the "three-pie" system, safety goals continue to be achieved and overcapitalization has been reduced.*

*However, the review also indicates that there are some aspects of the program that may merit further consideration. Program stakeholders, as well as the Advisory Panel, have identified several problem areas, including issues of equitable crew compensation, quota lease rates and active participation, as related to program participation opportunities and next generation ownership, and certain aspects of the binding arbitration system. Nevertheless, it will take some additional time for Council members to more fully evaluate the five year review and assess oral and written public testimony to determine whether or not additional Council action is needed. In the meantime, the Council strongly encourages crab rationalization stakeholders to work together within the industry to craft solutions to the concerns identified. Stakeholder solutions will be considered by the Council should a formalized five year review amendment package be developed.*

*At this time, the Council will limit its action on the five year review package to the following single issue, and at a subsequent meeting, the Council will consider whether or not concerns associated with the five year review merit additional Council action."*

This document will provide the solutions and steps industry has taken to address the concerns of:

- Active participation related to program participation opportunities and next generation ownership, pages 3-7;
- Crew investment opportunities, pages 8-12;
- Equitable crew compensation and quota lease rates, pages 13-19.

This document will not address binding arbitration.

**Summary of time and effort by industry to find solutions:**

The industry has invested a significant amount of time and resources to work towards acceptable industry wide solutions. Soon after the December meeting, an ad hoc group was formed which called itself the Crab Industry Workgroup. This workgroup consisted of vessel owners, quota share holders, and crew members. This workgroup met on the following dates:

- December 15th
- February 1st
- March 18th
- May 4th
- June 2nd
- August 8th
- October 29th
- November 21st

The task of the workgroup was to provide a forum for vessel owners, quota share holders and crew to discuss their differences in a professional and respectful manner. The workgroup had a large role in crafting the solutions presented here. In general, the workgroup felt that these solutions, though not perfect, should be moved forward. Concerns expressed by some crew particularly with crew pay and leasing issues include accountability and timeliness of reporting. This document will delve deeper into these concerns and how these concerns can be alleviated later.

Alaska Bering Sea Crabbers sponsored a Crab Crew Workshop which occurred on May 3rd in Seattle with remote locations in Kodiak and Anchorage. Speakers included Mark Fina (NPFMC), Clydina Bailey (NMFS RAM), Scott Houghtaling (NMFS Financial Services), Erik Olsen (Farm Credit Services), Jeff Osborn (Dock Street Brokers), Tim Henkel (Deep Sea Fishermen's Union) and Edward Poulsen (Alaska Bering Sea Crabbers). The primary goal of that meeting was to inform crew of opportunities to purchase crab QS and financing options. However, the meeting was also successful in engaging crew in preparation of crew pay and leasing discussions that were occurring in the Crab Industry Workgroup. There were over 100 attendees at this meeting, many of which were crew.

Of course, there were many additional meetings internally with harvester organizations. Dozens of such meetings occurred regularly from December 2010 until the current time.

Industry has contributed a significant amount of time and resources to provide meaningful and reasonable solutions to issues raised by the Council. It is important to note that this investment of resources has taken away focus from other important topics such as the Illegal, Unreported and Unregulated foreign harvest (IUU), Marine Spatial Planning, and a campaign to create a National Seafood Marketing Coalition among many other important priorities.

## Active Participation

### **Background:**

Issues relating to active participation as understood by the industry primarily relates to concerns that individuals or entities could purchase crab Quota Share (QS) simply as an investment with no intention of actively owning a vessel. In addition, there is concern that there is not a strong incentive for current QS owners to continue to own vessels as they can simply sell their vessels and receive a harvest fee at a much lower risk.

The proposed industry solution intends to reduce the opportunities for outside investors to purchase QS with no intention of owning a vessel as well as increase the incentive of current QS owners to become active.

Having said this, the industry does not believe that there has been any significant amount of quota purchased by outside investors with no real understanding of the fishing industry to this time. Part of the reason for this is that QS is inherently risky and not necessarily a stable investment. Quotas fluctuate rapidly as do prices from year to year. In addition, owning QS without having some stake in a vessel may not be a great long-term strategy if opilio quotas in particular continue to go up - they may have a difficult time finding a harvesting partner in this instance. In addition, the industry does not believe that non-active current QS holders have been significant purchasers of crab QS. Instead, the vast majority of crab QS that has been purchased was done by CDQ groups or by active vessel owners. This makes sense as they make money not just on the QS but also from vessel operations. The bottom line is that industry believes there is not a current problem with active participation, but that these measures are appropriate to ensure that it does not become a problem in the future.

It is important to understand that the current rules regarding purchases of crab QS are restrictive. In order to purchase crab QS, you must show that you either have 150 days of sea time or you must have at minimum a 20% partner who has 150 days of sea time. It is also possible to purchase an entity that initially qualified to hold QS. However the limited number of these entities as well as the downside risk of purchasing the entity as well as any previous liabilities limits the probability of purchasers pursuing this path.

The following solutions are intended to provide an additional layer of control on top of existing regulations to provide greater comfort that most future transactions will indeed be active purchasers.

### **Explanation of ICE membership agreement:**

Alaska Bering Sea Crabbers has drafted changes to their membership agreements which are intended to be in place for the 2012-2013 season and beyond to address issues raised by the Council regarding active participation. The full membership agreement can be found as an attachment to this document titled Bering Sea Crab Quota Share Right of First Offer Agreement.

In general, what this proposed solution would do is to provide a preferred access to quota for those who are deemed to be "active" in the fishery. Both vessel owners (Active Fishermen as defined below) and active crewmembers (Crab Crewmember as defined below) would be defined as active. This preferred access to quota would occur through the membership agreement forcing it's members to follow a Right

### **Compliance by non-ICE Coops:**

ABSC has been working with other non-ICE cooperatives on this proposed solution. Feedback received is that there is wide acceptance for this solution. ABSC is not aware of coops that hold any meaningful amount of quota that are opposed to this approach. It is expected that ICE/ABSC likely would act as a central administrator for the program.

### **Enforcement:**

In order for entities or individuals who believe they qualify as active to be admitted to the ROFO notification list, they would need to explain how they meet the definition. In addition, it is a fairly straightforward process to audit the QS database and determine who has sold and purchased QS over the past year as well as any address changes for existing QS entities. If there are transactions that have occurred by members in breach of the ROFO agreement, either liquidated damages or expulsion from the cooperative would occur.

If the industry determines that some individuals are taking advantage of loopholes to meet the letter but not the spirit of the definitions, the industry could modify definitions to tighten them as needed. Since these are private agreements, it is much easier for industry to make modifications to these agreements than it would be to modify regulation. Industry intends to not only monitor current transactions to determine if the purchaser is active or not, but also to track behavior as we move forward to determine if purchasers remain active.

### **Annual voluntary reporting:**

It is anticipated that the industry would provide annual reporting to the Council regarding the number of sales that have occurred that participated in the ROFO process, the number of sales that occurred that closed outside of the ROFO process but resulted in active entities purchasing, and finally the number of sales that occurred where the purchasing entity was not active. In addition, industry would anticipate that reporting would need to be provided regarding the actual active membership agreement in place to address active participation. It is anticipated that it may be necessary to refine the active participation agreement in the future and any such changes would be communicated to the Council.

### **Analysis and likely results:**

Although it is difficult to provide specific analysis regarding what the likely results of the industries action would be, several general conclusions can be drawn in terms of likely results.

There has not been any real consolidation in the number of Quota Share holders. In fact, according to the latest NMFS report to industry from 2011, "By the end of six Program years, initial issues holding QS or PQS decreased from 511 to 413, while the number of all quotaholders increased from 511 to 522." This shows that there have been a drop in those entities that initially received QS by about 100 while about 100 new entrants now own QS. These new entrants were required to meet the NMFS ownership requirements described above to purchase the QS. Many of these new entrants are crew or former crew as well as CDQ groups. Industry is not aware of outside investors purchasing crab QS. However,

this voluntary action on behalf of industry further insures that this will not happen. In addition, industry will be in a much better position to answer the question as to what portion of QS is truly being purchased by active vessel owners and crew due to the surveys that will occur.

This action, plus the fact that vessels are making very good profits at this time (partly due to industry efforts to address leasing issues) provides a strong incentive for QS holders to become active vessel owners. It is anticipated that this action will result in QS holders who either have vessels not well suited to fish crab, no vessel at all or allocations too small to fish on their own vessel to over time work together with others who do own vessels to partner together and "coop" the ownership of the vessel. This is a natural next step for the industry but will likely take time to develop.

It is also likely that under this proposed action that QS prices will decline to some degree as the ROFO process will create limits and inefficiencies on the market. For example, it will likely be much more difficult in the future for QS to be auctioned off to the highest bidder as the ROFO process would make this nearly unmanageable.

In addition, this action will not disrupt current business arrangements where a new entrant vessel owner is dependent upon leasing from a QS holder as QS holders are not forced to sell. Any sort of forced divestiture, even if it is over time, will be disruptive to those that have a business model dependent upon leasing. If a forced divestiture were to occur, it is likely that those with the deepest pockets would end up owning the quota. The new entrants would have a very difficult time competing to purchase the quota and over time would likely not have enough quota to lease on their vessel in order to be viable.

Finally, it is important to point out that there are numerous benefits gained from the ability of QS holders to continue to lease and not be forced to be active or else divest. If all QS holders were forced to be active or face divestiture, the number of vessels fishing would be a much higher level than it is today. As a result, profitability for vessel owners and crew pay would be significantly reduced. Just as importantly, the conservation benefits currently being gained would be reduced. This is because more boats would be fishing and on average vessels would be using less gear as they would have less crab to catch and less incentive to have enough gear to maximize soak time. If all you have is 50,000 lbs of red king crab to catch, you aren't going to fish with two loads of gear. However, if you have 200,000 lbs of red king crab to catch you have a strong incentive to fish with multiple loads of gear. The reduced fleet size obviously creates very significant savings in fuel and dramatically lowers the carbon footprint of the fleet as well.

## Crew Investment Opportunities

### **Background:**

Prior to the December 2010 Council meeting where the crab 5 Year Review was on the agenda, the Council had been struggling with ways to provide crew greater access to purchase crab IFQ. The specific approach the Council had considered was one where a portion of A share QS would be converted to C share QS. Crew who qualified to hold C share QS would need to purchase this QS so it became known as a "compensated reallocation". However, it soon became clear that this approach was very complicated as this compensated reallocation would have other unintended consequences such as diminishing the amount of IPQ as well as reducing the community protections as more quota is moved to C shares.

During the December 2010 Council meeting, the Council requested industry to provide a private solution to "program participation opportunities and next generation ownership". Industry has developed a proposed solution to these issues that provides crew better access to crab QS, without the disruptive reallocations, as well as incentives to ensure future QS purchases are held by active participants (described in the previous section).

Crew were involved from the start in developing this solution and have been supportive of this approach through the Crab Industry Workgroup process. In addition, ABSC held a conference on May 3rd where crew were formally invited to learn about opportunities to invest in crab QS. The below proposed solution was described during that meeting. In addition, NMFS Financial Services was at the meeting and announced that their crab crew loan program would be ready to provide financing to qualified crew during the summer of 2011.

In general, active crew are provided a right of first offer privilege to purchase up to 10% of all QS being sold. Since active crew are purchasing existing quota and no share re-designations occur, there are no issues with reducing the amount of IPQ or community protections.

