

HB 141

Duncan Fields' Testimony

January 17, 2011

Mr. Chairman, Fishery Committee Members

My name is Duncan Fields. I'm a consultant to several CQE communities on Kodiak Island and have worked on the structure and development of the Community Quota Entity program for almost 15 years. I've been involved in fisheries all my life. I currently serve as one of the State of Alaska's representatives on the North Pacific Fisheries Management Council. I was chairman of the Alaska Fisheries Marketing Board and a former Alaska Seafood Marketing Institute board member. Serve on the executive committee of United Fishermen of Alaska and manage a family salmon fishing operation. In other words, I'm both an active fisherman and a fisheries advocate.

I would like to first thank Representative Austerman for introducing HB 141. Discussions regarding funding for CQE's have been ongoing since the program was created in 2004 and many communities talked with Alan in his capacity as Governor's fisheries advisor as well as legislator regarding their concerns. Alan is experientially aware of the limited funding options available to CQE communities and has submitted HB 141 as the best solution to meet significant funding limitations. I trust the committee will appreciate that this bill represents several years of work regarding alternative funding for CQE purchases and the realization that a dedicated State loan program may be our only hope.

Why Community Quota Entities (CQEs)?

Limitation of State fishing licenses starting in 1973 combined with the Halibut and Sablefish IFQ program implemented in 1995 resulted in significant and accelerated loss of fishing licenses and quota shares for smaller Gulf of Alaska fishery dependent communities. For many of these communities fishing is their only economic activity. With the loss of community based permits and quota shares, families, especially young families, started leaving. Population losses initiated a downward spiral of revenue loss, essential services limitation, school teacher and school activity reductions, increased costs, expanding social issues and yet further population declines. Many of these communities have inherent social and cultural

value and are important to Alaska's overall economic health. These communities need revitalization and one approach to stabilizing the communities' economic base was to allow the community to purchase fishing quota and licenses that would then be held in trust for the community residents in perpetuity. Many community residents believe that if fishing opportunities are available, young families are more likely to remain in the community. This is the fundamental concept behind the Community Quota Entity program; the community is given the opportunity to enter the market place and purchase and hold quota shares that are then fished annually by community residents.

What is a Community Quota Entity?

It's best to understand the Community Quota Entity program by contrasting it with the Community Quota Development Program. These two acronyms sound the same but represent very different programs. First, there is no allocation of fishing quota to CQE communities. In contrast, the CDQ program enjoys an annual allocation of quota that generates substantial revenue each year. Secondly, there are no requirements that CDQ quota be fished by community residents. The basic purpose of the CQE program is to have quota fished by resident community members. CDQs are not limited in the amount of quota they can purchase and can expand freely both in and out of the fishing industry. CQEs are significantly limited both in the type of quota that can be acquired and the amount of quota that each community can purchase. In addition community residents are limited in the amount of CQE quota each individual can fish as well as the amount of quota fished on an individual vessel. In summary, and in contrast to the CDQ program, there is no annual revenue source for the CQEs and they are significantly limited in how much quota they can purchase.

When Will the CQE Program Be Successful?

Currently about half of the CQE eligible communities have formed CQEs. To form a CQE the community must come together and create a new entity. The CQE is not tribal, it is not part of the village or regional ANILCSA entity and it is not formed by the city or borough, should one exist. In short, the CQE represents all the residents of smaller fishing communities, both native and non-native. The CQEs are structured so that any resident may participate in the program. Once the community entity is formed, the CQE must adopt guidelines for distribution of quota. These guidelines might include criteria such as how many resident crewmen will be employed, how much existing quota do you have, what is your

fishing plan, experience age etc. Many CQE's favor younger community members who will be fishing in skiffs or smaller vessels. Once the distribution plan is adopted the CQE is ready to enter the IFQ market and acquire quota. When the regulatory process to form CQEs was started, halibut IFQs in Area 3-A were around \$7.00 per pound. Now the same IFQs sell for about \$30.00 per pound. CQEs quickly realized that they had funding issues. CQE's didn't have assets or income from other sources to put toward the down payment and with the ratio between exvessel value and quota purchase costs so high, the CQE would need a much longer time period to repay loans. In short, the reason that only one of 42, soon to be 45, CQEs has purchased quota is that they have not had to access capital for quota purchases.

Where can the CQEs go for funding?

