

DRAFT

Right of first refusal modifications North Pacific Fishery Management Council June 2009

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 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.

In response to concerns of participants, the Council tasked its crab advisory committee review the right of first refusal provisions to assess potential issues that limit the effectiveness of the right. The committee discussed the following four possible issues:

- 1) the lapse of the right after three consecutive years of use of the individual processing quota (IPQ) outside the community;
- 2) the requirement that the right apply to all assets involved in a transaction, which could include assets outside the community;
- 3) the short period of time allowed for exercising and performing under the right; and
- 4) the potential for communities to have inadequate funding exercising the right.

In response to the Council’s request, the committee reached a consensus in support of two amendments to the rights of first refusal. Under the first amendment, the time that a community has to exercise the right would be extended from 60 days to 90 days and the time that a community has to perform under the contract would be extended from 120 days to 150 days. These extended periods are intended to provide communities with additional time to assess whether to exercise its right and arrange financing for the transaction. The second suggested amendment would extend the right indefinitely, without lapse. This modification is intended to ensure that historical community interests in the fisheries are maintained in perpetuity.

The committee also discussed potential ways to address the other two issues directed to it by the Council. Specifically, the committee discussed potential methods of applying the right to only community-based assets (as opposed to all assets in a transaction). The committee was unable to reach a consensus on this issue. The committee also discussed potential measures to improve a community’s ability to use the right of first refusal. The committee supported the development of a loan program that could support acquisition of shares under the right by communities. At its February 2009 meeting, in light of the committee’s report, the Council directed staff to prepare a discussion paper examining these four issues. This paper is staff’s response to that request.

Background

Under the rationalization program, the Council adopted a provision for community rights of first refusal on PQS. The representative entity of any community that supported in excess of 3 percent of the qualified processing in any fishery received the right on the PQS arising from processing in that community.¹ In

¹ The community of Adak was excluded from the rights of first refusal, as that community received a direct allocation of 10 percent of the Western Aleutian Islands golden king crab fishery.

DRAFT

addition, entities representing qualified communities in Gulf of Alaska north of 56°20' N latitude received a right of first refusal on any PQS issued based on processing in a community not qualifying for a right of first refusal in that same area of the Gulf.

In the case of CDQ communities, the representative entity holding the right is the local CDQ group. In all other communities, the right is held by an entity designated by the community. The right is established by a contract that between the community entity and the PQS holder. Under the contract, the right applies to any sale of PQS and sales of IPQ, if more than 20 percent of the PQS holder's community-based IPQ in the fishery were processed outside the community by another company in 3 of the preceding 5 years.² To exercise the right, the community entity must accept all terms and conditions of the underlying agreement.

Any intra-company transfers are exempt from the right of first refusal. To qualify for this exemption, the IPQ must be used by the same company.³ In addition, transfers of PQS for use in a community are exempt from the right. To meet this exemption requirement, the purchaser must agree to use at least 80 percent of the annual IPQ in the community in 2 of the following 5 years and grant a right of first refusal on the received PQS. Under two circumstances, the right will lapse. First, if a company uses its IPQ outside of a community for three consecutive years, the right on the underlying PQS lapses. Second, if a community entity chooses not to exercise the right on the transfer of PQS, the right also lapses.

To exercise the right, a community entity must provide the seller of PQS with notice of its intent to exercise the right and earnest money in the amount of 10 percent of the contract amount or \$500,000, whichever is less, within 60 days of notice of a sale. In addition, the entity must perform under the terms of the agreement within the longer of 120 days or the time specified by the contract.

Based on the qualifying criteria, 7 community entities received rights of first refusal in the different fisheries governed by the program (see Table 1). The distribution of rights differs across fisheries, with Akutan, Unalaska, King Cove, St. Paul, and St. George all starting the program with rights on approximately 10 percent or more of the PQS in at least one fishery.