It is expected that crew will have a much greater ability to purchase A share quota than in the past under this solution. The two largest impediments for crew to buy crab QS in the past have been financing and availability. It is believed that issues with financing have been addressed through the NMFS crab crew loan program. It is believed that this industry provided solution will be able to address QS availability for crab crew.

In the past, crab QS in many cases has bypassed crew and was purchased by larger more established players who could commit to purchasing the entire transaction. In most cases, crew were not even aware that crab QS had changed hands. This solution intends to change this. Under this proposed solution, interested active crew will be notified when crab QS is available and they will have a real opportunity to purchase the QS.

In effect, the crab program have provided crew opportunities to become invested in the crab fishery that they would never have had prior to the crab program and this proposed industry solution will further these opportunities and benefits for crew.

### **Explanation of ICE membership agreement:**

ABSC and ICE, representing approximately 70% of the crab QS, are moving forward with changes to ICE cooperative membership agreements to address crew investment opportunities. The full agreement is attached to the end of this document. This solution and the solution for active participation are bundled in the same membership agreement titled, "ICE - Crew and Active Participation Right of First Offer".

In general, what this proposed solution would do is to provide a preferred access to 10% of crab QS being sold for the benefit of active crew. Active crew are defined as:

an individual whom (i) meets the Crab Rationalization Program "C" share recent participation requirements as of the Record Date, as the same may be amended from time to time; (ii) did not receive catcher vessel owner ("CVO") or catcher processor owner ("CPO") QS at initial allocation; and (iii) is named on the Crab Crewmember list that ICE maintains.

This preferred access to quota would occur through the membership agreement forcing it's members to follow a Right of First Offer (ROFO) process when they wish to sell crab quota share. Active crew would have a right of first offer to purchase 10% of quota share sold by members of cooperatives with this or similar membership agreements.

As reflected in the definitions above, Inter-Cooperative Exchange (ICE) will maintain a list of those crew who meet the definition for active. When quota share is made available, those on the active list will be notified and the ROFO process will begin.

The ROFO process begins when a QS holder, who is a member of a ROFO participating cooperative, wishes to sell his QS. The QS holder is required to sell 10% to active crew and 90% to either active crew or vessel owners (defined in the section above regarding active participation). The QS holder would determine the price at which he wishes to sell which would be communicated to all ROFO holders. ROFO holders would have 15 days to commit to purchasing the QS at the requested price. If there are no commitments, the QS is free to be purchased first by any active participants. If no active participants commit to purchase the QS, it can be sold outside of the ROFO process. If there is an over commitment of crew purchasers, the QS is split pro-rata based on commitments. If the quota does not find any commitments either through the crew or general active participation ROFO process or outside the ROFO process, the QS holder may wish to pull his QS off the market (which ends the process) or reduce his requested price. If the price is reduced, the QS then goes back through the ROFO process at the new reduced price and restarts the 15 day commitment period. This process continues until either all the QS is sold or the QS holder pulls the QS off the market.

There are several exemptions which are provided for transferring QS.

First, an exemption is made in connection with a foreclosure of a security interest or pursuant to a court order. This exemption is necessary as this agreement could complicate court proceedings.

Second, an exemption is made in connection with the sale of a Bering Sea or Aleutian Islands crab fishing vessel, or as part of the sale of an entire commercial fishing business. This exemption makes sense because when an entire fishing business is sold, the vessel is generally dependent upon the quota being transferred with the vessel. If a portion of the quota must go through the crew ROFO process, it is likely that the operation of the vessel will be impaired due to a lack of quota to fish.

Finally, exemptions are made for both related parties and inter-company transfers. This is to prevent the ROFO process from disrupting partnership restructuring where it could disrupt an ongoing fishing operation by triggering the ROFO process and resulting in the vessels QS being sold outside of the operation.

Having gone through all of this, it is anticipated that at the end of the day, many transactions will occur outside of the ROFO process. It is anticipated that many QS holders would simply find an active crewmember, either through personal knowledge or a broker, and sell directly to them for the 10% portion. ABSC will be asking members to provide documentation on these sales and will be following up with audits to ensure compliance.

Finally, it is important to consider that crew are provided not just a ROFO for 10% of crab QS being sold, but they also hold a ROFO for the remaining 90% of crab QS being sold in conjunction with active fishermen, as defined above in the active participation section.

#### **Other options considered and disregarded:**

The primary alternative option considered to the industry proposed solution was an alternative which would have provided a "compensated reallocation" of crab QS for crew. Under this alternative, crew would have had the ability to purchase a small (around 5%) of A share QS. This A share QS purchased by active crew would then be reallocated as C share QS. The intention was to increase the size of the C share pool that only active crew could purchase in the future.

There are numerous issues with this alternative. First, A share QS is matched one for one against PQS while there is no similar matching for C share QS. As more A share QS is converted to C share QS, the amount of PQS is diminished. As a result, both harvesters and processors are affected by this sort of alternative. In addition, communities are also affected. Since PQS is associated with community ROFRs, the more PQS is diminished, the greater the negative impact there is for crab dependent communities. It soon became obvious that pursuing this alternative would be extremely complicated and contentious.

Industry believes that the proposed solution described earlier in the section provides similar benefits to crew without these serious unintended consequences.

#### **Compliance by non-ICE Coops:**

ABSC has been working with other non-ICE cooperatives on this proposed solution. Feedback received is that there is wide acceptance for this solution. ABSC is not aware of coops that hold any meaningful amount of quota that are opposed to this approach. It is expected that ICE/ABSC likely would act as a central administrator for the program.

#### **Enforcement:**

In order for crew who believe they qualify as active to be admitted to the ROFO notification list, they would need to explain how they meet the definition. In addition, it is a fairly straightforward process to

audit the QS database and determine who has sold and purchased QS over the past year as well as any address changes for existing QS entities to determine compliance. If there are transactions that have occurred by members in breach of the ROFO agreement, either liquidated damages or expulsion from the cooperative would occur.

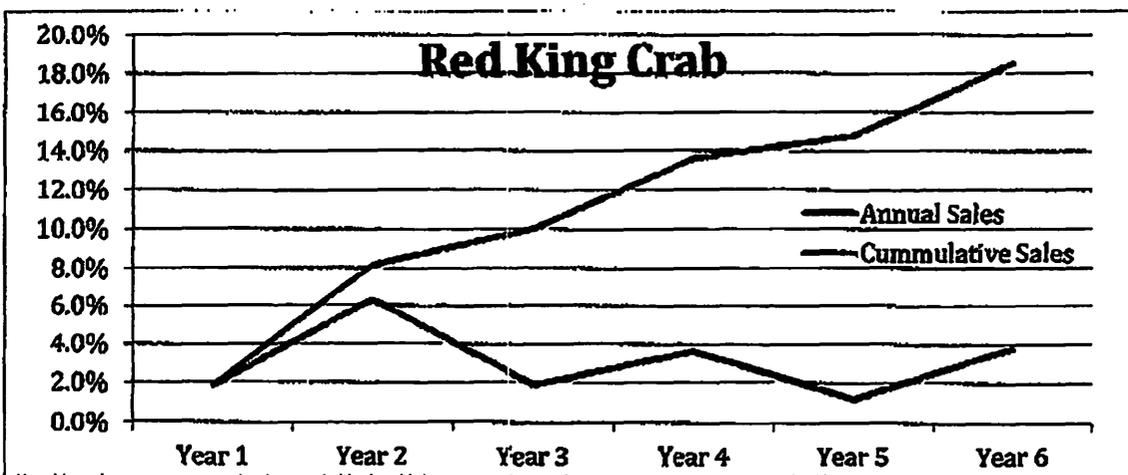
**Annual voluntary reporting:**

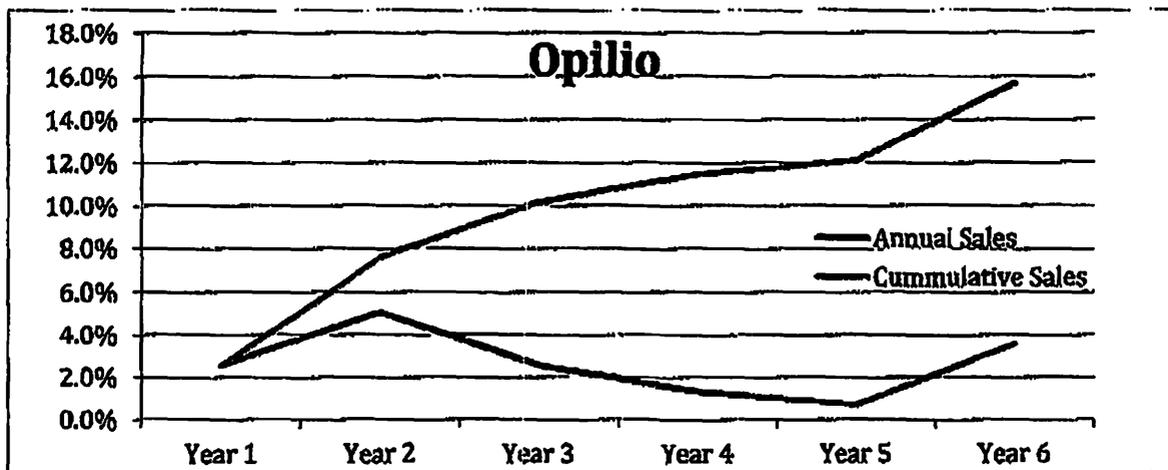
It is anticipated that the industry would provide annual reporting to the Council regarding the number of sales that have occurred that participated in the active crew ROFO process, the number of sales that occurred that closed outside of the active crew ROFO process but resulted in active crew purchasing, and finally the number of sales that occurred where active crew were not able to purchase QS as part of the transaction. In addition, industry would anticipate that reporting would need to be provided regarding the actual active membership agreement in place to address crew investment opportunities. It is possible that it may be necessary to refine the crew investment opportunity agreement in the future and any such changes would be communicated to the Council.

**Analysis and likely results:**

This action will help to ensure that crew have a much stronger ability to have access to purchase crab QS. In the past, when large blocks of crab QS were on the market through a broker, crew had an extremely limited opportunity to purchase this quota. The broker's incentive is simply to sell the quota with the least effort as possible. This meant that in most cases he would call those people with deep pockets who had contacted the broker in the past about an interest in purchasing crab QS. The quota would be sold to one of these folks and crew would be bypassed. This action will force sellers and brokers to provide crew an opportunity to purchase at least 10% of most QS sales in the future.

Below are charts showing the amount of crab QS that has been sold on an annual basis as well as cumulatively for both red king crab and opilio.





Clearly, there has been a substantial amount of crab QS sold since the inception of the crab program. Nearly 16% of opilio has turned over while over 18% of red king crab has changed hands. In addition, there does not appear to be a slowing trend occurring in the scale of sales in either fishery. As a matter of fact, the most recent year showed a higher than average level of sales of QS.

It is difficult to determine exactly what would have happened had the industry incorporated this proposal from the beginning of the program. Clearly though, crew would have had a much better opportunity to compete to purchase crab QS. They would have had a preferred status to purchase quota through the right of first offer for 100% of the quota that was sold (minus the portion that would have met exemptions, which is difficult to quantify). This would have been a tremendous opportunity for crew but the timing may not have been advantageous since financing of crab QS may have been an issue.

This past summer, money for the NMFS crab crew loan program finally became available. This program will provide crew with subsidized financing at extremely competitive rates and terms. This is a tremendous advantage for crew. The timing of the NMFS crab crew loan program as well as the proposed action on behalf of industry to help crew invest in crab is advantageous. Between the NMFS crab crew loan program, and this proposed action, crew will have a tremendous opportunity to purchase crab QS in the future.

