

# Recreational quota entity ownership caps

## Discussion paper<sup>1</sup>

December 2017

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### 1 Introduction

In December 2016, the Council requested a discussion paper exploring the possibility of changing or eliminating the ownership cap on Charter Halibut Permits (CHPs) for the Recreational Quota Entity (RQE). The RQE is a concept which was recommended by the Council in December 2016. It would allow for the creation of a non-profit entity that could purchase and hold Area 2C and Area 3A halibut quota share (QS). The pounds resulting annually from an RQE’s QS holdings would be added to the charter sector’s annual allocation to provide an adjusted charter allocation. This concept is currently being considered in the rule making process (82 FR 46016).

If approved by the Secretary of Commerce and established as a non-profit entity, an RQE would be subject to the same ownership cap regulations for the use of CHPs as any other non-profit entity. Currently regulations at 50 CFR 300.67(j)(1) state that a person may not own, hold, or control more than five CHPs, with some exceptions for initial recipients. The action that is being considered in this discussion paper is the possibility of allowing the RQE to purchase up to 30% of the CHPs in Area 2C and in Area 3A.

This action has previously been considered by the Council. Originally, it was considered in conjunction with the development of the RQE. In its first form, it was an action alternative that would have retired CHPs that did not meet a certain threshold of activity (NPFMC 2015). The Council changed this alternative at Initial Review (NPFMC 2016) to an alternative that would allow an RQE to purchase up to 10-30% (options) of all CHPs in either Area 3A or 2C, thereby temporarily removing them from use. This change was based around a discussion that halibut abundance and the demand for halibut charters may change in the future, and that allowing an RQE to purchase CHPs could add flexibility to fleet capacity, rather than through permanent restriction of supply. In April 2016, the Council chose to bifurcate this alternative from the RQE package, based on recommendations from the RQE committee and public testimony, as well as concern expressed at the SSC. The Council felt that concern around the use of CHPs, including the quantity of information about CHP use and holders, the leasing of non-transferable permits, and latent capacity, did not fit the purpose and need of the RQE and were best addressed through separate avenues.

This discussion paper focuses explicitly on the possibility of allowing an RQE to purchase and hold CHPs above the current use cap for such an entity. However, the intent for this action may have overlap with the purpose of another Council action concurrently being considered in a discussion paper on latent capacity (NPFMC 2017); a proposal that would add a new trip limit designation to each CHP. The categories

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would restrict the number of vessel (or angler) trips for each CHP within the year (i.e., annual CHP trip limits). The present discussion paper relies on and references the issues examined in the latency discussion paper as they relate. As further described in Section 4, these are actions that could be considered independently of one another, or as alternatives under the same purpose and need statement.

## 2 Examination of the Problem

The charter halibut fishery in Southeast and Southcentral Alaska is managed under an allocation that adjusts annually according to the combined commercial-charter catch limit. Stakeholders in the halibut charter sector, as well as others, have expressed concern about the potential for an increase in charter halibut angler effort and harvest, which could result in imposition of more restrictive annual management measures (e.g., bag limits, size restrictions, day of the week closure, etc) to keep the charter sector within its allocation. While an original, NMFS-issued CHP is required to be onboard a vessel in order to provide charter halibut guiding services, which restricts the total number of vessels and anglers that can participate, there has been substantial latent capacity among CHPs. Thus, increased CHP activity could contribute to more restrictive future regulations for existing charter businesses. The discussion paper on latent capacity (NPFMC 2017) which is being considered in tandem with this action, more thoroughly explains the role that CHP use plays in establishing charter halibut management measures. Controlling effort through a limit in the number of vessel trips or angler-trips could offer predictability in this variable, which may allow for greater control over management measures. However, other factors can also play a significant role, such as average weight of halibut harvested, and the charter catch limit.

The discussion paper on latent capacity also quantifies the substantial extent of unused and underused capacity in the charter halibut sector (NPFMC 2017). While it is unrealistic to think that all of this capacity will be realized, given the seasonal trends of angler demand, examples in the latency discussion paper demonstrate the potential for effort to increase by a factor of 2.4 to 3 if each CHP were used on 100 trips per season. This indicates that there are other factors, other than the requirement to have a CHP, that are constraining effort. Without substantially more data on the factors influencing angler demand, it is difficult to make long-term projections of the future level of operation within the charter sector. Since small changes to the factors that can influence management measures can result in big changes in management measures, it is likely management measures will continue to fluctuate annually under the catch sharing plan.

