


MEMORANDUM

TO: Council, SSC and AP Members
FROM: Chris Oliver 
Executive Director
DATE: January 30, 2008
SUBJECT: BSAI Crab Issues

ESTIMATED TIME 14 HOURS (All C-1 items)

ACTION REQUIRED

(f) Initial review of amendments to the arbitration program

~~(g) Discussion paper concerning potential grants of immunity under the arbitration program~~

BACKGROUND

(f) Initial review of amendments to the arbitration program

An important component of the crab rationalization program is the arbitration system that is used to resolve delivery terms between holders of Class A individual fishing quota (IFQ), which must be delivered to a processor holding unused individual processing quota (IPQ). In the first two years of the program, certain technical aspects of the arbitration system have limited the effectiveness of that system. This action includes alternatives that would modify the following three aspects of the arbitration system to improve it effectiveness:

- Removal of the requirement of market reports and non-binding price formulas for fisheries unlikely to open. The action would require arbitration organizations to agree to provisions for the contingency of a fishery opening being announced unexpectedly.
- Modification of the timeline for the golden king crab market report and formula to allow for data from most recent fishery to be used.
- Address staleness of the market reports by allowing those reports to be produced and supplemented at any time (provided those reports contain only publicly available information to allay any potential antitrust concerns).

At this meeting, the Council scheduled an initial review of that analysis. The executive summary is attached (Item C-1(f)(1)).

~~(g) Discussion paper concerning potential grants of immunity under the arbitration program~~

This paper is not ready for this meeting and will be rescheduled for the April meeting.

RIR/IRFA of Provisions Modifying the Arbitration System

Executive Summary

In August of 2005, fishing in the Bering Sea and Aleutian Island crab fisheries began under a new share-based management program (the “program” or “rationalization program”). The program is unique in several ways, including the allocation of processing shares corresponding to a portion of the harvest share pool. Under the program, 90 percent of the annual catcher vessel owner harvest share allocation is issued as “Class A” individual fishing quota (IFQ), which must be delivered in a designated region and may only be delivered to a processor holding unused individual processing quota (IPQ). The program also includes an arbitration system that may be used to resolve ex vessel price and other delivery term disputes for landings of harvests using Class A IFQ. In the first two years of the program certain technical aspects of the arbitration system have limited the effectiveness of that system. This action includes alternatives that would modify three aspects of the arbitration system to improve it effectiveness.

Action to revise market reports and non-binding price formulas for fisheries unlikely to open

Under the current regulations, arbitration organizations representing holders of harvest shares and processing shares are required to contract for market reports and non-binding price formulas annually for each fishery regardless of whether the fishery opens. In the first two years of the program, the St. Matthew Island blue king crab, Pribilof red and blue king crab, and the Western Aleutian Island red king crab fisheries have not opened. Production of these reports is unnecessary, since no landings occurred during this period. A modification of the regulations could be developed to remove the requirement for producing a market report and non-binding price formula for fisheries unlikely to open.

Purpose and need statement

Under the current regulations, market reports and non-binding formulas are required to be generated annually for each fishery regardless of whether the fishery is likely to or does open. This requirement adds to the cost of arbitration by needlessly requiring participants to contract for the production of these documents. An amendment that allows participants to avoid this requirement when a fishery is unlikely to open could save on costs of the arbitration system. The amendment should include provision for the preparation of the market report, in the event the fishery should open.

Alternative 1 (status quo)

Under the current regulations, arbitration organizations representing holders of harvest shares and processing shares are required to contract for market reports and non-binding price formulas annually for each fishery. In the first two years of the program, three of the rationalized fisheries have not opened due to stock conditions. Notwithstanding these closures, the regulations technically require the production of market reports and non-binding formulas. Since these documents are not needed for guiding negotiations in the closed fisheries, requiring these reports would seem to impose unnecessary costs on participants.

While the cost of producing the reports and formulas would seem to be unnecessary, one advantage of the current requirement for these reports is that the decision for opening a fishery is typically made very close to the fishery opening. Current management is structured to allow for the use of the most recent stock information when deciding whether to open a fishery and setting the TAC. By making the announcements shortly before the season opening occurs, arbitration participants are prevented from waiting until the fishery opening is certain before needing to contract for market reports and non-binding formulas. Given that little time is available to produce a report after a final decision on whether to open a fishery, some argument can be made that the unequivocal requirement for a market report and non-binding

formula for every fishery under the status quo could be beneficial for those circumstances when an unexpected decision to open a fishery is made based on the most recent stock information.

