

**Exemption of Custom Processing from Crab Processing Caps
North Pacific Fishery Management Council
June 2006**

The recent reauthorization of the Magnuson Stevens Act (MSA) included a provision to exempt custom processing in the North region of the Bering Sea *C. opilio* fishery from processing use caps established under the crab rationalization program. The exemption is believed to be intended primarily to improve efficiency in processing in that fishery. At its February 2007 meeting, the Council received a staff discussion paper concerning the implementation of this amendment and the potential for the Council extending the exemption to other fisheries included in the crab rationalization program. After receiving the discussion paper, input from the Advisory Panel, and hearing public testimony, the Council elected to consider whether this exemption should be extended to include all of the traditionally small crab fisheries governed by the rationalization program:

- the Western Aleutian Islands golden king crab fishery,
- the Western Aleutian Islands red king crab fishery,
- the Eastern Aleutian Islands golden king crab fishery,
- the St. Matthews blue king crab fishery, and
- the Pribilof red and blue king crab fishery.

Specifically, the Council requested staff to develop a draft purpose and need statement for the action for Council consideration, citing possible rationales for the action of enhancement of competition, contingencies in the event of a processor breakdown, processing efficiencies, enabling full harvest of the TAC, and sustaining coastal communities. Provided the Council elects to continue with this action, it is anticipated that the development of regulatory analyses and specific regulatory provisions to implement the exemption for the North region of the *C. opilio* fishery will be combined with the analysis and development of the amendment package used by the Council to consider extending the exemption to these other fisheries.

This paper includes a section describing the background for this action, a draft purpose and need statement for Council consideration, and draft elements and options that could be considered for analysis. The paper also includes a brief discussion of an issue related to the use of transferred shares in their community of origin and the application of the use cap to custom processing of those shares. This issue arises because of the possible divestiture of shares by an entity required to comply with the use cap. Under the current rules, on divestiture those shares could not be custom processed at the plant of origin. This use cap would effectively force either a new processor (either shore plant or floater¹) to be opened in the community or the shares to be moved from the community. The Council may wish to consider whether it is appropriate to develop a provision that would permit continued processing of these shares at the plant of their origin.

Background

To understand the custom processing use cap exemptions adopted under the MSA reauthorization and those proposed to the Council requires a basic understanding of the current processing share allocations and processing share use caps. Under the program, processor quota shares (PQS) were allocated to eligible processors in each fishery based on qualified processing history. Holders of PQS receive annual allocations of individual processor quota (IPQ), which authorize the holder to accept delivery of a specific number of pounds of crab harvested with Class A individual fishing quota (IFQ). Class A IFQ have one-

¹ Regulations limit processing to shore plants and stationary floating processors. In this document, any reference to a floating processor is a stationary floating processor.

to-one correspondence with IPQ and are issued for 90 percent of the annual total allowable catch (TAC) in each fishery. In the Bering Sea *C. opilio*, fishery Class A IFQ and IPQ are regionalized, with each share designated for landing either North or South of 56°20' N latitude (i.e., North region or South region). Allocations to North are approximately one-half of the total IPQ allocation in the fishery.

Adopted by the Council in June of 2002, the use caps prevent a single processor from using more than 30 percent of the processing shares in a fishery. An additional provision limits any processor from using in excess of 60 percent of the processing shares in the Northern region in the Bering Sea *C. opilio* fishery. No regional processing cap applies in any other fishery. So, a processor in the North would be restricted to processing 60 percent of the North IPQ allocation and to processing no more than 30 percent of the total allocation (including all processing in the North and South). Depending on the amount and North/South distribution of a processor's activity, either or both of these caps could be constraining. In most cases, though, the roughly equal allocation of shares in the North and South implies that if the North processing cap is binding, the overall cap will also bind.

Individual use caps are typically interpreted to prohibit an entity from holding either the long term shares (PQS) or annual allocations yielded by those long-term shares (IPQ) in excess of the cap. At its October 2002 meeting in clarifications to its original motion, the Council adopted the following broader interpretation of its processing share use caps:

Although custom processing is permitted by the Council motion, the Council established that limits on ownership and use would count any crab custom processed by a plant toward the cap of the plant owner. The application of the cap to custom processing is intended to prevent consolidation, which could occur if custom processing is not considered.