## 3 Initial Look at the Proposed Alternatives and the Scope of Impacts

The action that is being considered in this discussion paper is the possibility of allowing the RQE to purchase up to 30% of the CHPs in Area 2C and in Area 3A. Since an RQE would not be a charter operation able to take anglers out on halibut charter trips,<sup>2</sup> any CHPs purchased by the RQE would temporarily be removed from use. This could allow an RQE to have influence over the supply of halibut charter trips available, and corresponding effort expended.

Table 1 breaks out the count of CHPs into a number of categories. Since no individual or entity may purchase non-transferable CHPs, it is assumed the RQE's purchasing efforts would be focused only on transferable CHPs. It is unclear from the Council's motion if the 30% maximum would be applied to the pool of transferable CHPs or from the whole pool of CHPs (with the latter clearly generating a higher number of CHPs eligible for purchase). One disadvantage of establishing a cap based on the total pool of CHPs is that the number of existing CHPs will decrease as non-transferable CHPs are retired. This could

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<sup>2</sup> It is assumed that the intent was not to allow the RQE to lease CHPs to charter operations. The Council may clarify this intent.

create a fluctuating cap. If the cap is established as 30% of the pool of transferable CHPs, Table 1 shows that this represents 112 CHPs in Area 2C and 102 CHPs in Area 3A.

**Table 1 Number of CHPs for Area 2C and 3A, as of 10/31/17**

|                             | Area 2C | Area 3A |
|-----------------------------|---------|---------|
| All CHPs                    |         |         |
| Total number of CHPs        | 529     | 426     |
| 30% of CHPs                 | 159     | 128     |
| Transferable CHPs           |         |         |
| Number of transferable CHPs | 374     | 341     |
| 30% of transferable CHPs    | 112     | 102     |
| Percent of all CHPs         | 21%     | 24%     |

Source: NMFS RAM CHP database

***Could this option be successful in controlling latent capacity?***

Given the significant amount of unused and underutilized capacity within the current CHP pool, it is unlikely that an RQE purchasing only a few CHPs would have a constraining effect on effort in the long-run. If there was a sudden increase in angler demand or a new large buyer that entered the market, effort could be expanded through the remaining CHP capacity. The ability to lease also adds flexibility to the way CHPs could be more productive.

There may be a short-term decrease in effort if the RQE purchased CHPs that have been used intensively and those users exited the fishery. However, we would expect those that use their CHP the most intensively would place the highest value on their CHP and those that are used at a lower rate, or planned to be used at a lower rate due to retirement from halibut charter operations, would be relatively less valuable to their holders. Thus, the most productive CHPs are less likely to be sold, both because they are the most valuable to their users and because they are less likely to be made available to prospective buyers.

We use an example to understand the impact an RQE may have on overall charter effort if it purchased 30% of the transferable CHPs in each area and temporarily took them out of use. For purposes of this example, we use the assumption that an RQE would purchase the 112 transferable CHPs (from Area 2C) and 102 transferable CHPs (from Area 3A) with the greatest latent angler-trip capacity reported for 2016. Note that there may be other ways the RQE would strategize its purchases. Its decisions would likely be based on available funding and CHPs available for sale.

We demonstrate latent angler-trip capacity the same way as it is used in the latency discussion paper (NPFMC 2017). If we use 100 trips as an example of a “full-time” operation<sup>3</sup> and multiply this by the number of angler endorsements (this assumes one trip per day for each CHP),<sup>4</sup> we can see the possible number of angler-trips in 100 trips. Comparing this number to the number of angler-trips that were actually taken with each CHP provides the number of latent angler-trips.

Table 2 demonstrates the extent of latent capacity and use between the 30% of the Area 2C transferable CHPs that had the most latent capacity and the 70% of Area 2C transferable CHPs that had the least latent

<sup>3</sup> While the charter halibut season runs Feb 1 through Dec 31, one hundred trips was chosen for this example to demonstrate a “full time” halibut charter operations; i.e. fishing once a day from May 15 – Sept 8, with one day off a week. The majority of the CHPs are used on less than 100 trips (NPFMC 2017).

<sup>4</sup> CHPs in Area 3A are constrained to one trip per day under current management measures. However, CHPs in Area 2C may take more than one trip per day.

capacity in 2016. The transferable CHPs that represented the greatest latent capacity represented 13% of the angler-trips from all transferable CHPs, but 46% of the latent capacity, based on 100-trip season.