The limitations of the 'cooling off' provision prevented much of the IPQ subject to the right of first refusal from being used outside the community of origin in the first two years of the program. Only in the third year of the program (once the cooling off limitation lapsed) was any sizeable portion of the IPQ permitted to be moved. As a result, rights of first refusal on PQS are believed to have lapsed (as a result of use outside the community) in only a few instances. Most notably, the right is believed to have lapsed with respect to PQS 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, the right of first refusal lapsed on shares for which the Aleutian Pribilof Island Community Development Association (APICDA) holds rights of first refusal on behalf of St. George under the terms required by regulation. Despite these provisions, APICDA is reported to have reached agreements with both PQS holders. Under the agreement with one of the PQS holders, APICDA received the PQS formerly subject to the right. The terms of the other agreement are not known.

² Although custom processing of IPQ outside of the community could be argued to trigger this right on a subsequent transfer, a PQS holder could engage in custom processing for an indefinite period without triggering the right, if no transfer of IPQ is made.

³ It is believed that this provision does not apply to custom processing arrangements, as no share transfer occurs under those arrangements.

Table 1 Distribution of rights of first refusal by community on implementation.

Fishery	Region	Right of first refusal boundary	Number of PQS holders	Percentage of PQS pool
Bristol Bay red king crab	North	None	1	0.0
		St. Paul	2	2.7
	South	Akutan	1	20.8
		False Pass	1	3.9
		King Cove	1	9.8
		Kodiak	3	4.0
		None	4	3.6
		Port Moller	3	3.7
Unalaska	11	51.5		
Bering Sea <i>C. opilio</i>	North	None	3	1.0
		St. George	2	9.7
		St. Paul	6	36.3
	South	Akutan	1	9.7
		King Cove	1	6.3
		Kodiak	4	0.1
		None	4	1.8
		Unalaska	13	35.0
Eastern Aleutian Islands golden king crab	South	None	1	1.7
		Unalaska	7	98.3
Pribilof red and blue king crab	North	None	1	0.3
		St. Paul	5	67.3
	South	Akutan	1	1.2
		King Cove	1	3.8
		Kodiak	4	2.9
		Unalaska	5	24.6
St Matthew Island blue king crab	North	None	5	64.6
		St. Paul	4	13.8
	South	Akutan	1	2.7
		King Cove	1	1.3
		Kodiak	1	0.0
		Unalaska	6	17.6

Source: RAM PQS data 2007-2008.

In addition, PQS allocated based on processing in the Aleutians East Borough communities (i.e., Akutan, False Pass, King Cove, and Port Moller) was permitted to be moved within the borough during the cooling off period. As a consequence, rights of first refusal for the benefit of those communities may also have lapsed from movement of processing.

Also, certain IPQ have had the right removed as a consequence of other transfers that have occurred in the first few years of the program. In some cases, the PQS has been transferred to the right holder (see Table 2), while in others the right has lapsed because the right holder chose not to exercise the right at the time of a transfer (see Table 3). In one instance, a PQS holder elected to divest of a portion of its PQS holdings to remain within permitted share use caps.

In five cases, community entities holding the right have acquired PQS subject to the right. In one fishery, a portion of the PQS subject to the right was transferred to the community entity holding the right, while the right with respect to another portion of the PQS was allowed to lapse. In another fishery the PQS represented a relatively small portion of the total PQS on which the entity held rights of first refusal and

DRAFT

the PQS buyer was a different community entity. Rather than intervene in the transfer, the right holder elected to allow the transaction to proceed, lapsing the right of first refusal. In another instance, a PQS holder transferred its PQS to the right holding community entity to avoid a potential affiliation that would have prevented participation in the arbitration program. In most cases, right holding community entities have been actively involved in PQS transactions involving shares subject to their rights. In some cases, those entities have acquired shares; in others, they have allowed transactions to proceed. This community involvement in transactions suggests that the right has affected community interests.