## Crew Pay and Leasing

### **Background:**

At their December 2010 meeting, the Council identified *issues of equitable crew compensation and quota lease rates* as an issue for industry to focus on and propose solutions back to the Council. The primary concern is that harvest fees have resulted in issues with equitable crew pay. Discussions during the ad hoc Crab Industry Workgroup meetings characterized this issue as pertaining only to a subset of the fleet and the majority of the concern was with the red king crab fishery. This is due to the fact that EDR data has shown that vessels in the fourth quartile (fishing the most pounds) of red king crab have shown a gradual but steady decline in the percentage of gross revenues that are paid to crew since the program has gone into place (Opilio has not shown a similar trend). Industry believes that in many cases, the vessels in this category are those vessels which are "new entrants" into the fishery where the vessel owner specifically purchased a crab vessel to operate in crab through the leasing market. These owners have little owned crab QS and therefore are nearly completely dependent upon leasing quota.

From the industry's perspective, it is important to recognize the investment made by these new entrants and craft solutions that do not hamper their ability to continue as going concerns in the future. It is also important to point out that many of these new entrants would have had an extremely difficult time entering the fishery prior to the crab program. The fact that there are new entrants following this business model at all shows that there are profits to be made even if all quota is leased. These vessels are providing crew jobs, which would not otherwise be available, even if the crew jobs are not as high paying as on vessels where not all quota is leased. Crew on these vessels understand "the deal" when they are working on the boat, and just as in any labor market, crew who prove themselves can move up to a vessel that has a model that does not rely solely on leasing in the future.

At the end of the day, these new entrant vessels provide jobs to crew that would not be there otherwise. Most likely, quota fished on these vessels would have been fished on established vessels that are currently fishing and would have resulted in more consolidation in the industry and fewer jobs.

Industry believes that the vast majority of vessels that fish crab do not charge harvest fees on what is deemed the "initial allocation". In fact, there are several instances that industry is aware of where the purchaser of a vessel and quota continued to provide the initial allocation to crew free of any harvest fees even though they paid full market price for the QS. Just as has always been the case in the fishing industry, some vessel owners pay crew more than others for a multitude of reasons. With the crab program, it is more transparent to crew before they begin fishing what the final crew pay will be.

Industry further believes that for all crab fisheries, total pay for crew has been better than expected. Pay per crew day has actually increased slightly for red king crab and stayed the same for opilio. This is using EDR data from the 5 Year Review which was prior to significantly higher ex-vessel prices. Industry expects that crew pay per day is considerably higher now than it was before the crab program.

Having said this, there are concerns in the industry that there has continued to be upward pressure on red king crab harvest fees. Several factors have resulted in this upward pressure. First, red king crab is very profitable and prices have moved strongly higher in recent years. This has allowed vessels to pay higher harvest fees and continue to be quite profitable. Second, vessels dependent upon leasing have been very competitive in order to maintain their business relationships. As these vessels generally don't

have a long history in the fishery, they compete more on price than other vessels which can rely more on long standing relationships or reputations within the industry. Third, red king crab quotas are announced so late that vessels are generally already underway to Dutch Harbor by the time the TAC is announced. As a result, harvest agreements have already been signed before TACs are announced. For the last couple of years, the fleet has expected significant declines in red king crab TACs, so vessel owners have been more competitive to insure they have leased enough quota to make it worth their while to send their vessel fishing.

Taking these factors into account, the industry considered a solution that would have capped the harvest fee percentages that could be deducted from vessel revenues before calculating crew pay at 50% for opilio and 65% for red king crab. Under this approach, vessel owners could have paid harvest fees higher than 50% or 65%, but they simply could not have charged the percentage in excess of the proposed caps against crew pay.

Unfortunately, there are significant legal issues associated with this approach. Under the 1982 case *Arizona v. Maricopa County Medical Society*, the Supreme Court held that an agreement to establish a fee cap is illegal price fixing activity under Section 1 of the Sherman Act. Further, the Court held that an agreement of this type is illegal "per se", which means that parties to the agreement would not have an opportunity to demonstrate to the court that the fee cap has a legitimate purpose and no anti-competitive effect. Because of the serious problems posed by the Maricopa County decision, the industry has dropped the harvest fee deduction cap approach.

The antitrust law exemption granted to cooperatives formed under the Fishermen's Collective Marketing Act (FCMA), such as ICE, could potentially allow cooperative members to agree on the maximum harvest fee that non-fishing members would receive from members harvesting cooperative IFQ. Ironically, that exemption does not appear to cover agreements concerning crew share calculations.

ICE members have considered adopting a maximum harvest fee agreement. Unfortunately, not all cooperatives holding crab IFQ qualify under the FCMA. Given the Maricopa County decision, non-FCMA cooperatives clearly cannot risk the liability exposure associated with adopting caps on harvest fees. Under these circumstances, ICE members have concluded that it would not be appropriate for FCMA cooperatives alone to adopt a harvest fee cap, as ICE members believe any solution to the crew compensation issue should equitably apply to the entire crab fleet, and should not create an incentive for QS holders to migrate to non-FCMA cooperatives.

In meetings with crew, it was obvious that there was disappointment that a formal mandatory standard addressing the crew compensation issue could not be adopted for the 2011-2012 seasons. ABSC and ICE took this feedback seriously, and ICE asked its non-fishing members to consider voluntarily accepting harvest fees no greater than 50% for opilio and no greater than 65% for red king crab.

It is estimated that approximately 74% of the ICE QS holders adopted this voluntary arrangement for 2011-2012. This is significant as ICE represents approximately 70% of all QS. These voluntary measures show good faith to tackle tough issues and will result in real and significant increases in crew pay for the coming fishing year. Most importantly, industry was able to react much more quickly than any sort of Council action.

### **Explanation of Potential ICE Solution:**

As discussed above, ICE simply can't implement a mandated membership agreement that either violates law or results in significant risk in undermining the entire cooperative. As a result, a mandatory solution is not being considered at this time.

However, if the Council continues to be concerned about leasing impacting crew pay in the future, ABSC/ICE will communicate the Council's concerns to their members, and request they voluntarily take the Council's concerns into consideration. Further, ICE could develop a survey to determine its member's harvest fee and crew compensation practices. This sort of survey would provide more rapid feedback to industry and the Council and help determine if there is a continuing issue, and if so, the severity. In addition, EDR data would continue to compile both gross revenue and crew pay data at a high confidence level.

### **Other options considered and disregarded:**

There were several options considered to address the Council's concerns. As discussed earlier, any mandatory solution is simply not possible.

The main solution that was considered prior to fully understanding the legal ramifications was a mandatory agreement among all harvesting cooperatives that would limit the amount of harvest fees that could be deducted against crew pay both for opillo and red king crab. This option was favored by many as it was thought to be able to be implemented fleet wide (from the beginning, there were legal concerns of a mandatory harvest fee cap for non-ICE coops). This suggested solution also would have allowed for some competition which may be beneficial for vessels with a shorter history in the industry and more dependent upon competition rather than a long term relationship. Finally, it was viewed that this approach would in effect lower lease rates as vessel owners would feel the full effect of harvest fees above the standard. Harvest fees may be somewhat higher than the standard on some vessels, but in general, it would be expected that harvest fees would gravitate close to the standard.

There were other solutions discussed in the Workgroup process. However, these suggested solutions not only would have the same (if not worse) legal issues to implement, but they also would be unacceptable and quite disruptive to a significant portion of the fleet.

One such suggestion brought forward was the idea that there be a standard that crew are paid at least a set minimum percentage of gross revenue. The issue with this proposal is that if the standard is set at a level that is not disruptive for new entrants, the standard would be more or less meaningless. If you set the standard at the current average percentage of the gross, it would be very disruptive as many vessel owners simply would not be able to compete. Those vessel owners with lesser ownership of QS were adamantly opposed to this proposal as they felt it would change the playing field dramatically and they could not compete. The likely effect may be greater crew pay for some crew but also reduced crew in general as a meaningful amount of vessels would drop out of the fishery and the quota likely would be consolidated on existing vessels, particularly in the red king crab fishery.

Another approach considered was to implement a cap on the harvest fee on all QS holders. In essence, this would mean that no QS holder in ICE could receive harvest fees in excess of a certain percentage. There were several reasons this was not seen as a viable solution at this time. First and foremost,

affiliated cooperative representatives have stated repeatedly that they are not at all comfortable with this approach as it could be construed as collusion. Even if ICE could implement such a provision (it may be possible to do so as it is an FCMA cooperative and is exempt from some anti-trust law) there is concern that ICE members may shift membership to affiliated cooperatives who would then have less restrictive membership agreements. In addition, there are concerns that a consistent cap on the harvest fee on all QS holders would limit the ability of new entrants to compete in the marketplace. Many new entrants depend upon leasing QS and may not have the long term established relationships others in the industry have. Instead, they must rely more on providing a competitive harvest fee to QS holders in order to secure the quota they need to continue in the industry. This opportunity is removed from these vessels if a consistent cap on the harvest fee for all QS holders is implemented.

#### **Compliance by non-ICE Coops:**

ABSC made a request of its members that they consider voluntarily limiting the harvest fee that QS holders receive this year at 50% for opilio and 65% for red king crab. Although a similar request could not be made of non-ICE affiliated cooperatives, it would appear that a majority of these cooperatives are already operating at these levels.

#### **Enforcement:**

As these solutions are voluntary, there really is no enforcement. However, the crab industry is aware that EDR data will continue to be collected and that we will continue to be measured by this data. This continues to provide a strong incentive for industry to be good stewards and seriously consider any requests or recommendations from the Council.

Industry would much rather proactively address issues privately and voluntarily in a manner that provides the Council the level of confidence they feel is necessary so as to not take action. It is important to note that this is not the first time the Council, or other regulators, have provided the Bering Sea Crab Industry the ability to solve issues privately and voluntarily. For example, during the first year of the Crab Program, an issue of highgrading occurred among many of the participants. The industry quickly agreed to voluntary measures to not highgrade in the future. This has not been a problem since. In addition, several years ago, the Alaska Board of Fish agreed to remove pot limits from the Bering Sea crab fisheries. Enforcement requested industry to not use more than 400 pots per vessel in the future and industry has voluntarily agreed. These examples show industry does take requests by regulators seriously and adheres to voluntary agreements, as best as possible, even with little or no immediate enforcement.

#### **Annual voluntary reporting:**

As mentioned earlier, it is expected that each cooperative would request its harvesting members to complete a short survey after the opilio season. This survey could ask the following questions:

- Do you lease IFQ?
- If so, what percentage of your effective harvest fee is charged against crew?
- Have you otherwise adjusted the basis on which you calculate crew percentages?

A similar survey could also be sent to QS Holders asking what their average harvest fee percentage was.

ICE/ABSC would expect to annually provide results from this survey to the Council. The results would help industry and Council determine levels of compliance, if there indeed are issues with leasing and crew pay, and trends as we move forward. Again, this survey would provide information more rapidly to the Council than current EDR data.

#### **Analysis and likely results:**

Feedback from Industry Workgroup meetings has focused much of the attention regarding the crew pay/leasing issue on the Bristol Bay red king crab fishery. As a result, most of the comments in this section will also focus on the Bristol Bay red king crab fishery.