Even if the RQE purchased the 30% of the CHPs representing the most latency, substantial latent capacity still exists among the remaining 70% of transferable CHPs, as well as among non-transferable CHPs. For example, the 10,447 angler-trips subsumed by RQE purchase represents only 16% of the 64,238 latent angler-trips remaining during the 100-day season. It is difficult to say how many of those 10,447 angler-trips of effort could be accommodated by the remaining CHP users. The least latent 70% of the CHPs in Area 2C, represented 87% of the angler-trips, but 54% of the latent capacity, based on 100-trip season.

There are many factors that determine whether a party is able to book a trip, such as available dates, party size, preferred boats or guides, etc. For the most heavily used CHPs, most of the available capacity would likely be in the shoulder seasons.

Using the same technique, we consider Area 3A in Table 3. This table shows that if the RQE purchased 30% of the transferable CHPs that represented the most latent angler-trip capacity in Area 3A in 2016, this represents 34% of the total angler-trips, but 52% of the latent capacity, based on a 100-trip season.

Looking at the potential number of angler-trips in Area 3A, under the scenario of 100 trips per season, we see that the 30% of CHPs hypothetically purchased by the RQE represented 34,006 angler-trips in 2016. This falls under the potential capacity for the remaining 70% (with 78,318 angler-trips latent), but again, it is unclear if the remaining CHP holders can absorb this capacity. The least latent 70% of the Area 3A transferable CHPs took 66% of the area's angler-trips in 2016, and represented 48% of the area's latent angler-trip capacity.

**Table 2 Area 2C angler-trips in 2016 and potential angler-trips if all CHPs were used to their full endorsement for 100 trips per year, split by the most latent 30% and the least latent 70%**

| Transferable CHPs.... | Number of CHPs | Potential angler-trips | Angler-trips taken in 2016 | % of total angler-trips in 2016 | Latent angler-trips | % of total latent angler-trips | % of potential angler-trips taken |
|-----------------------|----------------|------------------------|----------------------------|---------------------------------|---------------------|--------------------------------|-----------------------------------|
| Held by RQE (30%)     | 112            | 65,500                 | 10,447                     | 13%                             | 55,053              | 46%                            | 16%                               |
| Not held by RQE (70%) | 262            | 131,400                | 67,162                     | 87%                             | 64,238              | 54%                            | 51%                               |
| Total 2A              | 374            | 196,900                | 77,609                     | 100%                            | 119,291             | 100%                           | 39%                               |

Source: ADF&G saltwater logbook data sourced through AKFIN

**Table 3 Area 3A angler-trips in 2016 and potential angler-trips if all CHPs were used to their full endorsement for 100 trips per year, split by the most latent 30% and the least latent 70%**

| Transferable CHPs.... | Number of CHPs | Potential angler-trips | Angler-trips taken in 2016 | % of total angler-trips in 2016 | Latent angler-trips | % of total latent angler-trips | % of potential angler-trips taken |
|-----------------------|----------------|------------------------|----------------------------|---------------------------------|---------------------|--------------------------------|-----------------------------------|
| Held by RQE (30%)     | 102            | 119,400                | 34,006                     | 34%                             | 85,394              | 52%                            | 28%                               |
| Not held by RQE (70%) | 239            | 144,400                | 66,082                     | 66%                             | 78,318              | 48%                            | 46%                               |
| Total 3A              | 341            | 263,800                | 100,088                    | 100%                            | 163,712             | 100%                           | 38%                               |

Source: ADF&G saltwater logbook data sourced through AKFIN

Overall, these scenarios exemplify how an RQE can remove substantial latent capacity from the charter fishery (46% in 2C and 52% in 3A) by purchasing the “most latent” 30% of the area’s transferable CHPs and temporarily removing them from the fishery. However, like squeezing a balloon, it is possible for this displaced effort to manifest in other places. The effort currently expended by these CHPs is not large and may be able to be absorbed by transferable and nontransferable permits, Community Quota Entities (CQE) community charter permits, and United States Military Morale, Welfare and Recreation (MWR) charter permits remaining in the fishery. A CHP holder that does not sell their CHP and does not use it at maximum capacity, may find it profitable to lease it out on days they do not use it. Leasing of non-transferable CHPs may increase as the value of the CHPs still in circulation increases with the diminished supply. An RQE’s ability to control effort through the purchase of CHPs depends on how the sector responds to the diminished supply of CHPs.

Note that if this action is considered in conjunction with an action to diminish latent capacity through annual CHP trip (or angler-trip) limits (as discussed in the CHP latency discussion paper), an RQE’s ability to influence effort may be more effective. In this case, the RQE may focus its purchases toward the tier of CHPs without (or with the highest) trip limit to have the most influence on controlling effort. This could result in relatively less availability in the CHPs with least restrictive annual CHP trip limit category.