Assessing the extent to which rights have lapsed, beyond those voluntarily reported to NOAA Fisheries, is difficult because of the nature of available landings data. While some PQS holders have reported lapsing of rights voluntarily, regulations do not require PQS holders to report lapsing of a right. Although geographic landing requirements are applied in the program, records concerning location of landings are limited by record keeping protocols. Currently, most deliveries to floating processors are recorded as 'at sea,' without designation of a port. These 'at sea' deliveries may take place within community boundaries, and therefore may not be considered as being outside of the community that benefits from the right of first refusal. On the other hand, landing records will not fully reflect the geographic distribution of landings, which may result in several rights lapsing (because of use of IPQ outside of the community for three consecutive years). In addition, no system is in place for reporting and documenting the lapse of rights of first refusal. Given this shortcoming, it is possible that other rights of first refusal may have lapsed.

Table 2. Percentage of PQS transferred to right of first refusal holder by fishery (as of 2009).

Fishery	Percent of PQS
	pool
Bristol Bay red king crab	8.8
Bering Sea <i>C. opilio</i>	6.1
St. Matthew Island blue king crab	0.1

Source: NMFS RAM Division database.

Table 3. Percentage of PQS on which right of first refusal lapse has been reported to NMFS by fishery (as of 2009).

Fishery	Percent of PQS
	pool
Bristol Bay red king crab	4.0
Eastern Aleutian Island golden king crab	6.9

Source: NMFS RAM Division database.

In developing an amendment package to address issues that have arisen with the rights of first refusal, the Council should consider its purposes for taking these actions and whether those purposes will be achieved, when considering whether to advance this action. To date, the rights have provided community entities with some degree of leverage with PQS holders that are attempting to move processing from a community. To date, this leverage has been largely asserted indirectly, as community entities have negotiated the purchase of PQS, in circumstances when the holder has had an interest in divesting of those shares or when the movement of processing has attracted political attention. Maintained in its current form (even with the suggested amendments), the right is likely to continue to have its greatest effect through these indirect means. PQS holders desiring to move processing from a community may avoid triggering the right in many instances, as the right is only triggered by a transfer. A PQS holder may use

DRAFT

the yielded IPQ at another of its plants or may have the IPQ custom processed at another company's plant without triggering the right. If the buyer of the PQS is willing to use a portion of the yielded IPQ in the community in 2 of the first 5 years after the transfer, the right is not triggered. After that period, the IPQ may be moved, provided not transfer is made. This limited applicability of the right may prevent modifications from fully achieving the Council's objectives. Yet, solving these shortcomings (or developing alternative community protections) could require large scale changes to the rights, which would not be simple to devise and could be disruptive to the current distribution of interests.

Extension of the periods to exercise and perform under the right of first refusal

Under the current right of first refusal contract requirements, a community entity has 60 days from receipt of a contract defining a transfer from a PQS holder to exercise the right of first refusal. Within that time period, the community entity must inform the PQS holder that it is exercising its right and provide earnest money of 10 percent of the transaction amount or \$500,000, whichever is less. The 60 day period in which to exercise the right is intended to provide community entities with the opportunity to assess the merits of intervening in the transaction. For some entities, such as CDQ groups, decisions of whether to enter simple, low value, transactions may be made expeditiously; however, larger more complex transactions, could involve a more extended decision making process for a community entity.

In considering whether to exercise a right of first refusal, a community must examine the merits of the transaction. Under the current rules, the entity must assess the value of the various items included in the transaction, which may include items other than PQS and could include items that are not present in the community and items that cannot be relocated to the community. Each item in the transaction must be assessed along with its value as part of the transaction, as a whole. In some cases, the entity may need to assess the values of different groups of assets in the transaction. For example, an entity may wish to retain only those assets based in or movable to the community.⁴ To make these determinations, an entity may need to consult experts or conduct its own appraisals. In addition to the other steps involved in the decision making process, the entity may need to arrange financing. Depending on the purchase, financing arrangements may require substantial due diligence on the part of any financing party. Independent assessments of the transaction, including valuations of possible collateral may be necessary. In some instances the entity may undertake a public meeting process or take formal board action to make a purchase. Notice requirements may be applied to any such meetings. Each of these various steps in the decision making process will require time.