Under this provision, not only are shares held by an entity counted toward that entity's cap, but also any processing undertaken at the entity's plants is counted toward its cap. Under the regulation, all processing at a plant that a person has a 10 percent or more ownership interest counts against that person's cap. Construed in this manner, the caps require at least two processors to operate in the North region of the Bering Sea *C. opilio* fishery and at least four processors in every fishery. Examining the regional distribution of processing shares provides some perspective on the extent to which current caps prevent consolidation (see Table 1).

Table 1. Regional distribution of processor quota shares by fishery (2006-2007).

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Fishery	Region	Number of PQS holders	Percent of PQS pool
Bristol Bay red king crab	North	2	2.6
	South	23	97.4
Bering Sea <i>C. opilio</i>	North	11	47.0
	South	22	53.0
E. Aleutian Islands golden king crab	South	9	100.0
Pribilof Island red and blue king crab	North	6	67.5
	South	11	32.5
St. Matthews blue king crab	North	9	78.3
	South	9	21.7
W. Aleutian Islands golden king crab	Undesignated	9	50.0
	West	10	50.0
W. Aleutian Islands red king crab	South	10	100.0

Source: NMFS RAM, PQS holdings 2006-2007.

In the Bering Sea *C. opilio* fishery, both the 60 percent cap on North region processing and the general 30 percent cap require two processors to operate in the North region. The custom processing exemption would allow North processing to consolidate in a single plant. In the Eastern Aleutian Islands golden king crab fishery, the exemption could allow all processing to be consolidated into a single plant. In the Pribilof Island fishery, three North plants would be required to operate under the current general cap, since over 60 percent of the processing shares carry a North region designation. Two plants would be required to operate in the South, since over 30 percent of the processor shares are designated for South region use. In the St. Matthews fishery, three plants are required to be operated in the North region, while one plant could process all crab in the South region. In the Western Aleutian Islands golden king crab fisheries, 50 percent of the Class A IFQ and IPQ are regionalized, with landings from those shares required to be made west of 174° W longitude (the West region). These West region shares in this fishery were issued proportionally to history, since qualified history in the West region was less than 50 percent of the total qualified history. The 30 percent share cap effectively requires two plants to operate in the West region for the fishery and at least four plants in the fishery overall. In the Western Aleutian Island red king crab fishery, at least four plants must operate under the current 30 percent cap. In considering these data, it should be borne in mind that, the current cap without the exemption could prevent custom processing from being consolidated into a particular processor's plant. For example a processor that holds 30 percent of the St. Matthews, split equally between the North and South region, could not consolidate any processing through custom processing at its plants, since its holdings and processing activity are constrained by the cap.

Draft Purpose and Need Statement

The MSA exemption of custom processing from use caps in the North region of the Bering Sea *C. opilio* is believed to be intended to enhance processing efficiencies. Under the rationalization program, fishing and processing are extended over a longer period of time. This extension of the season allows for both sectors to achieve production efficiencies by reducing capacity and inputs. Applying use caps to plants limits the ability to achieve production efficiencies by preventing consolidation of operations that would achieve economies of scale. In some small fisheries or in regions that are expensive to operate in, the combination of extended operational time and limits on consolidation in the rationalized fishery could lead to a loss of production efficiency in processing in comparison to the pre-rationalization, limited access, derby fishery. In some cases, these use caps could limit entry by or competition from processing platforms that can operate with greater efficiency only at higher production levels. Depending on the circumstances, not counting processing at a plant toward a share holder's use cap could also allow for processing consolidation in the event of unexpected circumstances (such as a breakdown at a competing facility). Lastly, not counting processing at a plant toward a share holder's use cap could aid in a situation in which availability of processing capacity prevents the TAC from being fully harvested. These potential purposes could be combined into the following purpose and need statement:

In remote areas and small TAC fisheries, the extended fishing seasons under rationalization require processing activity to be extended over a longer period of time. This temporal extension of processing activity, together with the lower throughput levels, limits the ability of processors to achieve production efficiencies. Allowing concentration of processing in fewer facilities, by exempting custom processing at a plant from the use cap of the plant owners, could increase processing efficiency. This efficiency increase could improve competition in processing. In some cases, exemption of custom processing at a facility from use caps of the owner could provide for contingencies in the event of a facility breakdown, assist in allowing full harvest of the TAC, and contribute to community sustainability.