ABSC designed a simple model to determine what the potential benefit may be for crew on vessels under various circumstances assuming acceptance within ICE of the voluntary request to cap harvest fees at 65% for Bristol Bay red king crab. The model was based on assumptions from the most recent 2011 Bristol Bay red king crab fishery. Some of the key assumptions are:

- Crew size (including skipper) is 6.
- Average pots hauled per day is 85 (likely conservative).
- A total of 10 "overhead" days were included which represents work done before and after the season, which is standard for this sort of reporting.
- Ex-vessel price is \$10/lb which is likely conservative.
- Net crew share is 35% which assumes fuel, food and bait already deducted but not harvest fees (if there were any given the vessel scenario shown below).

Following are the results of the model based on the above assumptions using four different vessels utilizing separate business strategies currently employed on a regular basis in the Bering Sea crab fishery.

Vessel A represents those vessels that were initially issued an average allocation of QS and have continued fishing their allocation without leasing any crab and without charging harvest fees to crew on this initial allocation.

Vessel B represents those vessels that were issued an average allocation of QS and have leased a small portion of crab to supplement their initial allocation. Harvest fees are charged to crew on the leased crab but not on the initial allocation.

Vessel C represents those vessels that were issued an average allocation of QS but have leased a large portion of crab to supplement their initial allocation. Again, harvest fees are charged to crew on the leased crab but not on the initial allocation.

Finally, Vessel D represents those vessels who could be considered new entrants. In most cases, they were purchased after the crab program began and therefore did not receive an initial allocation. Their business model is based entirely on leasing and therefore all quota caught has a harvest fee charged to crew.

Under the below scenario, Vessel A does not charge a harvest fee while Vessels B and C charge the previous standard of 70%. Vessel D charges a more competitive harvest fee of 75% in order to attract more crab to fish. Surprisingly, as can be seen in the results below, Vessel A (which doesn't charge any harvest fee to crew) and Vessel D (where all crab is charged a harvest fee) have very similar crew pay per day. The reason is simply because both vessels are investing the same amount of time before and after the season (overhead days) to get the boat ready and wrap up. The overhead days make up a large portion of the total days fished for Vessel A while overhead days make up a much smaller portion of the total days fished for Vessel D. This shows the tremendous efficiencies gained by crew from the program due to the ability to lease.

Pre-Voluntary Measures	Vessel A	Vessel B	Vessel C	Vessel D
Owned (no Lease) LBS	28,000	28,000	28,000	0
Leased LBS	0	50,000	200,000	250,000
Current Harvest Fee	0%	70%	70%	75%
Pay/Day per Crew Member	\$ 1,390.07	\$ 1,686.27	\$ 2,116.84	\$ 1,422.76

With the above information, it was fairly straightforward to simply change the harvest fee from 70% (or 75% for Vessel D) to 65% in the model to determine what the results to crew would be on a daily basis with acceptance within ICE of the voluntary request. Following are the results from this exercise:

Post-Voluntary Measures	Vessel A	Vessel B	Vessel C	Vessel D
Owned (no Lease) LBS	28,000	28,000	28,000	0
Leased LBS	0	50,000	200,000	250,000
Current Harvest Fee	0%	65%	65%	65%
Pay/Day per Crew Member	\$ 1,390.07	\$ 1,784.31	\$ 2,357.39	\$ 1,991.87

With this year's standard 65% harvest fee for Bristol Bay red king crab within ICE, it is clear that crew are making substantially more per day, particularly on vessel that are most dependent upon leasing. Below is information showing the difference in crew pay per day before and after acceptance within ICE of the 65% harvest fee.

	Vessel A	Vessel B	Vessel C	Vessel D
Pay/Day Difference	\$ -	\$ 98.04	\$ 240.55	\$ 569.11

Not surprisingly, crew on vessels that do not lease are unaffected. What is surprising is the benefit to crew on vessels which are more dependent upon leasing. For example, crew on vessels completely dependent upon leasing (Vessel D) are estimates to make an average of \$569.11 more per day with the voluntary measures than before.

Conversations with managers of various vessels reveals that the benefit that crew on highly lease dependent vessels (\$569.11/day) received from industries voluntary measures is actually greater than the total average daily pay of the same crew when they prosecute other non-catch share fisheries on the same vessel, such as pot cod fishing! Clearly crab crew are making a multiple of pay per day in crab (even on vessels that only lease crab) versus other fisheries with fewer risks and less demanding conditions. Industry hopes to provide more information on this topic for the Council meeting. ABSC's efforts have substantially benefited crew and lowered harvest fees in the ICE cooperative.

Obviously, with a voluntary approach, there may be concerns of ICE/ABSC complying in the future. However, the fact that there will be annual surveys and reports and knowing this is a concern of the Council, there will continue to be a strong push to voluntarily request ICE/ABSC members to continue to comply. The last thing industry would like to see is the Council taking any sort of action on this topic. ICE/ABSC are very much aware that if reporting shows low compliance, the Council will likely be incented to delve into a regulatory solution in the future. Therefore, ICE/ABSC has a very strong incentive to show success in the future.

### Next Steps

Assuming the Council concurs with the proposed solutions to crab 5 year review issues, ICE/ABSC will work to implement membership agreement changes to address active participation and crew investment opportunities. ICE/ABSC will also continue with our voluntary approach to cap harvest fees of our members. Finally, ICE/ABSC will develop the necessary infrastructure, protocols, surveys, and reports in order for these solutions to be successful. ICE/ABSC would expect to continue to update the Council regarding our progress at future Council meetings.

### Conclusion

Over the past year, numerous industry meetings have resulted in the aforementioned solutions to address issues raised during the crab 5 year review. Although they may not be perfect (no solution ever is), they do address the issues raised by the Council and are minimally disruptive. These solutions show good faith on industries part and do not result in additional regulatory action or implementation by NMFS. Finally, the Council will have better visibility to these issues under the industries proposed solutions due to robust surveying and reporting. ABSC believes that that this is one of the most comprehensive voluntary responses to address Council concerns and would like to thank the Council for this opportunity.

**MUNDT MACGREGOR LLP**  
ATTORNEYS AT LAW

Telephone (206) 624-5950  
Facsimile (206) 624-5469  
www.mundtmac.com

FISHERMEN'S TERMINAL OFFICE  
4005 20<sup>th</sup> Avenue West • Suite 221  
Seattle, WA 98199-1290

BAINBRIDGE ISLAND OFFICE  
271 Wyatt Way NE • Suite 106  
Bainbridge Island, WA 98110-2873

*Joseph M. Sullivan*  
Direct: (206) 995-8286  
[jsullivan@mundtmac.com](mailto:jsullivan@mundtmac.com)

*Reply to Fishermen's Terminal Office*

November 29, 2011

Mr. Eric A. Olson, Chairman  
North Pacific Fishery Management Council  
605 W. 4th Avenue, Suite 306  
Anchorage, Alaska 99501-2252

SENT VIA FAX

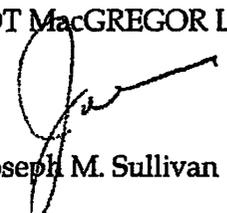
Re: Agenda item C-4(b), Binding Arbitration under the BSAI Crab  
Rationalization Program

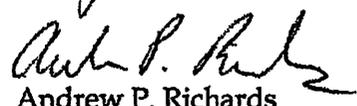
Dear Chairman Olson:

We represent the Inter-Cooperative Exchange ("ICE"), a cooperative of crab QS/IFQ holders. ICE negotiates and, when necessary, arbitrates crab price and other delivery terms under the Arbitration System of the BSAI Crab Rationalization Program. In connection with the Council's Five-Year Review of the Program, attached is a paper that describes the Arbitration System and reports on the practical aspects of its implementation.

Sincerely yours,

MUNDT MacGREGOR L.L.P.

  
Joseph M. Sullivan

  
Andrew P. Richards

Enclosure

## Arbitration under the Crab Rationalization Program

Submitted on behalf of the  
Inter-Cooperative Exchange ("ICE")

November 29, 2011

Prepared by: Erling E. (Jake) Jacobsen, ICE Executive Director  
Joseph M. Sullivan, Mundt MacGregor L.L.P.  
Andrew P. Richards, Mundt MacGregor L.L.P.

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## I. Introduction.

One of the unique aspects of the Crab Rationalization Program is the requirement that 87% of the crab harvested using catcher vessel individual fishing quota ("IFQ") be delivered to processors holding an equivalent amount of "individual processing quota" ("IPQ"). IPQ entitles its holder to a certain percentage of the crab processing market. So in a year when 10 million pounds of crab are available for harvest by holders of catcher vessel IFQ, an IPQ holder is entitled to a certain percentage of 8.7 million of such pounds. IPQ thus allocates the processing market for that crab and eliminates competition among processors for the related deliveries.

Prior to rationalization, the crab processing market was highly competitive. Harvesters solicited price offers from processors and delayed fishing until they received an acceptable offer from at least one processor. Other processors would have to match the price offer in order to maintain market share. *Final Environmental Impact Statement for Bering Sea and Aleutian Islands Crab Fisheries ("Final EIS")*, August 2004, Appendix 1, pp. 114-15.

By allocating the processing market, the Crab Rationalization Program eliminated the tools harvesters used to obtain competitive ex-vessel prices. If an IPQ holder is guaranteed to receive a certain number of pounds regardless of the price that it or any other IPQ holder may be paying, what is its incentive to offer any price other than the bare minimum necessary to cover an IFQ holder's harvesting expenses?

This concern is not speculative. The anticompetitive effect of dividing markets by allocating suppliers is well recognized. Agreements to that effect are treated as the equivalent of price-fixing and other hard-core cartel activity. Courts conclusively presume such agreements to be illegal, without inquiring into their claimed business purposes or procompetitive benefits. *Antitrust Guidelines for Collaboration Among Competitors*, issued by the Federal Trade Commission and the U.S. Department of Justice, April 2000, p. 3.

To mitigate the anticompetitive effect on ex-vessel price of allocating the processing market through IPQs, the North Pacific Fishery Management Council ("Council") developed a system for resolving price and delivery term disputes. Under the "Arbitration System" described at 50 C.F.R. § 680.20, a catcher vessel IFQ holder may initiate "Binding Arbitration" against an IPQ holder if they are unable to successfully negotiate delivery terms. Binding Arbitration serves as the linchpin of the Crab Rationalization Program by providing a mechanism to establish competitive market discipline in a setting where it would otherwise be lost.

This paper describes the structure of the Arbitration System and provides ICE's perspective on its practical impacts to date. The good news is that for every rationalized crab fishery save for one, arbitration has become an extremely rare event. The harvesting and processing sectors in those fisheries are successfully negotiating delivery terms for the vast majority of crab landings. The exception is the Aleutian Islands golden King crab fishery, in which price negotiations with some IPQ holders remain comparatively difficult. IFQ and IPQ holders are making efforts to find a solution that benefits both sectors in that fishery. The prospects for a negotiated solution have improved as the market value of golden King crab has increased substantially in the last couple of years. ICE therefore believes Council action to address delivery term negotiations in the golden King crab fishery is not necessary at this time.

## **II. IPQ Necessitates Arbitration.**

The Arbitration System is necessary because of one of the unique features of the Crab Rationalization Program—"processor quota shares" ("PQS") and IPQ. Each unit of PQS entitles the holder to process a certain percentage of the annual available resource for each rationalized crab fishery. That percentage is annually translated into pounds of crab in the form of IPQ.