Community entities may also need to undertake considerations beyond those confronted by entities acting as simple business entities. For example, an entity may only wish to exercise the right, if it is confident that the assets will bring some level of benefit to the community. Achieving these benefits may depend on relationships with other community-based operations and commitments of residents. These relationships and arrangements may be complex and commitments may take time to attain. Each of these factors suggests that an extended period for making a decision of whether to exercise a right could be beneficial to entities confronted by that decision. In some circumstances, a 30 day extension to a 90-day period, as suggested by the crab advisory committee, could be adequate for an entity to better evaluate a transaction, access earnest money, make preliminary financing arrangements, and make an appropriate decision concerning the exercise of its right.

In addition to having a limited period of time to exercise a right, community entities also have a limited period of time in which to perform under the right of first refusal. Under the current rule, an entity has

⁴ The willingness of an entity to retain items will likely vary across entities. CDQ groups with substantial fishing interests in many locations may be more interested in retaining items outside the community for use as a part of their fishery ventures.

DRAFT

exercised its right has 120 days from receipt of the contract to fully perform under the contract. This added time for performance is intended to provide the entity with adequate time to finalize financing arrangements. This extended period could also allow for the entity to make additional arrangements, such as partnerships or transactions for portions of the assets that it may not wish to maintain. The additional 90 days from the time from the exercise of the right is intended to ensure that the transaction may be finalized, with all necessary due diligence by lenders. If time to exercise is extended 30 days, concurrently extending the time to perform will maintain the existing 90 day window between the deadline for exercising the right and performing under the contract. This time was adopted to ensure that the community entity and any lenders would have adequate time to complete the transaction. Adding 30 days to the periods for exercising the right and performing under the applicable contract may make the right of first refusal more accessible to community entities wishing to enter a contract to protect a community's interests.

The current rule, which allows a community entity 60 days to determine whether to exercise a right, may challenge some community entities (particularly entities that use a more structured decision making process, face a more complex transaction, or have less experience in the industry); however, lengthening the time for decision making could complicate transactions for parties affected by the right. PQS holders and those wishing to acquire PQS may invest substantial efforts arranging transactions. Time may be of the essence in these transactions because of the seasonality of fisheries. Allowing an extended period for a community entity to exercise a right of first refusal may impinge on operations, if the time period extends into the fishing season. The extent of this disruption will depend on the transaction and its timing. If the transaction includes assets other than PQS (such as processing equipment or groundfish fishery assets) the disruption could be of even greater significance. These factors all suggest that an extended time period for the decision of whether to exercise a right could be problematic for the parties to the transaction.

In considering whether to extend the time periods for exercising the right and performing under the contract, the Council should also consider that the PQS holder and the buyer can prevent a community entity from intervening in the transaction, if the buyer agrees to grant a right of first refusal to the entity and to use the IPQ yielded by the transferred PQS in the community in two of the following five years. Although these concessions may affect the value of the assets transferred (including the PQS), the parties to the transaction can effectively limit the ability of the community entity to disrupt the transaction by exercising the right. This ability may limit both the difficulty posed by the extensions and their effectiveness in protecting community interests.

Possible amendments:

- 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.

Extending the right permanently

Under the current contract requirement, the right of first refusal lapses, if the IPQ yielded by the PQS subject to the right is used outside of the community for three consecutive years.⁵ The rationale for this lapse is that the community's connection to the PQS may be diminished, if the yielded IPQ are used

⁵ The contract also provides the community entity with a right of first refusal on the IPQ, if more than 20 percent of IPQ from a holder's community-based PQS is processed outside of the community by another company in 3 of the preceding 5 years. Yet, the holder may avoid triggering the right, if the no transfer of IPQ is made. This may occur by simply having the crab custom processed without transfer.

DRAFT

outside of the community for an extended period. In addition, the right of first refusal lapses, if the right holder elects not to exercise the right on a transfer to which it applies.⁶ The rationale for rights lapsing after these transfers is that the community entity chose to allow the transfer to occur, despite the recipient's intention to use the IPQ outside the community. Some proponents of strengthening the right of first refusal (including a consensus of the crab advisory committee) have recommended removing the provisions under which the right of first refusal lapses, effectively making that right permanent.