MSA exemption of North custom processing in the Bering Sea *C. opilio* fishery from processing use caps

The suggested revision to the use caps in the small crab fisheries would be based on the exemption developed in the MSA for the Bering Sea *C. opilio* fishery. Generally, that provision would exempt custom processing in the North region from the use caps. Provided processing share holders comply with the custom processing exemption, all North processing could be undertaken at a single facility. The rationale for the provision is that the slow rate of landings under the rationalization program has reduced processing efficiencies, particularly in low TAC years. Allowing all North processing to occur at a single platform would improve efficiencies. Limiting the exemption to custom processing is intended to prevent consolidation of holdings that could occur, if the processing of held or owned shares were included in the exemption. The specific provision in the MSA affecting the *C. opilio* fishery processing caps provides:

- (1) IN GENERAL. – Notwithstanding sections 680.42(b)(ii)(2) and 680.7(a)(ii)(7) of title 50, Code of Federal Regulations, custom processing arrangements shall not count against any use cap for the processing of *opilio* crab in the Northern Region so long as such crab is processed in the North region by a shore-based crab processor.
- (2) SHORE-BASED CRAB PROCESSOR DEFINED. – In this paragraph, the term “shore-based processor” means any person or vessel that receives, purchases, or arranges to purchase unprocessed crab, that is located on shore or moored within the harbor.
MSA §122(e).

The provision references two sections of the crab rationalization program regulations. Section 680.7 defines prohibitions, including the prohibition on exceeding the processing share use cap, from which custom processing in the North region would be exempt. That section specifically defines a prohibition:

For an IPQ holder to use more IPQ crab than the maximum amount of IPQ that may be held by that person. *Use of IPQ includes* all IPQ held by that person and *all IPQ crab that are received by any R[egistered] C[rab] R[eciever] at any shoreside crab processor or stationary floating crab processor in which that IPQ holder has a 10 percent or greater direct or indirect interest.* (50 CFR 680.7(a)(7)) (emphasis added).

Section 680.42 sets out the specific percent limits of the use caps, which include both a use cap of 30 percent on Bering Sea *C. opilio* processing shares and a use cap of 60 percent on North region Bering Sea *C. opilio* processing shares. The provision is believed to be intended to exempt custom processing arrangements from both of these caps.

Implementation of this provision raises a few questions. First, ‘custom processing’ must be defined for purposes of applying the exemption. Currently, federal regulations do not contain a definition of custom processing. Generally, custom processing is understood to be an arrangement under which a person processes crab on behalf of another, never taking ownership of the crab. Alaska regulations define a “custom processor” as a person who sells or offers for sale the service of seafood processing but who does not own the seafood being processed (18 AAC 34.990). This provision is implemented by identifying the actual owner of the crab (rather than the person processing the crab under the custom processing arrangement) on the fish ticket. Section 680.5(d)(8) contains a provision requiring a processor of crab to identify the party for which custom processing is being undertaken. This requirement could be used to identify processing that falls within the use cap exemption. Such an approach parallels the State of Alaska’s treatment of custom processing arrangements (which is used, in part, for determining liability for fish tax payments).

A simpler approach to developing the exemption could be to apply the cap based solely on share holdings (disregarding physical processing when applying the cap). Under this approach, only a person's share holdings (direct and indirect) would be considered when applying the cap. Defining the cap in this manner would simplify management of the cap, by allowing the agency to consider only share holdings, avoiding the need to collect and assess plant ownership information when applying the cap. Such an approach could be used by processors to use more creative ownership structures and risk sharing in fisheries and areas subject to the cap.²

A second issue that arises is the interpretation of "moored within the harbor". The provision is somewhat ambiguous, since no definition of "harbor" is contained in the current regulations. Legislative intent is believed to be lacking concerning this definition. Since the North region contains several harbors – for example, St. Paul, St. George, and Nome are all in the North region and have harbors – the provision will require development of a workable definition of "moored within the harbor". This provision is believed to be intended to protect community interests. The current, interim interpretation of the provision is that processing on a floating processor within the harbors of St. Paul and St. George would be considered moored within the harbor. A different definition could be adopted through the regulatory process, including through the Council as a part of a package extending the exemption to other fisheries as is currently under consideration.

To implement the use cap exemption, NOAA Fisheries will need to adopt conforming regulations. The revision will also require analysis of the interpretation of these specific cap exemptions. The timing of the analysis is not currently scheduled, but is likely to begin in the near future. The analysis and rule making process are likely to proceed in the usual timeline, which will encompass several months prior to finalization in regulation. In the meantime, NOAA General Counsel has issued the guidance letter attached concerning its interpretation of the MSA Bering Sea *C. opilio* custom processing exemption. That guidance will be superseded by future regulations addressing the exemption.

