Golden king crab arbitration workgroup meeting
PSPA Conference Room, Fishermen's Terminal, Seattle, Washington
North Pacific Fishery Management Council
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Participants – Duncan Fields, Joe Sullivan, Dick Tremaine, David Capri, Mark Fina, Greg White, Linda Kozak, Dick Powell, Jill Capri, Brett Reasor, Mark JoHahnson, Larry Cotter, Steve Minor, Jake Jacobsen, Ted Painter, John Iani

Discussion
The meeting began with a review of the process being followed by the committee and the possible uses of its work product. To date, the group has spent a large share of its time discussing the development of a variable percentage formula, which might fairly represent an application of the arbitration standard. The group discussed the potential of this work to inform both the Council and the formula arbitrator. The group agreed that any consensus on a possible formula could be forwarded to the Council for its consideration. If the Council believes that the formula reflects an appropriate application of the arbitration standard, it could recommend that the formula arbitrator consider the group's work product when developing a formula for the fishery. Participants in the fishery are free to express their opinions concerning the formula to the arbitrator, which might include lending their support to adoption of the consensus formula. Sector representatives suggested that this arrangement is unlikely to pose any antitrust risk, as recommendations would be provided to the Council and the Council would have the discretion of whether to make recommendations to the formula arbitrator. Representatives agreed to further review the group's work to confirm their opinions of antitrust issues prior to the next meeting.

Overall agreement
The group discussed elements that should be included in a consensus recommendation. This section of the minutes only defines the various elements without specifying the different positions of the participants. The positions of the parties are outlined in sections that follow. Necessary elements would include:

1) A base formula that establishes an acceptable ex vessel price as a percentage of first wholesale revenues for every first wholesale price. This percentage would likely be variable, changing with the first wholesale price.
    a. An Eastern Aleutians Golden/Western Aleutians Golden (EAG/WAG) differential – this could include a revenue adjustment based any difference in recovery rate and associated difference in processing cost
    b. West regional landing adjustment (for West region IFQ from the WAG fishery) – this adjustment would be made to address costs differences in between the East region and West region
2) Provision for the issuance of B shares in the event that no processor applies for their IPQ – in the absence of such a provision, all Class A IFQ would be undeliverable. This element would be needed, particularly if a formula is adopted that increases the percentage of first wholesale price that is paid to the harvester at low first wholesale prices. In these circumstances, harvesters believe the provision could be applied, if a PQS holder elected not to apply for IPQ to avoid a loss. The group reached a consensus supporting a regulatory change adopting this provision.
3) Provision for the publication of arbitration results. The group reached a consensus supporting this revision to the regulations. Both sides agreed to work together to address legal/antitrust issues that might arise from the release of decisions. A delay in the release of the decisions is believed to be useful for addressing some concerns.
4) Agreement on the terms of lengthy season agreements as proposed by the processors. Under that proposal length season agreements would consist of the following: once an IPQ holder (a)

receives 50% of the matched IFQ and sells 50% of that product (25% of the total match), the IPQ holder shall notify the IFQ holder (and make a price proposal); the IFQ holder then has 30 days to initiate arbitration. Both sectors agreed to support a regulatory change that includes this requirement for lengthy season agreements.

Participants agreed that any resolution of issues should include all of these elements. In addition, the group agreed that any proposals in this process should not affect or influence the outcome of the formula arbitration process, unless a consensus is reach on all elements that is forwarded through the Council. The group also acknowledged that items 2) through 4) might require Council action to revise regulations; however, item 1) could be implemented as the outcome of application of the existing arbitration standard (without regulatory action). In addition, all participants agreed that any consensus for a pricing formula through this process should not be construed as supporting the application of the pricing formula or its structure to any other fisheries.

<u>The base formula – the sliding or variable percentage formula</u>
Much of the meeting was spent discussing a possible formula that would define ex vessel prices in the fishery as a percentage of the first wholesale price. It was suggested that a formula that on average pays approximately 47.5 percent of first wholesale revenues to the harvesters might be acceptable.

Harvesters initially proposed a formula intended to preserve estimated processor profits, which was derived from negotiations with Westward in 2007. The proposal included an adjustment based on the location of processing (Dutch Harbor/Adak/Atka). The calculation results in the percentage of first wholesale revenues paid to harvesters increasing with first wholesale price (see attachment 1 – Westward 2007 proposal). By paying a lower share of first wholesale revenues to the harvester at lower prices, the processors margins are protected. Harvesters would recoup any losses from this protection in high price years.