Making the right permanent would establish a perpetual link between PQS and the community where processing occurred that led to the allocation of that PQS. This community/PQS association would be maintained regardless of whether the PQS holder used the yielded IPQ outside of the community for several years. In addition, once triggered by a transfer, the right would supersede the interests of other parties, including communities where the yielded IPQ have been processed in the intervening years.

Establishing a permanent right of first refusal could also remove the provision that allows the right to lapse, if a community entity elects not to exercise the right on a transfer of PQS with the intention of moving processing from the community. Under the current provision, if a community entity elects not to exercise its right when transfer is intended to move the PQS from the community the right lapses. Although the entity arguably demonstrates its intent to allow the shares to leave the community by not exercising its right, perpetuating the right could help overcome some other perceived shortcomings with rights of first refusal. If an entity chooses not to exercise its right because it cannot arrange financing or the transaction involves assets other than the PQS that the community has no interest in, extending the right would provide the entity with a possible future opportunity to reassert its interest in the PQS. Extending the right in this manner may aid entities (and communities) lacking the wherewithal to exercise a right of first refusal.

To the extent that the right is intended to protect community interests, the right may be lacking, in part, because of its lack of permanence. Yet, several other aspects of the right limit the effectiveness of the provision in protecting community interests. By its nature, the right only applies to transfers. Absent a transfer, shares may move freely among communities under other processing arrangements (including those internal to a company, as well as custom processing arrangements). This limitation on the right leaves a community entity unable to prevent the movement of processing from its community, as long as the PQS holder chooses not to transfer the shares. Yet, establishing a permanent right would prevent a PQS holder from moving shares outside of the community until the right lapses prior to putting the PQS on the market. Lapsing of the right in this manner could simplify any transaction to sell the PQS (and other assets) by removing the encumbrance of the right.

In considering whether to advance for analysis a provision extending rights indefinitely, the Council should consider the current structure and distribution of processing in the fishery, the possible redistribution of processing activity in the future, and community interests at stake. Over time, processing activity may be expected to be redistributed among communities. The redistribution will vary across fisheries depending on efficiencies and evolving circumstances. Under current rule, IPQ are free to be used in any location (within the designated region, if applicable). The only community-based limitation on processing shares arises when a transfer of those shares is made. As a result, it is possible that a community entity's right of first refusal could be triggered by a transfer several years after the PQS has effectively left the community.

⁶ It should be noted that the right applies, only if the recipient of the PQS acknowledges that the transfer is for use of the yielded IPQ outside of the community.

DRAFT

The indeterminate movement of IPQ use among communities could result in unintended (and, at times, paradoxical) effects. For example, IPQ use could shift dramatically from one community to another without sales triggering the right. Even with a large shift of shares in to one community, a small portion of the benefiting community's PQS could be transferred with the intent of using the yielded IPQ in the community that has lost processing. At the time of this transfer, the entity representing the community that has benefited from attracting additional processing would have a right of first refusal on the transfer. Under these circumstances, the right enhances the leverage of the entity of the community that has attracted substantially more processing and provides no power to the community that has lost processing. Although this possibility is somewhat speculative, it could arise in instances where a single company has multiple operations in a region or where substantial amounts of processing are consolidated through custom processing.

Possible amendments:

- 1) Require parties to rights of first refusal contracts to remove the provision that rights lapses, if the IPQ are used outside the community for a period of three consecutive years
- 2) Require parties to right of first refusal contracts to remove any provision for the right to lapse if an entity chooses not to exercise its right
- 3) Require that any person holding PQS that meet landing thresholds qualifying a community entity for a right of first refusal to maintain a contract providing that right at all times

Apply the right to the PQS only (rather than all assets included in the transaction)