Practically speaking, purchasing CHPs may be an expensive way to control latent effort. It is still unclear where an RQE may acquire a long-term source of funding. However, based on prices currently listed at Alaska Boat and Permit (11/8/17),<sup>5</sup> an Area 3A 5-angler CHP recently sold for \$47,000 and an Area 3A 6-angler CHP is listed for \$70,000. If the 102 CHPs in Area 3A were sold at \$70,000 per CHP, these CHPs would cost approximately \$7.1 million.<sup>6</sup> Note that this is assuming prices would remain stable. It would be expected that the price of CHP would increase as the supply is reduced. An RQE would need to determine where their funding is most cost-effective, by reducing or capping effort in the fishery or purchasing halibut QS to contribute to the charter sector catch limit.

### ***What other types of impacts might it have?***

One entity purchasing 30% of the (transferable) CHPs in each area would likely have an impact on the CHP market. Assuming an RQE is able to identify a funding source, this entity could have significant market power. Its purchases would likely increase the price of CHPs and make it more difficult to identify CHPs available for purchase. The market for leasing both transferable and non-transferable CHPs would likely be more active.

The Council may also consider how the RQE would participate in the CHP market and if there would be any other restrictions on the buying or selling of CHPs. For instance, it is assumed the RQE would use the current market structure for identifying CHPs available for sale. This could be through a broker or through a private transaction. Once established, individuals/ entities that hold CHPs and are interested in selling may seek the RQE out. It is assumed that the sale of a CHP to an individual or entity to be used in a charter operation would be overseen by the RQE board of directors. This is a similar process to what would be expected for the purchase and sale of halibut QS. In addition to market power, this allows the board the power to choose where CHPs are sold, if there are multiple interested parties.

Allowing an RQE to purchase CHPs may have less of a direct adverse impact to existing charter operations than implementing annual CHP trip (or angler-trip) limits (see latency discussion paper), because a CHP holder could choose whether to sell their CHPs to an RQE based on its individual value.

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<sup>5</sup> (<http://www.alaskaboat.com/permitpage.php>).

<sup>6</sup> Area 3A has an average angler-endorsement of 11.7 for the 30% of the CHPs that represent the most latent angler-trip activity in 2016. Thus, as price varies substantially depending on the angler-endorsement, total cost would be expected to be much greater than \$7.1 million. Area 2C has an average angler-endorsement of 5.8 for the 30% of the CHPs that represent the most latent angler-trip activity in 2016. No recent prices were available for Area 2C CHPs.

An annual CHP trip limit may change the value of a holder's CHP without compensation, while a seller of a CHP would receive compensation under this proposal. However, there could be indirect effects on the fishery from these willing-buyer, willing-seller transactions.

For instance, we would expect CHPs that are used at a lower rate or about to be used at a lower rate due to retirement from halibut charter operations, would be less valuable to their holders than those being used at a high frequency by their holders. Thus, the most productive CHPs are less likely to be sold. From a productivity standpoint, having fewer CHPs that are used at a higher rate is more efficient. However, depending on how the sector responds to the diminished supply of CHPs, having fewer CHPs that are used at a higher rate could change the characteristic of the charter fishery.

The extent of latent CHP capacity in the fishery is indicative of the current diversity of types of halibut charter operations. Many businesses in the halibut charter sector offer charter trips where anglers can target a variety of species. Some operations rarely take halibut trips and primarily focus on other species and some are mainly focused on halibut. Some charter halibut fishing opportunities are in conjunction with time spent at a lodge or on a multi-day cruise. Some businesses exclusively offer fishing trips and some offer package deals including hunting, hiking/beach combing, and/or wildlife viewing. There is also quite a bit of diversity in the size and extent of operations, from full time operators to 'weekend warriors'. If an RQE purchases 30% of the (transferable) CHPs and only those that use their CHP the most retain their CHP, this could reduce some of the diversity in the types of operations that exist. This may also result in a loss of employment for jobs directly related to halibut charter fishing and could have negative distributional impacts on communities that benefited from these types of halibut charter operations.

One way to possibly mitigate some of these impacts is implementation of both the annual CHP trip limit categories suggested in the CHP latency discussion paper in conjunction with allowing an RQE to purchase CHPs. The annual CHP trip categories would provide some level of continued opportunity for businesses that wanted to have access to halibut fishing, but do not take a large number of halibut trips per year.