Exemption of custom processing in additional fisheries

The extension of the exemption of custom processing from use caps to other fisheries will require the Council to specify the scope of the exemption consistent with the rationale expressed in the purpose and need statement. Allowing additional concentration of processing activity could provide an opportunity to improve production efficiency, but whether actual improvements are feasible is not known. In fisheries and regions with low amounts of harvests the ability of processors to achieve efficiencies of scale could be limited. Some processors may choose not to use larger, more efficient platforms in those markets, if they believe throughput is too dispersed or is not adequate to achieve reasonable efficiencies. Removing custom processing from the cap calculation could lead some processors to attempt to enter platforms that require larger (or more consistent) throughput, increasing competition in processing.

It is possible that consolidation of processing under the exemption could aid in addressing unanticipated circumstances in areas and fisheries with limited processing capacity. For example, if a processing platform is disabled, it is possible that allowing custom processing beyond the cap could be used to overcome logistical complications. For example, if a platform is disabled or inaccessible, rerouting landings to a different platform could limit disruption to harvester's fishing and landings schedules. Similarly, if a processing platform is disabled near the end of a season or if the cost of delaying fishing is too high for harvesters, it is possible that the exemption of custom processing could enable participants to fully harvest the TAC in cases when a portion of the TAC could be stranded. The cap exemption could also benefit some communities. For example, if the cap is preventing the consolidation of processing in a

² Any such coordinated arrangement would need to fully comply with any requirements and limitations of antitrust law, regardless of the rules governing application of the caps.

community or leading an IPQ holder to process its shares outside of a community, it is possible that the exemption could benefit the community.

Whether the exemption is likely to lead to any of these different benefits is likely to depend on the circumstances. In considering the different effects, it will also be important to consider that achievement of one benefit may effectively preclude another benefit from being realized. For example, a custom processing arrangement could be finalized in the preseason that leads to scheduling a single plant to operate in a region during a particular fishery. This arrangement could complicate any efforts to address contingencies that could arise, if that platform is later disabled or inaccessible. These competing effects will need to be explored as a part of the analysis of this action, but also could be considered in developing alternatives for analysis.

The Council should also consider the potential effects of the cap exemption resulting in consolidation of processing in a single processor in a region or fishery. This concentration could improve production efficiencies, particularly for processing in remote regions. On the other hand, this level of consolidation would reduce the market for landings, leaving all harvesters in the region (or fishery) with a single plant at which deliveries must be coordinated.

Elements for consideration

To advance the analysis of a potential action to exempt custom processing from use caps, the Council will need to develop specific elements and options. Several different aspects of the exemption should be considered in defining alternatives for analysis.

Fisheries and Regions

The Council has suggested that it is considering exempting custom processing in several fisheries from the use caps. In considering whether it is appropriate to apply the exemption to a particular fishery, the Council could consider the extent to which the cap in the absence of the exemption is likely to constrain processing consolidation. The size of the fishery, the temporal distribution of deliveries and processing, and the regional distribution of processing shares are all likely to affect the extent to which the exemption could relieve the constraint of the cap. Since all seasons extend over several months and fishing may be concentrated during a portion of the season, season length is not a reliable measure of the temporal dispersion of processing. In several fisheries, the processing cap constrains consolidation, particularly in remote regions of the fisheries (see Table 2).³

³ The discussion in this section is limited to fisheries that the Council has indicated that it is considering for the custom processing cap exemption.

Table 2. Most recent TAC, processing cap at most recent TAC, and remote region percent of IPQ and IPQ in pounds at most recent TAC.

Fishery	Most recent opening			Remote region		
	Year	TAC	Processing cap	Designation	Percent of IPQ	IPQ in pounds*
Bristol Bay red king crab	2006 - 2007	13,974,300	3,480,706	North	2.6	301,661
Pribilof red and blue king crab	1998	1,250,000	324,554	North	67.5	730,246
St. Matthews blue king crab	1998	4,000,000	1,023,406	North	78.3	2,671,090
Western Aleutian Islands red king crab	2003 - 2004	500,000	79,572	None	NA	NA
Eastern Aleutian Islands golden king crab	2006 - 2007	2,700,000	670,618	None	NA	NA
Western Aleutian Islands golden king crab	2006 - 2007	2,430,000	341,059	West	50.0	568,432
Bering Sea <i>C. opilio</i>	2006 - 2007	32,909,400	7,807,606	North	47.0	12,231,916
Western Bering Sea <i>C. bairdi</i>	2006 - 2007	984,600	239,710	None	NA	NA
Eastern Bering Sea <i>C. bairdi</i>	2006 - 2007	1,687,500	410,832	None	NA	NA

Source: Crab SAFE, 2006; NMFS RAM PQS holdings (2006-2007); NMFS RAM QS holdings (2006-2007).