The total amount of IPQ is equivalent to the total amount of Class A catcher-vessel IFQ issued to the harvesting sector. Class A IFQ constitutes 87% of the catcher-vessel IFQ issued each year, with the remaining 13% divided between Class B (10%) and Class C (3%) IFQ. All such IFQ is generated from underlying harvester "quota shares" ("QS"). IFQ may be issued to the QS holder or to a harvesting cooperative that the QS holder has joined.

As with halibut and sablefish IFQ, crab harvested under Class B and C IFQ may be delivered to any processor. There is no similar freedom with Class A IFQ—it is required to be delivered to holders of corresponding IPQ. The method of pairing Class A IFQ holders with IPQ holders is called "share matching." Class A IFQ holders and IPQ holders may consensually agree to "match" with each other during the "voluntary share match" period lasting five days from the time that the National Marine Fisheries Service ("NMFS") issues IFQ and IPQ for a crab fishery. After the voluntary match period expires, holders of uncommitted IFQ may unilaterally commit to deliver their crab to an IPQ holder with uncommitted IPQ. Any holder of uncommitted IPQ must accept all proposed IFQ commitments until it no longer has any uncommitted IPQ available, with certain extremely limited exceptions. Crab harvested under matched Class A IFQ must be delivered to the IPQ holder with whom the IFQ is matched, unless the IPQ holder consents to a different arrangement.

In practice, IFQ and IPQ holders do not negotiate ex-vessel price until after matching. Under those circumstances, if the parties fail to reach agreement on price, the IFQ holder cannot resolve the impasse by simply delivering to a different processor because it must deliver to the IPQ holder with whom it is matched. How are disagreements over price and other delivery terms resolved in that case?

**III. The Arbitration System Provides Recourse if an IFQ Holder and an IPQ Holder Fail to Agree on Delivery Terms.**

To address that critical issue, the Council adopted the Arbitration System now described at 50 C.F.R. § 680.20. The Arbitration System is the consensus product of a Council working group composed of harvester and processor representatives. Under the Arbitration System, IFQ and IPQ holders may engage in voluntary delivery term negotiations informed by a "Non-Binding Price Formula" developed for each fishery by a "Formula Arbitrator." If they are unable to reach agreement on price or other delivery terms, the IFQ holder may initiate Binding Arbitration before a "Contract Arbitrator," who will decide the ex-vessel price to be paid to the IFQ holder and any other disputed delivery terms. Both the Non-Binding Price Formula and the decision of the Contract Arbitrator at Binding Arbitration must conform to an "Arbitration Standard." The Arbitration Standard requires that ex-vessel prices preserve the pre-rationalization "historical division of first wholesale revenues" in the relevant fishery, subject to certain adjustments that may be made to account for post-rationalization developments. The following discussion examines each of these components of the Arbitration System.

- A. The Arbitration Standard mandates an ex-vessel price that "preserves the historical division of revenues" in light of other factors.

The heart of the Arbitration System is the Arbitration Standard. It requires that the Non-Binding Price Formula that informs voluntary price negotiations and the decision of the Contract Arbitrator at Binding Arbitration each "be based on the historical distribution of first wholesale revenues between fishermen and processors in the aggregate based on arm's length first wholesale prices and ex-vessel prices" and "establish [an ex-vessel] price that preserves the historical division of revenues in the fishery," while considering additional factors:

- (1) Current ex-vessel prices, including ex-vessel prices received for crab harvested under Class A IFQ, Class B IFQ, and CVC IFQ permits;
- (2) Consumer and wholesale product prices for the processing sector and the participants in the arbitration (recognizing the impact of sales to affiliates on wholesale pricing);

- (3) Innovations and developments of the harvesting and processing sectors and the participants in the arbitration (including new product forms);
- (4) Efficiency and productivity of the harvesting and processing sectors (recognizing the limitations on efficiency and productivity arising out of the management program structure);
- (5) Quality (including quality standards of markets served by the fishery and recognizing the influence of harvest strategies on the quality of landings);
- (6) The interest of maintaining financially healthy and stable harvesting and processing sectors;
- (7) Safety and expenditures for insuring adequate safety;
- (8) Timing and location of deliveries; and
- (9) The cost of harvesting and processing less than the full IFQ or IPQ allocation (underages) to avoid penalties for overharvesting IFQ and a mechanism for reasonable accounting for deadloss.

50 C.F.R. § 680.20(g)(ii) and (h)(4)(i) (emphasis supplied).

In essence, the Arbitration Standard was designed to maintain the pre-rationalization distribution of first wholesale revenues between harvesting and processing sectors, while allowing each sector to capture efficiencies achieved through rationalization:

[The Arbitration Standard] provides additional definition by directing the arbitrator to decide a price that maintains the historical division of revenues in the fishery, while considering other relevant factors. These additional factors would include product developments and efficiency gains, the benefits of which should generally be distributed to each sector based on the contribution of the sector to those benefits. The committee favors [the Standard] because of the additional guidance the historical division of revenues provides to the arbitrator. Retaining the historical division of revenues is thought to be a fair method of preserving the balance of interests of the two sectors in the fisheries.

*Five-Year Review of the Crab Rationalization Management Program ("Five-Year Review"),* December 2010, p. 112 (quoting *Workgroup on Binding Arbitration, 2002a*) (emphasis supplied).

By providing each sector with the benefit of its improvements in products and efficiency, the Arbitration Standard provides the incentive to make such improvements, notwithstanding the allocated processing market. The Arbitration Standard also maintains the market discipline that would have otherwise been lost in such an allocated market by explicitly allowing for consideration of current ex-vessel prices and first wholesale prices of the processing sector at large.

**B. The Non-Binding Price Formula informs ex-vessel price negotiations and arbitrations.**

The Formula Arbitrator is tasked with developing a mathematical formula—the Non-Binding Price Formula—that preserves the historical division of first wholesale revenues between harvesters and processors. As its name implies, the Non-Binding Price Formula is not binding on any of the participants in the Arbitration System. Instead, it is intended to inform IFQ and IPQ holders in their price negotiations and the Contract Arbitrator in making his or her decision in Binding Arbitration. IFQ and IPQ holders may agree to use any other approach to arrive at a negotiated ex-vessel price. The Contract Arbitrator also has latitude to depart from the price suggested by the Non-Binding Price Formula in making his or her decision in Binding Arbitration, within certain boundaries discussed below.

The Formula Arbitrator is jointly chosen by IFQ and IPQ holders. NMFS will not open the rationalized crab fisheries until a Formula Arbitrator has been selected. Accordingly, either IFQ holders or IPQ holders may essentially hold the fisheries hostage by withholding their consent to anyone other than their preferred Formula Arbitrator.

The current Formula Arbitrator is John Sackton, doing business as "Seafood Data Search." Based on data from State of Alaska fish ticket records, Commercial Operator Annual Reports ("COAR") and other sources, Mr. Sackton has constructed formulae to derive the distribution of revenues under various scenarios. Since 2009, Mr. Sackton has issued draft Non-Binding Price Formula reports for review and comment and has modified his final reports in response. He has explicitly conducted this process with the goal of producing consensus among harvesters and processors concerning the historical distribution of first wholesale revenues and collateral considerations that should be taken into account when applying the formula in a particular set of circumstances.

The ex-vessel price suggested by the Non-Binding Price Formula is typically expressed as a percentage of the first wholesale price, with or without a further adjustment factor. For example, the 2011 Non-Binding Price Formula for Bristol Bay red King crab proposes that the ex-vessel price be equal to 57.44% of the first wholesale price, less an adjustment factor of \$0.4964. *Non-Binding Price Formula for Red*

*King Crab*, August 2011, p. 4. Under that formula, a first wholesale price of \$10.00 would lead to an ex-vessel price of \$5.25. For golden King crab, the proposed formula for 2011-12 is a straight 47.85% with no adjustment factor. *Golden King Crab Price Formula Arbitrator and Market Report ("Golden King Crab Report")*, June 2011, p. 5. That formula would result in an ex-vessel price of \$4.78 on a \$10.00 first wholesale price.

The formulae for the major crab fisheries—Bristol Bay red King crab and Bering Sea snow crab (*C. Opilio*)—have not been changed in four and five fishing years, respectively. Neither harvesters nor processors proposed any changes to those formulae for this current fishing year. *Non-Binding Price Formula for Red King Crab*, p. 3.

On the other hand, harvesters and processors have contested the formula for golden King crab each year for the past seven fishing years—the entire period that the fishery has been rationalized. *Golden King Crab Report*, p. 4. Mr. Sackton initially tried to build consensus around a formula that reflected the historical distribution of revenues in the fishery. In 2008, he proposed a formula that harvesters felt adequately captured that distribution, but processors refused to accept it. Since then, Mr. Sackton has modified the formula from one year to the next to accommodate the sector (harvesting or processing) that expresses the most vociferous dissatisfaction with the prior year's formula. Having reached what he describes as "terminal frustration" for the 2011-12 fishing year, Mr. Sackton has proposed a formula constructed by simply averaging the formulae from the previous four fishing years. *Id.*, p. 5.

- C. The Contract Arbitrator must select the "last best offer" at Binding Arbitration that best "preserves the historical division of revenues" in light of other factors.

This section will discuss the initiation of Binding Arbitration, the Contract Arbitrator's application of the Arbitration Standard at Binding Arbitration, collective arbitration by cooperatives of QS holders, and the streamlined and relatively informal nature of Binding Arbitration.

1. IFQ holders have only one opportunity to initiate Binding Arbitration on price and other delivery terms.

Binding Arbitration on price and other delivery terms is initiated when an IFQ holder notifies the IPQ holder with whom it is matched and selects a Contract Arbitrator from among a pool of potential arbitrators jointly selected by IFQ and IPQ holders. On their face, Arbitration System regulations allow only an IFQ holder to initiate Binding Arbitration. However, an IPQ holder can effectively force Binding Arbitration by simply failing to offer price or other delivery terms or by rejecting an IFQ holder's proposed terms.

IFQ holders are limited to a single Binding Arbitration proceeding on delivery terms per IPQ holder per fishery. Consequently, an IFQ holder cannot initiate one Binding Arbitration proceeding to resolve a dispute regarding advance price, another to resolve a dispute regarding the timing or location of delivery and a third to resolve a dispute concerning final price. As a practical matter, IFQ holders typically reserve Binding Arbitration for final price, which oftentimes is not settled until after product from the season is sold. This gives IPQ holders the latitude to stipulate advance prices and delivery schedules early in the season.

An IFQ holder must initiate Binding Arbitration within 15 days after NMFS issues IFQ and IPQ for a crab fishery, unless a "lengthy season" approach is taken. Under the lengthy season approach, Binding Arbitration is delayed until later in the season. That approach can be adopted by agreement of the IFQ holder and IPQ holder via a "Lengthy Season Agreement" ("LSA"), or it can be imposed by an arbitrator at a scheduling arbitration. Since rationalization, no Binding Arbitration on price or other delivery terms has actually occurred within 15 days of IFQ/IPQ issuance—the few that have occurred have been delayed until later in the fishing year. Such delay is often beneficial to both IFQ holders and IPQ holders as it allows time for more market information to become available. More market data leads to better-informed price discussions, thereby increasing the chance of negotiated, rather than arbitrated, ex-vessel price agreements.

2. The Arbitration Standard guides the Contract Arbitrator's decision at Binding Arbitration and accounts for low-revenue IPQ holders and new product forms.

