

Oversight Hearing on “Catch Shares as a Management Option: Criteria for Ensuring Success”

March 16, 2010

Questions for Mr. Edward Backus, Vice President, Community Ecosystems Services, Ecotrust

Questions from Chairwoman Madeleine Z. Bordallo (D-GU)

1. If properly designed, catch share programs can play an effective role in a multi-faceted approach to responsibly managing fisheries. However, poorly designed catch shares can create as many problems as they solve. Would you agree with this statement?

Yes I would. Poor design can generate a variety of negative social and economic effects including; impacts to the culture and structure of fishing communities, increasing debt loads among existing and second generation fishing participants, reduced revenues and access from the practice of leasing, disenfranchisement of crew and their role in successful fishing businesses, disruption of the geographically proximate relationships between communities and natural resources via the migration of the intangible asset of quota shares away from communities through market trading, among other effects.

Well designed catch share programs will draw on the market design principles from other industries where new markets have been created using public trust assets (e.g. the wireless spectrum). In fisheries, good design should address economic, ecological, and social issues. Market design experts suggest that all of these issues can be addressed by market approaches. Some of these approaches were explored by Ecotrust during a market design workshop for catch shares programs in U.S. fisheries at the Harvard Business School in October 2007 (proceedings at: http://www.ecotrust.org/cbfm/WPS4_Fisheries_Mrkt_Design.pdf)

Julia Olson, social scientist with NOAA Fisheries, NE Fisheries Science Center in Woods Hole Massachusetts has conducted a social impact assessment of catch shares in fisheries in detail in the context of the New England scallop fishery. Her report is available here; the New England Fishery Management Council's [September 22-24, 2009 Council Discussion Documents](#). #9a [Environmental Impacts](#) Section 1.5.2 - Pages 93-103.

2. How can catch shares give fishers a “false sense of security?”

The emergence of catch shares as a defacto “property right” has supported the creation of much wealth in the U.S. fisheries sector. But it is hard for fishermen to remember that quota is a privilege that can be revoked, especially after many participants have engaged in successful market transactions to buy or sell quota shares.

First, in terms of allocations, quotas provide no more legal protection to fishermen than regular fishing permits or licenses. Whether a fisherman owns a permit or quota, the government can reallocate commercial catches to settle international or other treaties, or to meet demands of the

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sports-fishing sector. By way of example, in British Columbia, 12 percent of the commercial halibut catch was reallocated to the sports-fishing sector in 2003. There is a similar ongoing process in Southeast Alaska in the halibut sector, this time with litigation. This was done without compensation to halibut quota holders. Catch share quotas don't strengthen the property rights of fishermen to prevent reallocations or in seeking compensation.

Second, catch share quotas do nothing to mitigate ecological uncertainty. Climate change, marine survival rates, habitat damage, predation and other factors cause fish stock levels to fluctuate and thereby create the greatest uncertainty for fishermen. It must be remembered that quotas are generally a defined percentage of the total allowable catch (TAC) and don't represent a specific poundage of fish (even though quota shares are often sold in units of pounds). As a result, when fish stock levels rise and fall from year to year because of environmental conditions so do fishermen's quotas. Quotas will do nothing to mitigate this kind of ecological uncertainty. In fact when TACs decline, fishermen have a tendency to lobby Councils and other management entities (International Pacific Halibut Commission) to set the TAC higher than biological recommendations would suggest. This happened at the IPHC in 2010. In this sense, catch shares tend to develop a sense of entitlement and a resulting sense of betrayal when things must change due to ecological or biological limits.

Third, in terms of market forces, quotas can help fishermen respond better to the market by giving them flexibility to deliver catches when demand and prices are high. However, many fishermen lease quota in pre-season agreements, locking themselves into lease rates per pound. In some fisheries, 60 to 75 percent of the landed value goes to paying quota lease fees. If fish prices drop or fuel costs rise, their profits could disappear. As a result, quota leasing can actually increase fishermen's risk and exposure to changing market forces.

One certain aspect of catch share programs is that some fishermen will opt to lease their quotas if allowed, thus guaranteeing themselves revenue without any risk of having to actually go fishing.

3. In your testimony, you reference the research of Evelyn Pinkerton of Simon Fraser University, who found British Columbia small boat fishermen as “desperate” in the control of processors who dominate the holding of quota shares. Can you expand upon this point?

The term ‘desperation’ demonstrates how extreme the results, feelings, and impacts of allowing leasing in catch share programs can be. The context of the fisheries examined by Pinkerton also demonstrates that the effects are not just about economic efficiency, but have everything to do with fishing culture, community structure and well-being, inter-generational hope, and maintaining a sense that fisheries are a viable business to enter. It is critical to learn from the experience in British Columbia to prevent catch share programs from undermining small boat fishing as a viable small business. Fishing is not viable if it becomes just the labor component in a larger equation of control by non-fishing entities.