* estimated based on most recent TAC and QS and PQS allocations.

In the Pribilof Island fishery, the cap requires at least three processors to operate, limiting each to less than 325,000 pounds. Similarly, in the St. Matthews fishery three processors would be required to operate in the North, each limited to slightly more than one-million pounds. The extent to which the current cap in the absence of the exemption would constrain consolidation in the South region is unclear. Given the number of plants that process crab in the South, the only suggested benefit of the exemption likely to arise would be to allow for production efficiency gains. Several plants could be available to process the TAC or address unexpected circumstances. Most processing in the South occurs in large plants that serve both groundfish and crab fisheries. Historically, the St. Matthews and Pribilof Island fisheries have been concentrated in the early fall, prior to fishing in the Bristol Bay red king crab fishery. Currently, the season opening in these fisheries coincides with the Bristol Bay red king crab opening. The extent to which consolidation at plants in the South would be compromised by small amounts of crab from these fisheries being either integrated with landings from the Bristol Bay fishery or run through the plant independently is not known. The extent to which allowing custom processing in excess of the cap is likely to relieve any such burden is also not known. The cap does not directly limit consolidation of processing activity in the South in the St. Matthews fishery, since less than 30 percent of the IPQ are regionalized requiring South delivery. Particular processors may be limited in their ability to engage in custom processing in the South because their combined North and South PQS holdings approach or exceed the 30 percent cap. These companies would be unable to take on custom processing of additional crab from the fishery without the exemption.

In the Western Aleutian Islands red king crab fishery, the low TAC and relatively large share of the fishery allocated to catcher processors leads to a processing cap of less than 100,000 pounds. The current effect of the cap is likely limited to constraining processing efficiency, since most of the processing in this fishery has occurred in Dutch Harbor. Whether the exemption would lead to redistribution of processing to the west, closer to the fishing grounds, is not known.

In the Western Aleutian Islands golden king crab fishery, the cap limits each processor is limited to less than 350,000 pounds at current TAC levels. The caps require at least four plants to operate in each fishery and two plants to operate in the West region of the Western Aleutian Islands fishery. In the West region, the caps could limit consolidation. Currently, only one shore plant processes crab in that region. Exempting custom processing from the cap in that region could allow that plant (or possibly a floater depending on the specific exemption) to process all crab in the fishery in the region. Since the portion of the fishery that is not West designated is not subject to any regionalization, the custom processing cap exemption could also induce additional processing in remote areas by drawing undesignated IPQ to the

West region. Applying the exemption in the West region could address processing inefficiencies that region, provide benefits to remote communities, or be used contingencies in the fishery. As in the Pribilof and St. Matthews fisheries, the benefit of applying the exemption outside of the West region is likely to be limited to improving processing efficiencies, as substantial processing capacity and activity exists in Dutch Harbor, the primary port outside of the West region. In the Eastern Aleutian Islands golden king crab fishery, each processor is limited to approximately 700,000 pounds. Almost all processing activity is in Dutch Harbor. Consequently, the benefit from a cap exemption is likely to be limited to improved processing efficiency.

Platforms eligible for the exemption

The second aspect of the exemption that the Council could consider in developing options for analysis is whether to limit the exemption to plants operated in certain locations. The MSA provision creating an exemption in the North region of the Bering Sea *C. opilio* fishery applies only processing that occurs on a shore-based plant or on a plant that is moored in a harbor. The Council could choose among three different approaches to the exemption. The Council could exempt custom processing at shore plants only, at shore plants and floaters moored in a harbor, or at any plant.