Processors suggested that this year's draft formula from the formula arbitrator would be acceptable (see attachment 2, pp. 17-20). That formula provides for an increasing percentage of first wholesale revenues to be paid to harvesters as first wholesale prices increase. This formula has the opposite effect of the harvester proposal, with processors protecting harvest revenues at low first wholesale prices. Processors would recoup any losses at higher first wholesale prices.

Harvesters responded to the processor proposal that effectively combined the two previous proposals. The proposal averaged the two preceding proposals, resulting in a formula with the percentage of first wholesale revenues paid to harvesters decreasing with the first wholesale price. The formula limited the range of percentages, establishing a maximum percentage of 48.8 percent at a first wholesale price of \$5.00 and a minimum percentage of 47.4 percent at a first wholesale price of \$11.00. (A copy of the proposal is attachment 3.)

Processors responded that this proposal deviated too much from the suggested 47.5 percent suggested average division. The harvesters responded with a proposal that provided for an ex vessel price of 48.8 percent of the first wholesale price at a first wholesale price of \$5.20 and 47.4 percent of the first wholesale price at a first wholesale price of \$7.20. This last proposal was presented late in the meeting, leaving little time to evaluate it.

Although processors did not favor the proposal, they agreed to spend additional time reviewing the proposal to ensure that they understand it fully. Processors also agreed to develop a proposed formula for the next meeting.

The parties agreed that these discussions (and the various proposals) should not be considered by the formula arbitrator in developing the formula in the fishery, unless agreed to by all parties.

<u>Western fishery and Western region price adjustments</u>
Processors have expressed concern that prices in the Western fishery should be adjusted downward in recognition of the lower recovery rate from crab caught in that fishery (which, in turn, increases the cost of processing and decreases the revenues per pound of product). Processors have suggested that this adjustment should be based on approximately 1-2 percent difference in recovery rates across the two fisheries (resulting in a reduction in ex vessel price of approximately $0.05 per round pound). Harvesters suggested that no evidence of a recovery rate differential has been presented in the workgroup and that, therefor, no adjustment should be made. Processors agreed to bring evidence of the difference in recovery rates to the next meeting. Both sides agreed that any price adjustment should be generally applied (rather than applied to specific deliveries) to avoid the creation of incentives for high grading.

Processors have also suggested that West region processing costs are substantially higher. To date, the difference is suggested to be approximately $0.20 of additional cost per round pound. Harvesters have suggested that these costs be shared with the processors. Harvesters also assert that their costs operating in the West fishery and making deliveries to the West region are greater (as a result of both operating costs and additional taxes on landings in the West region). Processors have suggested that these costs should be addressed by reducing the price of West region deliveries by $0.125 per pound).

Harvesters have developed a competing proposal that acknowledges a difference in prices in the Eastern and Western fisheries, with the adjustment determined by the location of delivery. Under the proposal, deliveries of Western fishery catch:

a) to an East region plant would be subject to a $0.075 premium,
b) to a West region plant would be subject to a $0.075 discount.

These adjustments would be intended to address the different costs of processing in the different regions.

<u>Shared margin arrangements</u>
Both sectors expressed an interest in further developing shared margin arrangements. The group agreed to review the shared margin proposal (attachment 4) for discussion at the next meeting.

<u>Fixed price proposal</u>
Both sides support the development of fixed price arrangements, under which a final price would be established based on application of a formula to a price index. Harvesters prepared two spreadsheets concerning the application of indices (attachment 5 and 5A) for discussion, but no time was available for review of those materials.

Processors suggested that a fixed price arrangement could be applied by one side (e.g., harvesters) identifying an index and formula, which the processor could then choose to accept on a delivery by delivery basis. Effectively, the harvesters would make a standing offer that could be accepted (or rejected) by the processor at the time of each delivery. If the offer is not accepted, the delivery price would be subject to negotiation. Processors agreed to write up their suggestion for the review by the harvesters prior to the next meeting.

<u>Next meeting</u>
August 7th and 8th from 9:30 am to 5 pm at PSPA office at Fishermen’s Terminal in Seattle, WA.

In preparation for the next meeting:

- Processor representatives agreed to provide additional information concerning recovery rate differentials across the fisheries.
- Processors agreed to work through the most recent harvester proposal (including an exchange of emails with harvester representatives to ensure that both sides have the same understanding of the proposal)
- Processors agreed to prepare a counter-proposal revising the harvesters proposal to extend range of sliding scale to higher prices. The proposal should include any suggested price adjustments for Western fishery harvests and West region landings.
- Processors agreed to write up their idea for the fixed price arrangement for review by harvesters prior to the next meeting
- Both sectors agreed to further review of the shared margin proposal
- Both sectors agreed to review the proposals to date to identify any antitrust concerns.

Attachments available upon request from the Council office.