A Binding Arbitration proceeding typically begins with the participants—an IFQ holder and an IPQ holder—submitting a "last best offer" ("LBO") on ex-vessel price and other delivery terms to each other and the Contract Arbitrator. Following presentations by the IFQ and IPQ holders in support of their respective LBOs, the Contract Arbitrator is required to select the LBO that best comports with the Arbitration Standard. The Contract Arbitrator does not have the authority to substitute his or her judgment and independently construct an ex-vessel price. The decision of the Contract Arbitration is final and binding on the participants in arbitration.

In a simple case, the Arbitration Standard could be applied mechanically. Suppose the Formula Arbitrator has determined that, historically, the ex-vessel price was 50% of the first wholesale price of the crab species at issue. If the first wholesale price received by the IPQ holder in arbitration was \$10.00 per pound, a \$5.00 per pound ex-vessel price could be considered to "preserve the historical division of revenues." The Contract Arbitrator may pick the LBO closest to that price.

More complex cases are not susceptible to such a mechanical approach. One such case is when the first wholesale price of the IPQ holder in arbitration is substantially lower than the wholesale prices of other IPQ holders in the relevant fishery. May the Contract Arbitrator select a price that would effectively give the IFQ holder a share of the IPQ holder's first wholesale price that is greater than the historical division? A converse situation arises when the IPQ holder's first wholesale price is substantially above the prices attained by other IPQ holders (perhaps as the result of a unique marketing program or development of a new product form). May the Contract Arbitrator select an LBO that awards the IFQ holder a share of the IPQ holder's first wholesale price that is less than the historical division? The Arbitration Standard allows the Contract Arbitrator to make both of those adjustments in appropriate circumstances.

*i. Low-revenue IPQ holder.*

Arbitration System factors (1) and (2) support awarding an IFQ holder a larger-than-historical percentage of a particular IPQ holder's first wholesale revenues if the IPQ holder's marketing and sales performance lags behind other participants in the processing sector without reasonable justification. Those factors allow for adjustment of the historical division of revenues based on "[c]urrent ex-vessel prices" and "[c]onsumer and wholesale product prices for the processing sector and the participants in the arbitration." The Final EIS for the Crab Rationalization Program explains the rationale for granting the Contract Arbitrator that authority:

The separation of IPQ holders in the process could limit the effectiveness of the system in protecting IFQ holders who deliver to low revenue IPQ holders. To create incentives for each IPQ holder to increase revenues, the arbitrator will need to consider the performance of the IPQ holder with respect to all other processors in the fishery (including any that do not hold IPOs). A revenue dividing price formula that only considers the revenues of the participating IPQ holder might reduce the incentive for low revenue IPQ holders to improve revenues. On the other hand, a revenue dividing formula that has a component that weights the performance of all processors in a fishery could be used to create an incentive for an IPQ holder to be competitive with others in the industry.

*Final EIS, Appendix 1, p. 393 (emphasis supplied).*

If a particular IPQ holder were not at risk of being compelled to pay an ex-vessel price based on the first wholesale prices of other IPQ holders who made legitimate efforts at marketing their crab, it may be tempted to make little or no

investment in marketing and sales efforts and simply liquidate its crab products on a "fire sale" basis. This is not a theoretical concern – it has actually happened when an IPQ holder had cash flow problems.

If the Arbitration Standard did not allow for ex-vessel price correction under those circumstances, all IFQ holders matched with that IPQ holder would be unfairly prejudiced. It would not matter whether the IFQ holders matched with the IPQ holder voluntarily, early in the share match process, or later on when there were no other options (the "last man standing"). Once IFQ holders are matched with an IPQ holder, they are all in the same boat, regardless of the timing of their match, because none of them can unilaterally deliver to anyone else if price negotiations fail. At that point, the Arbitration System is designed to provide IFQ holders with a means of attaining a fair price when the IPQ holder with whom they are matched fails to make reasonable sales efforts.

This aspect of Binding Arbitration reintroduces some of the market dynamics that existed before rationalization. In those days, harvester representatives would solicit price offers from processors until at least one processor offered a price acceptable to harvesters. Because the crab delivery market was not allocated among processors, other processors would have to match the price leader if they wanted to maintain their market shares. Through that dynamic, processors were essentially compelled to either keep up with the price leaders in the particular fishery or exit the fishery. *Final EIS*, Appendix 1, pp. 114-15.

Although the Arbitration System provides similar discipline, it is actually much more forgiving than pre-rationalization market forces because it does not require the Contract Arbitrator to select an LBO reflecting the highest or even the "fleet-wide average" ex-vessel price. Ex-vessel prices paid and first wholesale prices achieved by other IPQ holders are factors that the Contract Arbitrator must consider but is not required to adopt. ICE has consistently maintained that an IPQ holder whose first wholesale prices lag considerably behind other IPQ holders should not be required to pay an ex-vessel price reflecting a greater percentage of its particular first wholesale price if it made reasonable good-faith efforts at marketing its crab.

This flexible approach is reflected in the ex-vessel prices actually paid under crab rationalization. Far from converging on a leading price or a "fleet-wide average" price, ex-vessel prices have, if anything, varied to a greater degree than they did before rationalization. For example, in the 2010-11 fishing year ex-vessel prices paid per pound of crab delivered under Class A IFQ held by ICE varied from \$7.34 to \$7.54 (a range of 20 cents) for Bristol Bay red King crab; \$2.421 to \$2.61 (range of 18.9 cents) for Bering Sea snow crab; \$3.93 (arbitrated) to \$5.05 (range of \$1.12) for Western Aleutian Islands golden King crab; \$4.106 to \$4.45 (range of 34.4 cents) for Eastern Aleutian Islands golden King crab; and \$4.92 to \$5.10 (range of 18 cents) for

St. Matthews Island blue King crab. Such variability was unheard of prior to rationalization.

Not only has the pressure to match a single leading price dissipated, but so too has the harsh consequence of failing to remain competitive. Processors who failed to match the prevailing ex-vessel price in the pre-rationalization crab fisheries typically lost crab delivery market share until they had no option but to make an uncompensated exit from those fisheries. Under the Crab Rationalization Program, a low-revenue IPQ holder who is unwilling or unable to improve its performance may sell its PQS to a processor who is better positioned to realize greater revenue from the resource. That is a substantial benefit that did not exist before rationalization.

*ii. New product forms.*

The Five-Year Review suggests the Arbitration Standard may prevent an IPQ holder from recovering increased revenues generated by new products and thereby reduce the IPQ holder's incentive to develop such new products:

In addition to fishery-specific factors that may hinder product developments, those developments may be constrained by certain aspects of the arbitration program ... [I]f a formula returns only 30 percent of the first wholesale revenues to a processor, a processor would realize no additional return from a product that costs 30 additional cents to produce and sells for an additional dollar.

*Five-Year Review*, pp. 98, 112. This statement is certainly true if the formula is mechanically applied, without adjustment. But under factor (3) of the Arbitration Standard – which allows for adjustment of the historical division of revenues based on “[i]nnovations and developments of the harvesting and processing sectors and the participants in the arbitration (including new product forms)” – an IPQ holder can make a compelling case that it should realize an additional return above its costs on the increased revenue from the new product.

Using the hypothetical from the Five-Year Review, assume a Non-Binding Price Formula returning 30% of first wholesale revenues to the IPQ holder, and therefore 70% to the IFQ holder. At a first wholesale price of \$10.00 per pound, that formula would return \$7.00 to the IFQ holder and \$3.00 to the IPQ holder. Also assume that while most IPQ holders on average received \$10.00 per pound, a particular IPQ holder received \$11.00 per pound because it developed a new product, at a cost of \$0.30 per pound, for which the market was willing to pay a premium of \$1.00 per pound.

There are at least two ways for that IPQ holder to realize a return on its investment under the Arbitration Standard. First, the Contract Arbitrator may ensure the IPQ holder's recovery of the new product's cost of development by subtracting \$0.30 from the \$11.00 per pound first wholesale price before applying the Non-Binding Price Formula. This would result in an ex-vessel price of \$7.49 to the IFQ holder (70% of \$10.70), effectively reducing the IFQ holder's share of revenues down to 68.1% (\$7.49/\$11.00). The remaining \$3.51 would go to the IPQ holder, or \$0.51 more per pound than it would have received at a \$10.00 per pound first wholesale price (\$3.00). That represents a net increase of \$0.21 per pound after accounting for the \$0.30 cost of product development.

Alternatively, the Contract Arbitrator could apply the Non-Binding Price Formula to the \$10.00 average first wholesale price achieved by the other IPQ holders, with all of the additional \$1.00 per pound revenue going to the IPQ holder – a net increase of \$0.70 per pound accounting for the \$0.30 increased production cost. In that scenario, the IFQ holder would receive the same price that it would have received at a \$10.00 per pound first wholesale price (\$7.00). Its share of first wholesale revenues would effectively be reduced from 70% to 63.6% (\$7.00/\$11.00).

While each approach has its merits, ICE maintains the latter approach is the more appropriate. An IPQ holder that develops a higher-value product should keep all of the additional net revenue generated by the new product, unless the IFQ holder made contributions to or incurred costs associated with the development or marketing of the new product, in which case the additional revenues should be shared. Consistent with this principle, ICE has negotiated and arbitrated prices on a basis under which the Non-Binding Price Formula is applied only to the price attained for brine frozen sections (the main pre-rationalization product form), and has made no claim to the incremental value associated with new product forms. Under this approach, IPQ holders clearly still have an incentive to develop new products.

Finally, to put the issue of new product development in some perspective, it is important to consider its history before and after rationalization. Before rationalization in 2005, the last significant developments in product form – including whole cooked crab, fresh water cooking techniques and live shipping – had occurred by the early 1990s. Since rationalization in 2005, one new product has been developed – fresh cooked crab (i.e., crab that is not frozen after cooking) – along with several new methods of packaging crab product. Rationalization therefore does not appear to have stymied product development in the BSAI crab fisheries. And to the extent that other fisheries may have seen more rapid development of new products following their own rationalization, that is explained by a number of regulatory, geographic and market considerations unrelated to the Arbitration System:

A few characteristics of the Bering Sea and Aleutian Islands crab fisheries have likely slowed product innovation. First, the requirement that all crab harvested in BSAI fisheries be processed live was in effect before the rationalization program began; consequently, the opportunities to make product quality improvements were less than those commonly observed in the transition to share-based management in other fisheries. Secondly, the distance to markets and less reliable air service in remote processing locations pose challenges to processors attempting to innovate with products with relatively short shelf lives, such as live crab and fresh crab. Thirdly, development of new product forms, such as more heavily processed products, may require significant outlay of capital or increases in labor, which may be more costly in remote Alaska communities where most of the crab from program fisheries is processed. Finally, the recent market price for shellfish sections has been so high that processors may have little incentive to produce anything else. The higher price received for value added products, such as meat, may not offset the yield loss of those products.

*Five-Year Review*, p. 98 (emphasis supplied).

3. QS holders may form harvesting cooperatives and collectively negotiate and arbitrate IFQ delivery terms.

The Arbitration System incorporates the collective bargaining tradition of the BSAI crab fisheries. Prior to crab rationalization, a large percentage of the crab harvesting fleet joined the Alaska Marketing Association ("AMA") in an effort to increase their bargaining power in price negotiations with processors. The AMA handled negotiations with processors on behalf of its member harvesters. The relatively large number of potential deliveries from AMA members provided the association with much greater leverage than any individual harvester could ever bring to bear negotiating on its own.

Similarly, under the Arbitration System, QS holders are eligible to join one crab harvesting cooperative per crab fishery. A crab harvesting cooperative receives an IFQ allocation equivalent to the sum of the annual allocations of its members in the applicable fisheries. Members of cooperatives that are not "affiliated" with IPQ holders may collectively negotiate and, if necessary, arbitrate delivery terms with IPQ holders.