Quoting from the Pinkerton and Edwards paper in Marine Policy...

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“Of the 182 active halibut fishing vessels in 2006, 37 vessels leased 90% or more of the halibut quota they fished, 67 vessels leased 70% or more of the halibut quota they fished, and 91 vessels (half the active fleet) leased 50% or more of the halibut quota they fished.... It is impossible to know exactly what percent of leasing creates a marginal operation, because individual situations are varied and complex. But it is clear ... that leasing is by far the largest fishing cost and that operations become increasingly less profitable, the more of their quota they must lease. It is also clear ... that a significant number of operations—more than a third of the fleet—currently fall in the less viable or marginally viable category (those leasing 70% or more of the quota they fish).”

“Why do lessee skippers continue to fish if their operations are marginal? Why do not they correctly receive the market signals that they are financially non-viable? Economic theory predicts that such marginal operations will simply cease to lease quota and find more profitable employment. But there are many reasons why marginal operations continue. Sometimes a vessel owner leases quota to pay for the maintenance of the vessel. A vessel may serve multiple subsistence, transportation, identity, or prestige functions, or maintaining it may simply represent the hope that the price will go up. Operating a vessel may be the best or only way to offer a job to a son to help pay for his education, and to have a working experience with him. In some cases, fishermen know no other life, have no other skills, subsidize their fishing with another job or another fishery, or are unwilling to relocate to places with more economic opportunity because they have extended family and community and low cost housing where they live.”

Pinkerton and Edwards conclude;

“Increasingly, those who have advocated ITQs as economically efficient are making broader claims about the general health of the industry and broader public benefits. So in the question of “efficient for whom?”, the answer is assumed to be “efficient not just for holders of ITQs but also for all actors in the fishery and the owners of the resource, the Canadian public”. This discussion has shown that this assumption, as well other assumptions under- pinning the indiscriminate promotion of ITQs, do not apply in the British Columbia halibut fishery.”...

“The quota leasing market in the BC halibut fishery is limiting efficiency, stifling innovation, and causing financial hardship. It is clear that a well functioning ITQ fishery requires greater forethought, oversight, and regulation in the design and implementation of transferability rules.”

Reference: Pinkerton E, Edwards DN. The elephant in the room: The hidden costs of leasing individual transferable fishing. Marine Policy 33 (2009) 707-713.

4. Could you describe the advantages that community entities could provide in addressing the issues of leasing, debt, new entrants, taxes, and other issues?

Fisheries are an important economic development asset that provides the broadest set of benefits when access is tied to the traditional pattern of fishing communities on our coasts. A catch share program needs the flexibility to meet the multiple goals it has defined either explicitly or implicitly such as bycatch avoidance, rebuilding of stocks, community stability, and economic “effectiveness” (not necessarily always efficiency) via different incentives. In changing resource, policy, and business environments, stability and flexibility can foster innovation and adaptation in new markets, fishery methods, and adaptive organizations such as Community Fisheries Associations.

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If, under the community provisions of the MSA, community entities are set up such as Fishing Communities (yet needing definition by Councils) or Regional Fishery Associations as non-profit 501c3 tax exempt organizations under the IRS code, then these organizations can provide economic incentives to address leasing, debt, taxes and other issues.

Using the example of the pending Pacific trawl individual quota program, a fisherman receives an allotment of quota. Let’s say he wishes to retire and sell his quota (not leasing it.) His cost basis for receiving the quota is zero and so he will have to pay **capital gains taxes**. Selling his quota at a discount to a non-profit community entity creates a multi-year capital gains tax abatement strategy. The discount is a charitable donation, an “investment” in that fisherman’s own community that has supported him during his fishing career.

To continue this same example, now a new generation fisherman wishes to get into the business, and he has just enough capital to buy the active vessel from the retiring fisherman, but he cannot afford a loan to buy quota shares which are required to go fishing. Now he can **lease** that quota from the Community Entity at **rates well below sub-market** (assuming the Community Entity has no debt – which it might...) 8-12% rates which help pay the low overhead for the Community Entity.

The issue of whether the Community Entity has any **debt** is germane to the initial allocation issue. Again, in the case of the Pacific trawl individual quota program, there is a 10% set aside known as the Adaptive Management Program, the specific use or allocation of which is yet undefined by the Pacific Council. This 10% might be allocated to processors in fact as one of the options. But, it could be (should be) allocated to community entities thus combining the program ideas for Adaptive Management and Community Fishing Associations that the Pacific Council is considering in trailing actions after it submits this new catch share program as an amendment to its groundfish management plan.