Exempting only shore plants could be used to benefit those plants that have the strongest locational ties. These plants could provide community benefits through resident processing crews and support facilities. The extent of these benefits will vary across communities and facilities. Applying the exemption to shore plants only would provide owners of existing shore plants with a much stronger position in the market by limiting the ability of floating processors to compete on the same terms (i.e., subject to the same exemption). For a floating processor to compete on equivalent terms with the existing shore plant would require the capital investment to develop a crab processing shore plant in the region. Compelling the development of additional shore facilities to induce competition would seem inappropriate and inconsistent with the some of the stated rationales for the exemption. The magnitude of this effect differs across fisheries and regions with the number of shore plants.

Depending on the exact terms of the exemption, extending the exemption to floating processors “moored in a harbor” could allow additional competition, while deriving or preserving some of the community benefits from the exemption. If the Council could adopt a definition that relies on community boundaries for determining whether processing is occurring on a platform “moored within a harbor,” the provision could be used to ensure that communities receive the fish tax from processing activity arising under the exemption. The provision could use either city or borough boundaries for determining the scope of the requirement that a vessel be moored within a harbor. Using borough boundaries may be more consistent with existing aspects of the program, given that the cooling off provision applied at the borough level and the right of first refusal extend to the borough in one instance.⁴

If the Council’s primary objective is to allow greater flexibility in consolidation of processing, the exemption could be applied to custom processing in the fishery and region regardless of whether the processing is on a floater or within community boundaries. This provision could provide processors with greater flexibility in locating floating platforms, but may sacrifice some community benefits that could arise under a more restrictive exemption.

⁴ In its enforcement guidance letter concerning to the MSA exemption of custom processing from processing use caps in the North region of the Bering Sea *C. opilio* fishery, NOAA GC defined “moored within the harbor” as being within the harbor of St. George or St. Paul shown on navigation charts. The definitions suggested here are believed to better parallel community interests of concern to the Council without detracting from potential benefits.

Possible elements and options

The following elements and options could be considered by the Council for this action:

Fisheries and Regions:

Custom processing will be exempt from use caps in the following regions and fisheries:

The North region of the Bering Sea *C. opilio* fishery (analyzed here for regulation change from MSA reauthorization – not optional)

- Option 1) the Western Aleutian Islands golden king crab fishery,
Suboption: West region only
- Option 2) the Western Aleutian Islands red king crab fishery,
- Option 3) the Eastern Aleutian Islands golden king crab fishery,
- Option 4) the St. Matthews blue king crab fishery, and
Suboption: North region only
- Option 5) the Pribilof red and blue king crab fishery
Suboption: North region only

Definition of custom processing exemption:

- Option 1) Physical processing of crab at a facility owned by an entity does not count toward the cap of the entity (only processor share holdings count toward an entity's cap).
- Option 2) Custom processing is the processing of crab received with IPQ that has 50 percent or less common ownership with the processing plant.

Locations qualified for the exemption:

Custom processing will qualify for the exemption provided that processing is undertaken in the applicable fishery and region at:

- Option 1) a shore plant
- Option 2) a shore plant or a floating processor that is moored in a harbor
A floating processor moored within a harbor, if it is moored within the boundaries of:
 - Suboption A) a first or second class city or borough
 - Suboption B) a first or second class city
- Option 3) any shore plant or floating processor

Possible interaction with community provisions

Any relaxation of limits on the consolidation of processing activity is indirectly affected by the regionalization component of the rationalization program. Consolidation cannot occur across regions, regardless any absence of direct limits on consolidation. So, a processor with shares in both regions will be compelled to have crab processed at two plants, regardless of any exemption allowing the movement of shares through custom processing arrangements. Unlike regionalization, the right-of-first-refusal, which benefits communities in which crab was historically processed, applies only to the sale of PQS and IPQ. Since IPQ are not transferred under a custom processing arrangement, custom processing would not seem to trigger the right of first refusal. A possible concern is the provision for a right of first refusal to lapse, if a PQS holder uses shares outside of the historic community for a period of three consecutive years. To the extent that processing consolidates away from a community of origin because of the exemption of custom processing from use caps, the exemption could harm communities that have historic dependence on the fisheries. Assessing any potential for consolidation across community boundaries arising from the custom processing exemption from use caps is challenging and may not be possible.