Some supporters of modification of the rights of first refusal have suggested that applying the right to PQS only (as opposed to all assets that may be involved in a transaction) may more effectively protect interests of communities. Under the current structure, a community entity has a right of first refusal on a transaction involving the subject PQS (including all assets included in that transaction). The provision requires that an entity exercising the right accept all terms and conditions of the proposed transaction. Transactions may include a variety of assets, including processing equipment and real estate. Some of these assets may have no connection to the crab fisheries or the represented community. In these instances, a community entity may be unable to effectively use its right for several reasons. Financing may be more difficult to obtain as the cost of these additional assets drive up the transaction price. The entity may have no justifiable interest in assets unrelated to its host community. Acquiring these unrelated assets under the right may effectively require the entity to act as a broker for the assets to avoid maintaining those assets beyond its local interests.

To avoid the potential complications that arise from applying the right to assets beyond the PQS, it has been suggested that the right could be limited to the PQS. Under this approach, a community entity would have a right of first refusal on any PQS included in transfers, but no other assets would be subject to the right. Establishing such a right creates several issues. First, PQS values must be established, independently of other assets. With few trades and little public information concerning those trades developing a valuation method will be challenging. Under the current regulations, the right of first refusal is administered directly by the parties to the contract establishing the right. NOAA Fisheries only direct role in administration of the rights was ensure that contracts were established as required for PQS issuance. Enforcement of contracts, once established, is through civil proceedings by the parties. If this approach is continued, the regulations could define contract requirements that must be followed by the parties to ensure that fair PQS valuations apply when the right is triggered. NOAA Fisheries role, under this approach, would be to ensure that adequate contracts were entered by PQS holders prior to IPQ issuance. A system by which the parties jointly select one or more persons to value PQS could be the simplest approach to establishing a value for the PQS. Development of other competing methods for

DRAFT

establishing a value could also be considered (and should be explored), if the Council wishes to proceed with this action.

A second effect that arises from applying the right of first refusal to only the PQS in a transaction is a potential disruption to the transaction and business operations of the participants. Transactions that include assets other than PQS are likely to be valued based on all assets in the transaction (including the PQS), as a whole. At the extreme, the value of assets (particularly crab processing equipment in a community) could be quite minimal in the absence of the accompanying PQS. Given this possibility, some participants may question the equity of the right to intervene in a transaction in a manner that removes only a portion of the assets. It is unlikely that the buyer would obligate itself to complete the transaction, in the event the right on the PQS is exercised. Consequently, the exercise of the right could result in the community entity acquiring the PQS and the former holder of the PQS retaining all other assets. Whether this outcome (the PQS would be separated from the assets as a result of the right being exercised) would ever occur is doubtful, though. PQS buyers and sellers are likely to take steps to avoid the outcome.

A few avenues may be pursued to avoid the separation of PQS from related assets. First, the PQS holder may attempt to negotiate an agreement with the community entity to allow the sale to proceed without the entity exercising the right. To secure an agreement the PQS holder may need to provide something of value to the entity, which could be financial remuneration or a portion of the PQS. A community entity may have little leverage in this negotiation, if the PQS holder knows that the entity is without the wherewithal to exercise the right, but could receive some compensation for the security it provides by indicating its intent to allow the sale.

Alternatively, the person receiving the PQS could avoid the right being triggered by agreeing to use the requisite amount of IPQ in the community for the requisite period and extending the right to the entity in a second contract. This approach maintains that community entity's interest in the PQS under the terms of the right with the new holder. This approach would apply, only if the person acquiring the PQS is willing to use the yielded IPQ in the community for a period of years. After that period expires, the IPQ may be used outside the community.

A third way to avoid community entity intervention in a transaction is for the PQS holder, prior to the transfer, to use the IPQ outside of the community for three consecutive years causing the right to lapse.⁷ To use this approach, the PQS holder would need move the IPQ from the community ahead of the transaction to ensure the right lapsed; however, this approach provides the PQS holder with the greatest flexibility at the time of the PQS sale.