Allowing an RQE to buy up to 30% of the CHPs in each area, removing this capacity from use, would likely impact the charter anglers as well. A diminished supply of CHPs could make halibut charter trips more expensive and/ or less available, particularly during peak season. However, there are some CHPs not used in a year and many used at low levels. If the RQE purchased these CHPs with significant latent capacity, the reduction in the supply of halibut charter seats might not be felt so acutely. This change could affect the operation of the businesses that remain. For instance, it could give businesses more of an incentive to try to fill seats on a vessel, rather than use a 6-angler CHP for a group of three anglers. It may also motivate businesses to work harder to fill seats in the shoulder season, where most of the unused capacity exists.

If the RQE is successful at maintaining more control over the level of effort expended by temporarily removing CHPs from operations, this could decrease some of the negative distributional impacts experienced by the remaining charter operations from stricter management measures. It could potentially provide more predictable and relatively less restrictive management measures for remaining operations, which could indirectly positively impact other halibut user groups as well. If halibut abundance increased, the RQE could transfer the CHP (presumably through a sale) back into the charter sector. This would allow effort and capacity to react to the other factors that influence halibut charter management measures.

If the RQE is successful at maintaining more control over the level of effort expended, it could also decrease some of the competition for the halibut resource between the charter sector and other user groups. For instance, the ability to loosen management measures by controlling latent effort, may lessen the RQE's pressure on the halibut QS market. An RQE will need to determine what is the most cost-effective use of its funds. Purchasing halibut QS would have a more immediate and direct effect on the

charter management measures. Even small purchases of QS could have an impact on management measures. Depending on the funding level, an RQE may not reach a point where purchasing CHPs would provide any control over latent effort. However, depending on future effort and halibut biomass, the ability to purchase CHPs could provide a tool to have more control over long-term effort.

### **What are the policy implications?**

When this issue was previously raised at the Council (NPFMC 2015; 2016), some stakeholders voiced a philosophical objection to the RQE's involvement with restricting halibut charter trip supply. The issue, as stated, is that the RQE is a non-profit that would be established to support increased angler opportunity. Depending on how it is funded, this additional fishing opportunity may even directly or indirectly be funded from anglers. Thus, a policy discussion was raised about whether it is appropriate for this entity (or these funds) to be used to limit the supply of angling opportunities by limiting CHPs.

The Northern Pacific Halibut Act of 1982 (the Act), which governs fisheries for Pacific halibut speaks to allocation of fishing privileges and distribution of those privileges. The Act states:

*If it becomes necessary to allocate or assign halibut fishing privileges among various United States fishermen, such allocation shall be fair and equitable to all such fishermen, based upon the rights and obligations in existing Federal law, reasonably calculated to promote conservation, and carried out in such manner that no particular individual, corporation, or other entity acquires an excessive share of the halibut fishing privileges...*

An "excessive share" is not defined in the Act. Moreover, there are use caps in other fisheries that allow up to 30% of privileges to be held by one entity (for example, processing quota share use caps in the crab rationalization crab fishery). However, the Council will need to consider if 30% is an appropriate cap for the RQE. While all other entities and individuals are capped at five CHPs (with some exceptions), an RQE could hold up to 22 times this amount in Area 2C. This action may require a consideration of the balance between what constitutes "excessive share" and what allows an RQE to be effective at influencing management measures and protecting the sector from sudden increase in active CHPs.

## **4 Next Steps**

The next step is for stakeholders and the Council to identify if there is a problem here. If the Council believes there is a need for action, it could clarify its intent through a purpose and need statement and establish a set of alternatives. Based on National Environmental Policy Act (NEPA) guidance, a purpose and need should be able to:

- 1) *identify the undesirable conditions,*
- 2) *link the conditions to agency guidance (law, regulations, agency policy, etc.),*
- 3) *frame the initial goals as clearly as possible, with reference to the resources conditions expected to exist at a future date,*
- 4) *rework the goals into measurable objectives, and*
- 5) *set a target goal or threshold value for successfully achieving each objective.*

Thus, when preparing a purpose and need, it is important for the Council and stakeholders to consider the goal of the action, including what the fishery would look like if those goals were accomplished. For instance, is the objective to control effort? To stabilize management measures? To add more flexibility to management measures? This intent will serve as guidance for any subsequent analysis. Any alternatives that are generated should flow directly from the specified purpose and need (Freeman 2010).

The Council may choose to consider this action in conjunction with the alternatives presented in the latency discussion paper (NPFMC 2017) under the same purpose and need statement, or continue with this action separately. While the implications of these actions could be different, they may be working towards a common goal. This will depend on how the Council chooses to craft a purpose and need statement.

## 5 References

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