The distribution of rights of first refusal and regionalization provides some perspective on the potential for consolidation under the exemption to lead to lapse of rights of first refusal (see Table 3). It is important to note that the exemption only has an effect, if the share cap would have been binding in the absence of the exemption. Unless the use cap prevents shares from being consolidated (either inside or out of a community), the exemption has no effect; however, in fisheries with relatively small TACs (such as those being considered for the exemption) it is possible that most or all of the processing in a region could be consolidated in a single facility. Whether movement of processing outside of a community would be economical would likely depend on the circumstances. For example, in most instances, it would seem that movement of processing from Dutch Harbor plants to other communities that have less accessible services would add to processing costs.

If the Council believes that this movement of shares should not lapse rights of first refusal, it could clarify that the custom processing of shares does not count toward a processor's use of those shares outside of the community of origin for purposes of the lapse of rights of first refusal. This provision could be implemented by requiring processors with rights of first refusal contracts with communities to modify those contracts to include a provision specifying that custom processing would not count toward a lapse of a right of first refusal. Such an exemption would be significantly broader than necessary to address the particular issue arising under this action, but could be desirable for specifying the interaction between custom processing activity and the right of first refusal provision in the program.

Table 3. Distribution of PQS in each fishery by region and community of right of first refusal.

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Fishery	Region	Community of Right of First Refusal	Number of PQS holders	Percent of PQS pool
Bristol Bay red king crab	North	St. Paul	2	2.6
		Akutan	1	19.9
	South	False Pass	1	3.7
		King Cove	1	12.8
		Kodiak	3	3.8
		None	3	2.7
		Port Moller	3	3.5
		Unalaska	11	51.1
		Total		97.4
	Bering Sea <i>C. opilio</i>	North	None	3
St. George			2	9.7
St. Paul			6	36.3
Total				47.0
South		Akutan	1	9.7
		King Cove	1	6.3
		Kodiak	4	0.1
		None	4	1.8
		Unalaska	12	35.0
		Total		53.0
E. Aleutian Islands golden king crab	South	Akutan	1	1.0
		None	1	0.9
		Unalaska	7	98.1
Pribilof Island red and blue king crab	North	None	1	0.3
		St. Paul	5	67.3
		Total		67.5
	South	Akutan	1	1.2
		King Cove	1	3.8
Unalaska		5	24.6	
Total		32.5		
St. Matthews blue king crab	North	None	5	64.6
		St. Paul	4	13.8
		Total		78.3
	South	Akutan	1	2.7
King Cove		1	1.3	
Kodiak		1	0.0	
Unalaska		6	17.6	
Total		21.7		
W. Aleutian Islands golden king crab	Undesignated	NA	9	50.0
	West	NA	10	50.0
W. Aleutian Islands red king crab	South	NA	10	100.0

Source: NMFS RAM PQS holdings 2006-2007.

Effects of the limit on custom processing of divested shares

Recent consolidation in the processing sector is likely to lead to a divestiture of shares by a processing company that will exceed the use cap in its holdings. Portions of the holdings of the new consolidated entity are subject to rights of first refusal in two communities, including one community that is home to a single shore plant. Under the company's current plan a portion of its holdings in the two communities will be divested to comply with the cap. The shares may be divested to the entity representing the community under the right of first refusal. Under the existing processing caps, the shares divested in the single shore

plant community cannot be processed at that shore plant, since that processing activity would count toward the use cap of the consolidated entity. Whether an additional platform could be brought into the community is not known. The Council may wish to consider whether it is appropriate to develop a provision that would permit continued processing of these shares at the plant of their origin. While several options exist for developing such a provision, two of the more straightforward options are:

- Option 1) in the event that processing shares are transferred to the community entity holding the right of first refusal for those shares, the processing of those shares in the community of origin will not count toward the cap of the processing plant
- Option 2) in the event that processing shares subject to a right of first refusal are transferred from the initial recipient, custom processing of shares in the community of origin will not be counted toward cap of processing plant (the shares would only count toward the cap of the share holder)

If the Council were to advance these options for analysis, an accompanying purpose and need statement would need to be developed. A possible purpose and need statement could be:

Under the rationalization program, community interests in historic processing are protected by granting communities a right of first refusal on the transfer of shares from the community of origin. In some instances, the combination of consolidation of processing share holdings and the counting of processing at a plant against the plant owner's cap on the use of processing shares could complicate the retention of processing in the community of origin. Exempting processing of shares in the plant of origin from the use cap of the plant owner could facilitate retention of historical processing in communities.

Conclusion

In the event the Council wishes to proceed with analysis of an exemption of custom processing from processing share use caps, the Council could adopt a draft statement of purpose and need and consistent elements and options for analysis.