ICE is one such cooperative. Members of ICE hold harvesting QS but assign their annual IFQ to ICE. ICE coordinates crab harvesting and delivery on behalf of its members, and represents its members in collective delivery term negotiations and arbitrations.

Collective negotiation and arbitration benefit IFQ holders and IPQ holders alike. As was true for AMA-member harvesters before rationalization, IFQ holders benefit from the increased leverage that additional pounds represent. And both IFQ and IPQ holders benefit from the reduced cost of fewer negotiations and arbitrations covering a greater number of pounds, rather than more negotiations and arbitrations involving smaller amounts.

#### 4. Binding Arbitration is streamlined to minimize expense.

The Arbitration System intentionally lacks many of the formal requirements of civil litigation in state or federal courts. Binding Arbitration can be initiated by a simple email to the IPQ holder and Contract Arbitrator. There is no formal document discovery process in which one side can require the other to produce supporting documents, and the Contract Arbitrator has no subpoena power to compel such document production. There are no depositions of witnesses and no process for exchanging written questions that the other side must respond to, as there would be in court proceedings. Neither side files pre-hearing motions. Instead, the focus of Binding Arbitration is on the hearing itself, which typically takes two days at most.

The streamlined nature of Binding Arbitration keeps costs down. The Five-Year Review estimates that, in its current form, the Arbitration System overall—including the costs of the Formula Arbitrator and the pool of Contract Arbitrators—is anticipated to cost less than 1 cent per pound of crab landed. *Five-Year Review*, p. 119. The cost is shared by IFQ holders and IPQ holders.

The relatively low cost of Binding Arbitration is one key to the success of the Arbitration System. It helps keep the focus of price negotiations on the crab markets themselves, while reducing the temptation to make an offer that accounts for the expense of trying to achieve a better result at arbitration. If there is any downside to the informality of the Arbitration System, it is borne by IFQ holders, who lack the ability to compel IPQ holders to produce product sales documentation in support of their stated first wholesale prices.

#### IV. The Arbitration System Is Working.

Overall, the Arbitration System is generally working well. In all but one of the rationalized crab fisheries, the Non-Binding Price Formula for distributing the revenues from IPQ holders' first wholesale sales is now relatively established.

Arbitration proceedings for the red King, snow (*C. Opilio*) and Tanner (*C. Bairdi*) fisheries have declined in frequency, as IFQ holders, IPQ holders and Contract Arbitrators have developed more familiarity with the Arbitration Standard and a more nuanced sense of how it should be applied. Unfortunately, as noted above, the Non-Binding Price Formula for the golden King crab fishery remains disputed. For that fishery, it appears that a new industry-driven approach may be necessary, which can be achieved without modifying the Arbitration System.

A. Binding Arbitration is a rare event in most fisheries.

Perhaps the best evidence that the Arbitration System is generally working well is the infrequency of arbitrations. For the vast majority of crab delivered under Class A IFQ, ex-vessel prices are determined by consensual negotiation rather than arbitration. In the first six fishing years of the Crab Rationalization Program, there were only eleven (11) Binding Arbitrations on price and other delivery terms across all of the rationalized crab fisheries. Seven (7) of those occurred in the first two fishing years (2005/06 and 2006/07), when IFQ and IPQ holders were still adjusting to the application of the Arbitration Standard. There has not been a price arbitration in the Bristol Bay red King crab fishery since the 2008 fishing year, and only one price arbitration in the Bering Sea snow crab (*C. Opilio*) fishery since the 2006-2007 fishing year. *BSAI Crab Rationalization Report Fishing Year 2010/11*, Sept. 2011, Table 3.8, p. 16. The dearth of arbitrations in most of the rationalized crab fisheries reflects the success of the Arbitration System in facilitating successful price negotiations between the harvesting and processing sectors.

B. The golden King crab fishery would benefit from a new industry-driven approach, which can be achieved without modifying the Arbitration System.

In contrast to the other crab fisheries, the golden King crab fishery has seen an uptick in the number of price arbitrations in recent history. But even in that fishery, there have been only two (2) such arbitrations over the last two fishing years. *Id.* Those two arbitrations reflect the lack of consensus between some members of the harvesting and processing sectors over how revenues from that fishery should be distributed. Some IPQ holders assert that they are either losing money or barely breaking even on their operations in the fishery, even under the most recent Non-Binding Price Formula – which is quite favorable to IPQ holders.

What should be done? The Formula Arbitrator has noted the Arbitration System already provides IFQ and IPQ holders the freedom to negotiate alternative arrangements that are more flexible than the “historical division of revenues.” *Golden King Crab Report*, pp. 8-9. This is consistent with the conclusion of the Five-Year

Review, which predicts that "a few more iterations" of a price formula for golden King crab will be necessary before consensus is reached. *Five-Year Review*, p. 108.

ICE agrees with the Formula Arbitrator that it is within the power of IFQ and IPQ holders to make the golden King crab fishery work for both harvesting and processing sectors. Rather than focusing solely on the most appropriate mathematical division of the existing "pie" from the fishery, the key to the future success of both sectors is "growing the pie" by increasing overall revenues. There are a number of means through which revenues can be increased, including marketing collaborations among IFQ and IPQ holders and the development of new product forms.

Some IPQ holders have recently advocated one approach that would focus only on the existing pie and simply divide whatever profit IPQ holders are able to achieve from the fishery. ICE is opposed to such an approach, because it would essentially resurrect the "division of rents" standard that the Council rejected when it adopted the "division of revenues" standard, and implicates all of the related issues. Specifically, the division of rents standard depends on determining which costs are appropriately charged against the gross revenues from the fishery in the first place, and requires that a proxy standard be developed for distributing the remaining profit. It also comes with an enhanced risk that an inefficient or poorly performing IPQ holder will not be exposed to market discipline, because its revenues and costs would be taken "off the top" before dividing profits. In addition, it would require a fundamentally different approach to resolving price setting disputes, along the lines of a utility rate commission hearing, where the financial books of the participants would be fully available and open to the Contract Arbitrator for review. Overall, the "division of rents" approach would require substantially different rules and procedures than those of the current Arbitration System.

While the harvesting and processing sectors have not yet reached agreement on a better approach to dividing revenues of the golden King crab fishery, negotiations are still at an early stage. ICE is hopeful that an agreed solution ultimately will be reached. IFQ holders and IPQ holders spent the first six fishing years of the rationalized golden King crab fishery attempting to influence the Formula Arbitrator in his development of the Non-Binding Price Formula. The continued disagreement between the harvesting and processing sectors has caused the Formula Arbitrator, in his latest report, to essentially say "you figure it out." Early signs are generally positive that IFQ and IPQ holders have taken this message to heart and will be able to negotiate a mutually-acceptable new approach to the golden King crab fishery. ICE therefore believes no Council action is necessary or appropriate at this time.

## V. Conclusion.

The Arbitration System is generally working well and there is no need for the Council to take any steps toward modifying it at this time. When considering the benefits of maintaining the Arbitration System in its present form against any proposals to alter it, the Five-Year Review best summarizes the case for preserving the Arbitration System:

[T]he arbitration system provides a great degree of stability and certainty to participants in both sectors ... Although many of the participants in the [Crab Rationalization Program] share the opinion that the [Arbitration System] has effectively resolved pricing issues, some participants in each sector have expressed reservations. Some harvesters believe that the system cannot achieve the results (either in ex vessel price payments or in competition in product markets) that would be achieved by a competitive market for landings. Some processors believe the rules of the arbitration (including the unilateral authority of harvesters to initiate arbitration[]) unfairly disadvantage processors[]. While these concerns may be worth considering, it is not clear that adjustments to the arbitration system (even minor ones) are possible without disrupting the stability that it provides.

*Five-Year Review*, pp. 116-17 (emphasis supplied).



Mark Gleason, Executive Director  
5470 Shilshole Ave NW Suite #505  
Seattle, WA 98107  
(831) 419-6993  
[markgleason@gmail.com](mailto:markgleason@gmail.com)  
<http://alaskaberingscraabbers.org/>

Date: November 21st, 2011

To: Eric A. Olson, Chairman  
Chris Oliver, Executive Director  
North Pacific Fishery Management Council  
605 West 4th Avenue, Suite 306  
Anchorage, Alaska 99501-2252

From: The Alaska Bering Sea Crabbers

Re: Agenda item C-4 BSAI Crab Stakeholder reports (5-year review issues)

Following is the proposed Right of First Offer Agreement which is referenced in the Alaska Bering Sea Crabbers (ABSC) Stakeholders report, also submitted to the Council. ABSC represents approximately 70% of the harvesters fishing crab in the Bering Sea. This Proposed Agreement was developed by ABSC in conjunction with Crab Industry Workgroup meetings over the past year. The intention is for this Agreement to become part of the ICE cooperative membership agreement as well as other cooperative membership agreements industry wide.

This proposed Agreement is intended to provide solutions to both active participation and crew investment opportunity issues identified by the Council during the Crab 5 Year Review during the December 2010 meeting. Please note that there may be several slight modifications to the document when presented to the Council during the December 2011 meeting which would reflect feedback from the most recent Crab Industry Workgroup meeting.

Sincerely,

Mark Gleason, Executive Director  
Alaska Bering Sea Crabbers

Edward Poulsen, Advisor  
Alaska Bering Sea Crabbers

Joe Sullivan, Legal Counsel  
Alaska Bering Sea Crabbers

Jim Stone, President  
Alaska Bering Sea Crabbers

**BERING SEA CRAB QUOTA SHARE  
RIGHT OF FIRST OFFER AGREEMENT**

This BERING SEA CRAB QUOTA SHARE RIGHT OF FIRST OFFER AGREEMENT is entered into by and among INTER-COOPERATIVE EXCHANGE, a Washington Fish Marketing Act corporation ("ICE"), and its members (each, a "Member" and collectively the "Members") as of \_\_\_\_\_, 2011 with respect to the following facts.

A. The Members hold certain Bering Sea crab quota shares ("QS") issued under the Bering Sea Crab Rationalization program implemented by National Marine Fisheries Service regulations at 50 C.F.R. 680 et seq. (the "Crab Rationalization Program").

B. The Members wish to promote QS ownership among Bering Sea crab vessel crew members and persons who are actively engaged in commercial fishing in Alaska.

Now, therefore, the parties agree as follows:

1. **Definitions.** For purposes of this Agreement, the following terms shall have the following meanings.

1.1 "Active Fisherman" means a person that either: (i) holds a direct or indirect ownership interest in a Commercial Fishing Vessel as of the Annual Record Date, provides ICE or its agent with the information and documents that ICE requests as evidence of such ownership interest, and is named on the "Active Fisherman" list that ICE maintains; or (ii) is a Crab Crewmember.

1.2 "Annual Record Date" means the annual date selected and announced as such by the ICE Board of Directors from time to time.

1.3 "Commercial Fishing Vessel" means a vessel [option - not less than twenty-nine feet in length overall] that has been employed in commercial fishing in Alaska state waters or in the Federal Fishery Conservation Zone off Alaska during the twelve (12) month period prior to the Annual Record Date. For purposes of this definition, a vessel that is employed in support of commercial fishing as a tender or research vessel shall be considered a Commercial Fishing Vessel.