Lastly, a PQS holder that is undertaking a transaction might also subdivide the transaction. One transaction would be for the PQS; the other transaction would be for any other assets. By subdividing the transaction in this manner, the PQS holder and the buyer can ensure that the price of PQS and the price of other assets in the transaction are set at an acceptable level, if the right holder intervenes in the transaction. At the extreme, assets other than the PQS could be offered at a nominal price, with the PQS carrying the entire value of the transaction. Alternatively, the sale of other assets may be contingent on the sale of PQS (without exercise of the right). Clearly, a variety of contractual arrangements can be made to ensure that the PQS holder receives reasonable value for assets (including the PQS), particularly in cases where the value of the assets is highly dependent on the accompanying PQS. The extent to which

⁷ This choice may be unavailable, if the Council elects to extend the right in perpetuity.

DRAFT

these different arrangements might circumvent the Council purpose for applying the right to the PQS exclusively depends on the goal it intends to achieve with this change.

An alternative approach to applying the right of first refusal exclusively to PQS is to apply the right to PQS and any assets based in the community protected by the right of first refusal. This approach necessitates a system for valuing the PQS and other community-based assets. Valuing these other assets (beyond the PQS) will further complicate administration of the right. As with an approach that applies the right exclusively to the PQS, PQS holders and persons acquiring PQS could use a variety of means to ensure that their positions are not diminished by the right. Whether these different arrangements subvert the Council's intent depend on its object in considering this amendment.

Possible amendments:

- 1) Require parties to rights of first refusal contracts to provide that the right shall apply only to the PQS. In the event other assets are included in the proposed sale, the price of the PQS to which the price applies shall be determined by:
 - a) an appraiser jointly selected by the PQS holder and the entity holding the right of first refusal, or,
 - b) *further options to be developed by the Council.*
- 2) Require parties to rights of first refusal contracts to provide that the right shall apply only to the PQS and other assets physically present in the community benefiting from the right of first refusal. In the event other assets are included in the proposed sale, the price of the PQS to which the price applies shall be determined by:
 - a) an appraiser jointly selected by the PQS holder and the entity holding the right of first refusal, or,
 - b) *further options to be developed by the Council.*

A loan program to support community entity purchases

Periodically throughout discussions of community entity rights of first refusal, community representatives and other stakeholders have suggested that the effectiveness of the right of first refusal may be limited in cases where the right holder is without the wherewithal to exercise the right. Some supporters of the right (and the crab advisory committee) have suggested that the development of a federal loan program to support purchases of QS and PQS could benefit right holding entities and the communities that they represent. Since the Council has no authority for the development of a loan program to support holders of a right of first refusal on PQS, it may only suggest that such a program is appropriate.

The need for loan support likely varies substantially across these entities. CDQ communities are represented by their local CDQ groups. These groups already hold substantial fishery assets and have access to financing comparable to (or, in some cases, better than) many other participants in the fisheries. Yet, it is possible that funding for particularly large transactions could be inaccessible to CDQ groups. Other communities are represented by entities with substantially poorer access to financing. These entities may find financing challenging on even small transactions. In considering whether to suggest that a loan program be developed for right holders, the Council should consider these differences among right holders and the scope of the program that it believes should be developed. If the Council believes that the program should be used to support only certain transactions or right holders, it should develop criteria for those limitations and a rationale for the limitations. These limitations could be developed (or suggested) at this time or could be developed, if a loan program is authorized in the future.

DRAFT

Conclusion

As the Council begins the process of developing an amendment package to modify rights of first refusal, it should focus its efforts on developing a thorough understand of its purpose and the extent to which the amendment package will achieve that end. In its current form, the right of first refusal provides a community entity with some leverage in the event a PQS holder wishes to transfer PQS. Yet, a PQS holder may take several measures to limit the effectiveness of the right. The moderate measures proposed to date may strengthen the position of the community entity slightly; however, these measures are unlikely to substantially change the negotiating position of a right holder, particularly if the PQS holder is determined to undermine that negotiating position. More realistically, the right (either in its current form or as modified by the proposed measures) will provide community entities (and the communities that they represent) with both negotiating leverage and political leverage, in the event that a PQS holder wishes (or attempts) to move IPQ use from a community to the detrimental of the community.