One potential use of the 10% Adaptive Management allocation could be to reduce capital requirements for in-season needs to cover overages incurred by vessels (disaster tows). The Groundfish Management Team report on this matter indicates that this allocation should be “**used for reasons beyond generating profit, for a broad sector benefit.**” For example, the Adaptive Management 10% could also be used to buffer the “margin” needed to address Over Fished Species (OFS) allocations. Allocating this 10% set-aside to Community Fishing Associations for these purposes could also reduce in-season **transaction costs** by making it easier for vessels to find and lease the needed marginal Quota Share to address these bycatch or overage issues.

Community Entities as described in the MSA are conceived of exactly to provide “broad sector benefits” as described by Pacific Council process.

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5. In the Magnuson-Stevens Fishery Conservation and Management Act, the language of part of the Limited Access Privileges Program section describes Regional Fishery Associations. Can you explain the term Community Fishing Associations and describe how either of those entities can function to help communities?

As described in the previous question the MSA contains two specific community provisions in relation to catch share (limited access privileges) programs; Fishing Communities and Regional Fishery Associations. One can be allocated catch share quota – Fishing Communities, and one cannot – Regional Fishery Associations.

In the case of the pending Pacific trawl individual quota program, the Pacific Fishery Management Council began to explore using the concept of the Regional Fishery Associations (RFA) in March of 2009, well into to the design process of the program. The Council decided to name them Community Fishing Associations (CFA), which we interpret as the same as the RFA structures defined in the Magnuson-Stevens Fishery Conservation and Management Act.

In any case, RFA or CFA entities can function as community entities (trusts) as described in the previous question. The overall functions of a CFA/RFA are to provide fishing communities a way to hold quota share assets within catch share programs, either through purchase or donation thus providing tax advantages. Having a CFA entity in a community also can provide incentives to keep fishermen, landings, and infrastructure in place, and therefore tax revenues, and economic multipliers from other businesses.

CFAs will require community boards to run them, and this will enhance the transparency of the quota process, leasing, market prices of quota sales and other functions. Markets work best when there are multiple sources of information about prices and community entities can be a source.

To reiterate the functions and benefits of CFA/RFA structures, I quote from my prior written testimony; -

- Having an allotment of quota that is permanently anchored in communities can help community and geographic stability.
- Trusts with no debt can lease for 8-12% overhead rates.
- New entrants to the fishery have an incentive to stay and fish in that community if they can get a start with low rate leases of quota.
- New entrants can then bootstrap themselves into gradual individual ownership of quota as they earn greater revenues with less overall debt.
- Trusts can offer capital gains tax solutions to retiring fishermen, thus investing additional amounts of quota into the community.
- Community or Regional Fishery Associations as written in the Magnuson Act can function as Trusts.

In addition, Regional and Community Fishing Associations can contribute to environmental, economic, and community needs, including:

- **Protecting smaller ports and smaller-scale fishermen.** Community Trusts can help protect smaller ports and smaller-scale fishermen by initiating strategies to (a) anchor

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fishing quota in the community; (b) facilitate intergenerational transfer of fishery access; (c) incentivize and leverage affordable catch share financing; (d) help fishermen diversify their fishing ‘portfolios’; and (e) deliver health care to fishermen and their families. In turn, these activities will support the maintenance of fisheries related infrastructure in communities and attract new entrants to the fishing community.

- **Participating in the development and design of effective fisheries management.** Trusts can provide a key role in emerging catch share systems (e.g. program design, planning, permit auctions, finance, marketing) by bringing fishermen’s voices to FMC meetings or by retaining specialized expertise. In addition, they can participate in bycatch reduction initiatives such as gear modification, mapping bycatch hotspots, improved fishing practices, etc.
- **Creating fishery conservation networks.** Community Trusts can serve as vehicles for information sharing, contribute to scientific research, reduce carbon footprints, and mentor young fishermen.
- **Building and participating in new emerging markets for sustainable community-based seafood products.** In recent years, increases in aquaculture production and seafood imports have had a profound effect on the domestic ocean fishing industry. While aquaculture and foreign seafood may have a competitive advantage in price, US fishermen still have several advantages over producers of these product types. First, many domestic wild fisheries have the advantage of being closer to markets and therefore a shorter supply chain to the consumer. At the same time, the demand for both fresh and locally caught seafood is growing rapidly. A CFA could capitalize on these advantages by (a) supporting development of regional brand; (b) initiating marketing to reach key consumers and providing increased coordination for existing marketing efforts; and (c) promoting awareness among consumers about local and seasonal seafood options.