The costs of the additional reports required under the current regulation would be a relatively minor additional expense. In addition to the financial costs, the production of additional reports involves some logistical complications. Reports are required to be produced in a compressed period under the current regulations. Requiring additional reports and formulas adds to the burden of the person producing those reports and could limit time available to ensure that all sources fully utilized and are put to their most complete and best uses. In addition, the production of reports could affect the ability of participants to adequately communicate with the market analyst and formula arbitrator concerning reports produced for fisheries that are scheduled to open. This lack of attention could have consequences in future years, if the earlier reports are the starting point for reports in future years.

Alternative 2

In the event that the arbitration organizations representing at least 50 percent of the PQS holders and at least 50 percent of the unaffiliated QS holders agree that a fishery is unlikely to open, neither a market report nor non-binding formula will be required for the fishery. Any such agreement will include provision for the production of the market report and non-binding formula, in the event that an opening is later announced for a fishery, specifying a timeline for the production of those reports. The determination of whether the fishery is unlikely to open would be fully at the discretion of the arbitration organizations. Although managers may be in a better position to make an assessment of the potential for a fishery to open, it is believed by managers that any official declaration (or absence of a declaration) by managers concerning a fisheries closure could confuse participants, if a future, inconsistent determination is made to either open or close a fishery. Managers, in general, have been willing to discuss the potential opening of a fishery with industry, both informally and during meetings with industry, such as the annual Pacific Northwest Crab Industry Advisory Committee (PNCIAC) meetings. From these communications, arbitration organizations and their members can make reasonable decisions concerning the potential for a fishery to open, and whether a market report and non-binding formula are unnecessary.

To fully understand the potential application of this provision, several aspects of this provision should be clearly described. First, in the event the two arbitration organizations disagree concerning whether a fishery is likely to open, a market report and non-binding formula will be required for the fishery under the standard timeline. Second, the arbitration organizations must also agree to terms for the provision of the market report and the non-binding formula, in the event that the fishery unexpectedly opens. This agreement must specify the timeline for production of the report and formula. Given that a contingency plan for developing the market report and non-binding formula are required for the arbitration organizations to use this provision, the risk of fishery participants being left without adequate information to guide their negotiations is limited.

The greatest concern arising from this provision is that fisheries in which the provision is most likely to be used are fisheries for which a market report and non-binding formula have yet to be produced (i.e., the Western Aleutian Islands red king crab, the St. Matthew Island blue king crab, and the Pribilof red and blue king crab fisheries). For fisheries that have been open, these documents are largely derivative of the prior year's report. So, an unexpected opening of a fishery that has had prior reports and formulas will pose less of a time pressure on the market analyst and formula arbitrator contracted to produce the market report and non-binding formula, respectively. Although the cost savings from using this provision to avoid producing unnecessary reports and formulas is rather minor, the provision should provide a benefit to participants who wish to avoid those costs. The provision does pose some risk that participants in a fishery will have inadequate information to guide their negotiations of A share deliveries. This risk arises only in fisheries that have not been opened, which are relatively small fisheries. Also, the risk is reduced to the extent that participants have chosen to wait in or after the season when market prices for production from the fishery's catch is more certain.

Action to modify the timeline for the golden king crab market report and formula does not allow for data from most recent fishery to be used

Under the current regulation, data from the most recent season are not available for use in developing the market report and non-binding formula because those reports are required to be completed 50 days prior to the August 15 fishery opening. A modification to allow an additional 20 days for the completion of the report and formula would enable the market analyst and formula arbitrator to the use of data from the most recent fisheries in the production of the market report and non-binding formula, respectively.

Purpose and need statement

Under the current regulation, the market report and non-binding formula for the Aleutian Islands golden king crab fisheries are required to be completed 50 days prior to the August 15 fishery opening. Under this timeline, data from the most recent season are not available for use in development of those reports. The inability to use data from the most recent season could diminish the accuracy and quality of these reports. Postponing the due date of these reports to a later time in the preseason could allow for more complete and accurate reports that provide timely information to market participants.