The Gulf of Alaska Coastal Communities Coalition, Sea Grant and other entities initiated two conferences to help CQEs organize and find funding. Traditional lenders, NGOs, corporate representatives and the State attended these events. Conventional lenders were not interested in CQE loans. As one banker said, a borrower needs the 4 C's: Collateral, Capacity, Credit and Capital. CQE's lacked all four. NGO's had some funding available but it still required startup capital and the funding was limited to a 5 year term. The State quickly qualified CQEs for their existing loan programs but the terms of the program, at that time 40% down and 15 years, didn't work for the CQE's. Recently, as you may know, the State has modified its permit loan program to 20% down and 20 years. Although comes closer to what is needed for quota share purchases, it still doesn't pencil for the CQE communities (examples provided). Remember, other borrowers can bring fishing revenue or income from other assets to pay the down payment or meet debt service. However, the CQE does not have other revenue streams. Tribal funding sources are limited to programs that are tribe specific and the CQE is community based --- native and non-native alike. Finally, the ANCSA corporations were quickly advised that funding CQE could be viewed as a disproportionate distribution of dividends. Over the past 6 years CQE representatives have had numerous meetings trying to obtain funding and have not been successful to date. It appears that a State loan program may be the only answer.

How will a State loan program like HB 141 help fund CQE quota share Purchases?

CQE's are not like individuals and consequently State of Alaska loans need to be structured to recognize the CQEs uniqueness. CQEs view quota shares differently from individuals. When the quota is purchased, it is likely to remain in the community and be fished by community members for the foreseeable future. Consequently, conventional loan terms of 15 or 20 years don't make sense for the CQE. HB 141 extends the loan term to 25 years. I would like to committee to also consider a 30 year term to further smooth debt repayment. Remember, we're not talking about the career or earning curve of an individual but the long term use of quota in the community. As mentioned previously, CQEs don't have start up capital for down payments and don't have alternative revenue sources to "bring to the table". Consequently, a CQE loan program must have low initial capital requirements. HB 141 provides for a 5% initial down payment with a 95% debt to equity ratio. Although this may still be a barrier for some CQE's, the 5% down provision makes program participation much more likely.

HB 141 provides the conventional "prime plus 2%" interest rate used in existing State quota share loan programs. The committee may want to consider the "prime" or a "prime plus 1%" interest rate used by the State in other loan programs that encourage economic development. A slightly lower interest rate would further incentivize CQE participation. Finally, CQEs borrowing money from the State must have the opportunity to build up some reserves so that annual quota fluctuations (recently a reduction of 28% in area 3A) don't interrupt revenue flow to the extent that the CQE can't make its payments. HB 141's suspension of interest payments for up to 10 years provides the time needed for the CQE to build reserves. In summary, HB 141 is carefully crafted to meet the specific and unique financing needs of the CQEs.

Who will oppose a State of Alaska loan program specific to CQEs?

Opposition to the CQE program has always come from individuals or fishing organizations that don't want competition for the purchase of fishing quota shares. They believe that CQE's will "drive the price of quota shares up" and their personal economic interests will be harmed. Those fears have not been realized and it is unlikely that the loan program proposed in HB 141 will substantially impact the quota share market. Let me give some perspective. If each CQE community qualified for the maximum loan amount under HB 141 of \$1,000,000, they could each buy approximately 30,000# of quota or

cumulatively about 1.3 million pounds of quota. This is less than 5% of the quota held by individual in areas 2C, 3A and 3B and far less than the 21% authorized by the NPFMC when creating the CQE program. In addition, 30,000# of quota is only about 20% of what the CQE's individual community limit of approximately 150,000#. In other words, the CQE loan program may have some impact in the market place but it is highly, unlikely because of substantial regulatory limitations, that the impact would be significant.

Other fishermen may argue that it is inequitable for communities to have loan opportunities that individuals don't have. The CQE program was created to address economic development and revitalization needs in communities and to mitigate adverse economic community impacts from regulatory fishery management changes. The CQEs are purchasing quota for use by a defined set of individuals residing in rural Alaska communities. Any suggested inequities created by the loan program need to be seen in light of the historical inequities experienced by Alaska communities when the IFQ halibut and Sablefish management program was put in place.

In closing let me say that HB 141 is a carefully crafted piece of legislation to meet a significant and real need by 45 smaller, isolated, fishery dependant, Alaska communities. It will not solve all community issues nor will it solve all the challenges the CQEs face. Nevertheless, it will go a long way toward creating a positive partnership between the State of Alaska and fishery dependent communities to provide jobs and economic opportunity. The State's investment is the CQE program is likely to pay significant dividends over time --- both in loan repayment and community health.