6. There are two community entity structures in Alaska, the Community Quota Entities and the Community Development Corporations. Could you explain their functions and similarities or differences?

Let us look at the Community Development Quota corporations in Alaska – successful due to allocation vs. Community Quota Entities – which have to purchase on open market, and therefore not competitive nor successful.

Two experiences in Alaska with Community Fisheries Trust-like entities are instructive for developing a Community Entity framework: Community Quota Entities (CQEs) and Community Development Corporations (CDQ).

CDQs were established 15 years ago by an act of Congress and were allocated 10% of overall quota in many species. Today they are vibrant multi-million dollar revenue community based economic development engines.

Community Quota Entities (CQEs) were formed 10 years into the Alaska IFQ program by the North Pacific Fishery Management Council and were not allocated any Quota Shares and must

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buy them on the open market. They do this with great difficulty, given the price for quota and the capital barriers to entering into the market.

Both CDQs and CQEs are examples of Community Entities. The management processes of both organizations create a sense of cohesion and cooperation at the scale of communities. Both forms have evolved considerable managerial skill and capacity. In terms of viability, however, one system is healthy, one is not.

The major lesson here is that it is beneficial to establish community entity organizations immediately when starting any catch share program.

7. If access to the federal fisheries finance program were expanded, would that help the situation in communities?

Representatives for the Community Quota Entity Program in Alaska and the North Pacific Fisheries Trust have had discussions with the headquarters (Silver Spring/NOAA) and regional offices of the federal fisheries finance program. The headquarters office was not aware of the CQE program.

The current federal program which finances the purchase of quota shares is only accessible by individuals. This is a very successful program in financial terms and has the enviable record of no defaults on loans the program has made for quota purchases.

It would be of great benefit to communities if the access to this federal finance program was provided for community entities, such as the Community Quota Entity Program in Alaska, as well as Community Fishing Associations and Regional Fishery Associations.

Our understanding is that this would require legislative action by the Congress, and we endorse such a potential action.

Questions from Republican Members

1. Are you familiar with the North Pacific halibut plan? How would that fishery have changed if your idea of requiring up to 25 percent of the fishery be giving to communities?

I am familiar with the halibut quota program as implemented by the North Pacific Fishery Management Council. The North Pacific Fisheries Trust is active in many Alaska communities that fish halibut, own quota, or seek to acquire quota.

The halibut fishery experienced a 25% consolidation in the early years (1-4) of the program. Based on studies by Alaska-based university social scientists and economists and NOAA program administrators, one would project that community allocations would have dampened the

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negative effects of the program (see references at end of section). In fact the subsequent allocations to the Community Development Quota Corporations managed to allow many communities to recover from those effects.

In general with community allocations, one would expect to see far less quota migrate away from communities, more stable communities from a social and economic structural perspective, far more viable small fishing communities, less human migration away from communities, a greater sense of hope in communities which became marginalized through the process, more time for people to understand the creation of a new “asset” – quota shares and how the value of that asset would change over time and more incentives for fishing businesses to stay in particular communities in order to access the community-based quota.

Fishing businesses are not independent in their relationship to communities, although many of them migrate around with the seasonal fisheries, even as they may be based in another state or larger community somewhere else in the same state. Crews, gear shops, fuel docks, processors, secondary businesses in supplies and other services must be part of the equation when considering the design of catch share programs with public trust fisheries. Owners should not be the sole beneficiaries of the “conversion” catch shares. One way to recognize the role and relationship of communities in this process is to allocate a modest amount (10%) to community entities (either Fishing Communities or Regional Fishery Associations) as provided for in the Magnuson Stevens Fishery Conservation and Management Act (as revised 2006).

References:

Enclosing the Fisheries: people, places, and power. Marie E. Lowe and Courtney Carothers, editors. 223 pages. Published by the American Fisheries Society, December 2008. Bethesda, MD. ISBN: 978-1-934874-05-9

Report on Holdings of Individual Fishing Quota (IFQ) by Residents of Selected Gulf of Alaska Fishing Communities 1995 – 2004, March 2005. Alaska Region, NOAA Fisheries Service (NMFS) Restricted Access Management Program , Juneau, AK 99802 www.fakr.noaa.gov

2. Do you think that taking a percentage of the quota off the top for communities would work in New England fisheries?

Yes I do. But in fact the sector allocations could effectively generate the same result. However they are not designed consistently for geographic coherence. In other words some sectors have boats from Maine and Martha’s Vineyard in the same sector, boats that do not share/fish the same waters and stocks, or use/participate in the same ports. This is not an approach that supports the connections between “people and place” – the natural affinities and knowledge that fishermen have for fisheries resources – the patterns of seasons, stocks, and their inherent variability.