1.4 "Crab Crewmember" means an individual whom (i) meets the Crab Rationalization Program "C" share recent participation requirements as of the Record Date, as the same may be amended from time to time; (ii) did not receive catcher vessel owner ("CVO") or catcher processor owner ("CPO") QS at initial allocation; and (iii) is named on the Crab Crewmember list that ICE maintains.

1.5 "Person" means an individual, corporation, partnership, limited liability company or other form of business entity

2. Restrictions on Transfer. No Member shall sell any portion of his, her or its QS other than in strict compliance with the terms of this Agreement. Any sale of QS by a Member that is not made in strict compliance with the provisions of this Agreement shall be a material breach of this Agreement. For purposes of this Agreement, selling an ownership interest in an entity that holds QS and does not hold an interest in a Commercial Fishing Vessel shall be considered a QS sale, and an amount of the QS held by the entity proportionate to the ownership interest being transferred shall be subject to the rights of first offer set forth herein.

3. Sales to Crab Crewmembers. A Member may sell some or all of such Member's QS directly to one or more Crab Crewmembers on such terms as the Member and the purchasing Crab Crewmember(s) may agree. Such sales shall not be subject to the rights of first offer granted under this Agreement.

4. Rights of First Offer. A Member who wishes to sell some or all of his, her or its QS to a person who is not a Crab Crewmember (a "Selling Member") may only do so in strict compliance with the procedure set forth in this Section 4, unless the transaction is exempt from the Crab Crewmember and Active Fisherman right of first offer pursuant to Section 5, below.

4.1 Before offering QS for sale to a person who is not a Crab Crewmember, the Selling Member shall notify ICE of the amount of QS offered for sale (the "Offered QS"), and the associated sale terms (the "Offer Terms").

4.2 Upon receiving notice from a Selling Member, ICE shall notify the Crab Crewmembers that ten percent (10%) of the Offered QS is available for purchase on the Offer Terms (such 10% being the "Crew Offer QS"). Each Crab Crewmember shall have fifteen (15) days from receiving such notice during which he or she may irrevocably agree to purchase some or all of the Crew Offer QS on the Offer Terms. If the Crab Crewmember(s) agreeing to purchase Crew Offer QS (the "Purchasing Crewmembers") collectively agree to purchase an amount of QS in excess of the Crew Offer QS, ICE shall allocate the right to purchase Crew Offer QS among the Purchasing Crewmembers pro rata, according to the amount of the Crew Offer QS each of them has agreed to purchase.

4.3 Upon expiration of the 15 day Crab Crewmember offer period, ICE shall determine the amount of the Offered QS available for purchase, net of the amount that Crab Crewmembers have agreed to purchase (such remaining amount being the "Fisherman Offer QS"). The Selling Member may sell the Fisherman Offer QS to one or more Active Fishermen on such terms as the Selling Member and the Active Fishermen may agree. If the Selling Member wishes to sell some or all of the Fisherman Offer QS to one or more persons who are not Active Fishermen, the Selling Member shall first notify ICE, and ICE shall notify the Active Fishermen of the amount of Fisherman Offer QS that the Selling Member proposes to sell to persons other than Active Fishermen (the "Third Party QS") and the Offer Terms on which the Third Party QS can be purchased. The Active Fishermen shall have five (5) days during which one or more of them may agree to purchase some or all of the Third Party QS on the Offer Terms. If the

Active Fishermen agreeing to purchase Third Party QS (the "Purchasing Fishermen") collectively agree to purchase an amount of QS in excess of the Third Party QS, ICE shall allocate the right to purchase the Third Party QS among the Purchasing Fishermen pro rata, according to the amount each of them has agreed to receive. [Deposit required?]

4.4 Upon expiration of the 5 day Active Fisherman offer period, ICE shall determine the amount of the Offered QS that the Crab Crewmembers and the Active Fishermen have agreed to purchase on the Offer Terms, and shall notify the Selling Member. The Selling Member shall then have the right to offer the balance of the Offered QS in excess of the amount that the Crab Crewmembers and Active Fishermen have agreed to purchase (the "Marketable QS") for sale to persons other than the Crab Crewmembers and Active Fishermen (the "Third Parties") on terms no more favorable to the Third Parties than the Offer Terms for a period of one hundred eighty (180) days (the "Market Period").

4.5 If a Selling Member accepts an offer during the Market Period from one or more Third Parties to purchase some or all of the Marketable QS on terms no more favorable to the Third Parties than the Offer Terms (an "Accepted Offer"), the Selling Member shall notify ICE of the Accepted Offer and the proposed closing date for the related transaction, which shall not be earlier than twelve (12) business days from the date of such notice. Within two (2) business days of receiving such notice, ICE shall notify the Purchasing Crewmembers and the Purchasing Fishermen of the Accepted Offer and proposed closing date. Within ten (10) days of receiving such notice from ICE, each Purchasing Crewmember and Purchasing Fisherman shall deposit their share of any cash to be paid to the Selling Member at closing into escrow as directed by ICE, and shall execute and deliver into escrow as ICE directs any financial instruments and other documents consistent with the Offer Terms.

4.6 If the Selling Member transfers QS to one or more Third Parties in accordance with the Accepted Offer, the Selling Member shall notify ICE, and ICE shall notify the Purchasing Crewmembers, Purchasing Fishermen and direct the escrow agent with whom their funds and documents have been deposited to proceed with closing of the QS transfers from the Selling Member to the Purchasing Crewmembers and Purchasing Fishermen.

4.7 If the Selling Member does not transfer any of the Offered QS to a Third Party within the Market Period, the Transferring Member shall not offer any QS for sale unless and until the Selling Member has repeated the first offer procedure set forth in Sections 4.1 through 4.3, above.

5. Transactions Exempted from Right of First Offer. Notwithstanding the foregoing, the following QS sales shall not be subject to the rights of first offer in favor of Crab Crewmembers or Active Fishermen described above.

5.1 QS sales made in connection with a foreclosure of a security interest or pursuant to a court order.

5.2 QS sales made in connection with the sale of a Bering Sea or Aleutian Islands crab fishing vessel, or as part of the sale of an entire commercial fishing business.

5.3 QS transfers or sales between affiliated business entities. For purposes of this provision business entities in which the same person holds a ten percent (10%) or greater voting interest or ownership interest are affiliated.

5.4 Notwithstanding the provisions of Section 2 to the contrary, transfers of a direct or indirect ownership interest in a business entity between or among existing owners.

6. Termination of Crab Crewmember and Active Fisherman Rights for Failure to Perform. In consideration for the benefits extended to Crab Crewmembers and Active Fishermen under this Agreement, each of them shall have an obligation of strict performance in connection with the closing and purchase of any QS they agree to take under the right of first offer that is extended to them under this Agreement. ICE reserves the right in its sole discretion to permanently remove a person from the Crab Crewmember and/or Active Fisherman list maintained by ICE in response to any single breach by such person of their obligations under this Agreement.

7. Breach by a Member. A Member's breach of this Agreement shall constitute a material breach of the ICE Membership Agreement. Because the damages associated with a breach of this Agreement are not possible to quantify, a Member in breach shall be liable for such liquidated damages as the ICE Board of Directors adopts and announces to the Members from time to time, provided no such liquidated damages shall take effect until the next ICE membership period following their adoption and announcement. In addition to imposing liquidated damages in connection with a breach of this Agreement, the ICE Board of Directors may in its sole discretion revoke the ICE membership of a Member who breaches this Agreement.

8. Assignment. The rights granted to Crab Crewmembers and Active Fishermen under this Agreement are personal, and may not be assigned. Any purported assignment of such rights shall be void. ICE may assign any or all of its rights and obligations under this Agreement to such persons as ICE selects in its sole discretion.



# Alaska Bering Sea Crabbers

## Report on 5-Year Review Issues

North Pacific Council  
December 2011

# Participants in the Process

- Alaska Bering Sea Crabbers
- Alaska Crab Coalition
- Crab Group of Independent Harvesters
- Deep Sea Fishermen's Union
- Crew
- NPFMC Staff

# Issues Identified by the North Pacific Council

- Crew Investment Opportunities
- Active Participation
- Crew Pay/Lease Issues

# Council's Request of Industry

- Encourage industry to work together to craft private solutions to issues identified by the Council
- Create an informal stakeholder group similar to Emergency Relief
- Provide the Council with regular reports
- Provide final report to the Council in December 2011

## Industry Representation

- ABSC, ACC, and Crab Group, including vessel owners and quota share holders have created a **5 Year Review Committee**.
- Industry including vessel owners, quota share holders and crew have created an informal **Crab Industry Workgroup**.
- Affiliated Cooperatives and CDQ Groups participated in the discussion.

# Industry Meetings

## Dates of Important Meetings:

### Crab Industry Workgroup (All Stakeholders)

- December 15<sup>th</sup>, February 1<sup>st</sup>, March 18<sup>th</sup>, May 4<sup>th</sup> and June 2<sup>nd</sup>, August 8<sup>th</sup>, October 29<sup>th</sup> and November 21<sup>st</sup>

### 5 Year Review Committee (Vessel & QS Owners)

- Too numerous to list...

### Crab Crew Workshop: May 3<sup>rd</sup>

# Crew Engagement: Crab Crew Workshop

- A Crab Crew Workshop occurred May 3<sup>rd</sup> in Seattle with remote locations in Kodiak and Anchorage
- Speakers included Mark Fina (NPFMC), Clydina Bailey (NMFS RAM), Scott Houghtaling (NMFS Financial Services), Erik Olsen (Farm Credit Services), Jeff Osborn (Dock Street Brokers), Tim Henkel (Deep Sea Fishermen's Union) and Edward Poulsen (Alaska Bering Sea Crabbers)
- Results:
  - informed crew of IFQ opportunities
  - Engage crew in preparation of crew pay and leasing discussion
  - Over 100 attendees combined, most were crew
  - Presentations available on Council website and free DVD of conference available as well

# Right of First Offer (ROFO)

- Applicable fleetwide via co-op membership agreements
- Private with no Council/NMFS action needed
- Layered on top of existing QS ownership requirements
- If no sale, QS can be offered broadly at same terms
- If seller lowers price, must go back through ROFO process

# Crew Investment Opportunities

- Crew have ROFO on 10% of QS PLUS the other 90%
- NMFS Crab Crew Loan Program to provide financing
- 15 days to commit versus 5
- Provides bite size amounts for crew
- Crew list maintained through ICE developed website

# Active Participation

## Right of First Offer (ROFO) Agreement:

- Provides vessel owners and crew a ROFO on 90% of QS sold
- Incentives for QS holders to remain active
- Result will be migration of QS to active participants

# Active Participation and Crew Investment Opportunities

## Voluntary reporting:

- ABSC will monitor changes to public QS database
- Survey sent to purchasers regarding qualification
- Industry to provide annual report after season
- May need to change agreements based on results

# Crew Pay/Leasing

- Mandatory solutions are not legally feasible
- ICE members took individual voluntary measures
- Many ICE QS holders capped lease “ask” at 65% red crab and 50% opilio
- In place past red crab season with strong acceptance
- Ex-vessel over \$10/lb, very good money made @65%
- ICE will continue to communicate importance of these measures to its members

# Crew Pay/Leasing Reporting

- Annual third-party post-season survey of vessels/QS holders
- Survey to ask about harvest fees and crew pay
- Survey results will be aggregated and reported annually

# Conclusion

- Industry has provided reasonable and meaningful solutions to issues raised by the Council
- Industry solutions will take no additional Council or NMFS resources
- Industry solutions can be modified privately in the future if they don't appear to be having intended impact
- The Council will continue to conduct reviews of the crab rationalization program