Alternative 1 (status quo)

Under the status quo, arbitration organizations are required to contract for delivery of the market report and non-binding formula at least 50 days prior to the fishery opening. The rationale for this timing is that it would allow participants ample time to use the information in negotiations prior to the fishery opening. The timing with respect to the Aleutian Island golden king crab fisheries, however, prevents the market analyst and formula arbitrator from using the most current information from Commercial Operators Annual Reports. Since the golden king crab fisheries open in mid-August, the reports are due in late June. At this time, data from the prior year are typically not fully compiled.

Alternative 2

Under this alternative, the market report and non-binding price formula for the golden king crab fisheries will be required to be completed at least 30 days prior to the opening of those fisheries (20 days later than is required under the status quo). This delay will allow the market analyst and formula arbitrator to use data from the most recent season in preparing their respective reports. Although public sources are not the only source of data relevant to the development of the market report and formula, public sources are reliable for verifying information from other sources and may be deemed more reliable by participants in the fisheries. This greater reliability could aid in reducing disputes during negotiations.

Action to address staleness of the market reports

The current requirement that market reports be complete at least 50 days prior to the season prevents the inclusion of the most current and relevant pricing information in the report. In addition, the prohibition on supplements to the report prevents modification of the requirement to provide useful market information in season or after completion of the initial report. Market reports would be more timely and informative, if those reports can be produced and supplemented at any time (provided those reports contain only publicly available information to allay any potential antitrust concerns).

Purpose and need statement

The current requirement that market reports be complete at least 50 days prior to the season prevents the inclusion of the most current and relevant pricing information in the report. In addition, the prohibition on supplements to the report prevents modification of the requirement to provide useful market information in season or after completion of the initial report. More timely and relevant market information to be used for price negotiations might be provided to participants in the fisheries, if those participants are permitted to negotiate agreeable terms (including due dates) for the provision of a market report and supplements to suit their needs.

Alternative 1 (status quo)

Some participants have questioned the utility of the market report, which is required to be released at least 50 days prior to the season opening. Furthermore, any price information contained in the report is required to be at least 3 months old at the time of release, to prevent the use of private information used in the report for anticompetitive purposes. Because of the timing of the report and the limitations on information it may contain, most participants in the fisheries believe that the information in the reports is stale by the time it would be useful for negotiations. As a consequence, most participants in the fishery have needed to locate other sources of up-to-date information to support their negotiations.

Alternative 2

The regulatory amendment would generally provide that at least 50 days prior to a season opening, the arbitration organizations representing at least 50 percent of the PQS holders and at least 50 percent of the unaffiliated QS holders are required to reach an agreement for the provision of a market report (which may include supplements at any time prior to the end of the season). The market report will utilize only publicly available information. Such an amendment would provide the arbitration organizations with the most latitude to define a market report that will best serve participants in a fishery.

The organizations have already discussed several ways that the market report process could be improved. First, the report can use information gathered from publicly available market reports to periodically inform all participants in the fishery of general market trends. Annually (or more frequently, if conditions merit) an analytical report could be provided to participants from a market expert to provide participants with a synthesized description of the market. Although this alternative structure for market reports sacrifices the use of private information, private information may not be useful, if the primary goal of the report is to provide a general description of market conditions and developments. It should be noted that this change in market report requirements gives extensive power to the arbitration organizations. Currently, a single organization represents unaffiliated harvesters and a single organization represents processor. The organizations have worked amicably to improve the arbitration system and seem to be sensitive to the needs of all members (including members with small holdings and little power). If conditions change (by larger members asserting their position) it is possible that the organizations could agree to do away with all but a minimal market report requirement. This could disadvantage smaller entities that currently rely on the market report as a source of market conditions.

Since the scope of the market report and any supplements would be subject to agreement of the arbitration organizations, its costs are difficult to predict and may change with time and circumstances. Depending on the scope of the agreed report, its costs could increase or decrease. It is likely that the organizations would make an effort to keep costs in most years lower than under the current standard market report requirement.

Overall, this alternative provides the arbitration organizations with the ability to develop a system for providing market information to their members. The flexibility of the requirement should allow the organization to provide the most useful, timely information to participants in need of market information for their price negotiations. The alternative, however, presents some risk (albeit minor) that majority QS and PQS holders could assert their position in the arbitration organizations to provide a market report that is not particularly beneficial to those small share holders, who are likely to derive the greatest benefit from the market reports.

Net benefits to the Nation

A minor overall net benefit to the Nation is likely to arise from this action. Each of the proposed actions are likely to decreasing costs and transaction costs or by improving the quality of information provided to participants in the program.