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If sectors, which are effectively co-operatives, were delimited geographically, such as the Cape Cod hook sector, then you would have a set of community supporting structures, assuming you require all fishery participants in that cluster of related communities to participate in the sector in order to fish. That way all of the issues subordinate to the initial allocation of potential harvests to that sector can be managed by the co-op approach to the sector; when and where to fish, catch and bycatch sub-allocations, intra-sector in-season exchange of sub-allocations to allow fishing to continue as long as possible etc.

The goal of community allocations, either via community entities, or community-based sectors is to provide an “anchor” for the quota or allocations in communities to dampen the potential effects of quota markets, escalating prices, quota and human migration, barriers to new entrants, and so on. Some observers suggest that bycatch species or stocks still under rebuilding plans overly limit the sector approach and thus it will not work. Within an ecosystem-based approach to a multispecies fishery (such as New England groundfish) I do not see any other approach which could provide more flexibility in dealing with a broad spectrum of issues while operating within the biological limits of the marine ecosystem.

3. How would a community set-aside work in an area where there are many small communities? Would there be enough quota in any one community to support a fleet? If not, how would a community set-aside work?

In general, any community set-aside will not be enough to support an entire fleet regardless of how many or few communities are involved. However, the central concept is that a community allocation creates an incentive for individual fishermen to stay fishing in that community as there is an “anchor” of quota that will never leave that community. The assumption is made in the community set-aside process that individuals will have quota holdings that can be matched up with community holdings to create larger pools in income. Thus there is an incentive to stay and fish in that community.

In addition, the potential uses of that quota (based on experiences in Alaska) could be to promote new entrants into a fishery – such as the skiff class in the halibut fishery. The overall goal being to create interactions between individual and community incentives, specifically by helping new fishermen have access to low cost leases for quota, then earning enough income to be able to save for their own quota purchases in the same vessel class (again using the Alaska halibut example). Thus you are using the community process to “bootstrap” individual ownership of catch share quota, building community stability in the process.

In Alaska, the Community Quota Entity program allows for multiple communities to operate under one single Entity (organization) thus pooling quota and representing a greater synergy of interests. This option has yet to be used.

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4. Most people believe that Councils should have flexibility in developing fishery management plans. Why do you believe it is okay to mandate community set-asides?

Flexibility has its place, but we need some boundaries on flexibility. We need some mandates and as well limits on those mandates, balance in other words. Sideboards or basic requirements are needed, based on the lessons one can learn from the experience to date from around the world with catch shares in fisheries. 10% set asides have been established in Alaska in many quota fisheries, 10% has been allocated – though not defined in its ultimate purpose – for adaptive management in the Pacific trawl individual quota program being proposed. We have enough experience with the negative effects of catch share programs, and enough experience with community set-asides to show that, done correctly, their economic and social effects are positive. 10% hardly impacts any flexibility the Councils have in designing catch share programs.

5. You have harsh things to say about the fishery management councils. Do you think we would have better fishery management plans if NOAA wrote them? If you are concerned about NOAA’s push toward catch shares and you are concerned with the council, who do you think should develop fishery management plans?

This question tries to frame the issue as “one or the other” e.g. the Councils vs. NOAA as the decision maker or arbiter in fisheries management. This is a false dichotomy. My point is that within the democratic process of the fishery management councils, we commonly observe that economic politics tends to highly influence the outcomes of the voting process in the creation or amendment of fishery management plans. If I appear critical of that process, I am only making a realistic statement that describes the process.

The reason we have national standards (which do not carry the force of law as does the rest of the Magnuson Stevens Act) is to try and provide some consistency in the outcomes of fishery management plans in the U.S. But since these standards are open to wide interpretation by Councils depending on the political pressures they are subject to, the outcomes are inconsistent - for example National Standard 8 (the social and economic effects on communities) requiring only the consideration of these effects.

The Council process is a genuinely democratic process but it needs to some minimum requirements. NOAA is pushing catch shares as a policy but it cannot implement that policy except through the Councils (aside from technical or financial assistance NOAA may provide). Catch shares are complex market instruments. Few if any Council members, staffs or committee members have expertise in market design.

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Therefore, based on what is widely known on the social and economic effects of catch shares on communities, in the process of creating catch share programs it is time we established some mandates for minimum requirements for Councils to implement the community provisions that are already written in the Magnuson Stevens Fishery Conservation and Management Act (as revised 2006).