

EXECUTIVE COUNCIL

RESTRICTED

Title of Report: *Illex* Fees 2010
Paper No: 245/09
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Report of: Director of Natural Resources

1.0 Purpose

This paper sets out proposals for *Illex* fees for 2010, including options for significant changes to fee levels and payment schedules.

2.0 Recommendations

That Executive Council be advised to recommend that:

- (a) A clear refund policy be set out based on catch achieved (4.9(a)(i)), and if the policy is invoked that authority for implementing the refund policy be delegated to the Director of Natural Resources in consultation with the Director of Corporate Resources.
- (b) The Taiwanese proposal be accepted as the basis for the refund policy (4.9(a)(ii)), but that this be adjusted so that refunds will only apply if catches are less than 1500mt per vessel.
- (c) The *Illex* season be split into three periods as per the Korean proposal with the total fee split across the three periods in the proportion of 5%, 80%, 15% respectively. (The minimum proportion to be purchased is 80% (4.9(b))).
- (d) Fee payments to be made at least 15 days in advance of the fishing period starting, although a discount to be available for early payment and this discount could be revised to encourage earlier payment (4.9(c)).
- (e) The fee structure and formula remain the same as 2009, but that the second and higher cost formula for new applicants be discontinued (4.9(d)).

- (f) One to two exploratory licences be issued if necessary for the first fishing period (and possibly the last period) if necessary to establish that *Illex* are present in the zone (4.9e).

3.0 Summary of Financial Implications

The financial impact of the changes proposed is uncertain and this is considered fuller in section 5.

4.0 Background

- 4.1 Access fees for the fishery generally for 2010 are to be set in December, however it is useful if *Illex* licence fees can be set earlier. *Illex* is the one main fishery not involved in the Individual Transferable Quota (ITQ) system, and it is helpful to give potential licence customers more time to consider their options. In addition to considering fee levels there are a number of related issues to consider. The 2009 *Illex* season was a complete failure with only about 3 tonnes being caught by jiggers, compared to a 5 year average annual catch of 72000 tonnes. As a consequence *Illex* fees were refunded in their entirety in 2009.
- 4.2 The poor 2009 season is likely to have exacerbated financial problems besetting the industry and reduced confidence. Licence numbers have been declining for some time:

Year	2002	2003	2004	2005	2006	2007	2008	2009
Licences	125	122	89	70	43	57	44	47 *

* In 2009, 25 vessels either paid licence fees in full or had their fees guaranteed by letter of credit or by a third party. 4 vessels had 10% deposits paid, and 18 vessels had paid nothing. There are two aspects to the decline in licence numbers. It is partly due to a reduction in fleet size by traditional (Korea, Japan) licence customers. The Japanese fleet which used to take up 60+ licences no longer exists. There may still be a handful of jiggers (< 5), but they no longer fish in the Southwest Atlantic. The Korean fleet which also numbered 60+ vessels is down to just over 30 vessels. In terms of traditional customers, the numbers simply aren't there any more. The Taiwanese fleet supposedly has 90-120 vessels, however they are much more 'selective' about whether they take FI licences. They are more likely to see what fishing conditions look like before paying for any licence. The Chinese fleet is believed to be substantial and whilst records show they took 25 licences in 2002, they have only taken up 5 licences or less in the last 5 years.

There were no Chinese customers in 2008 or 2009 and some industry sources claim that the Chinese government has instructed Chinese boatowners not to take FI licences, although this has seemingly been denied by the Chinese Government. Whatever the truth there was no take-up of licences by Chinese vessels in '08/09.

- 4.3** The other aspect of the reducing take-up of licences is the difficulty some boatowners have in paying or guaranteeing payments. In 2009 about half those applying for licences failed to come up with the full fee; some only paying the deposit. Had the season been 'normal' it is uncertain whether these vessels would have paid up. A number of Korean vessels have had their fees guaranteed by a couple of reefer companies, and one of those appears to have gone out of business.
- 4.4** *Illex* fees are typically of the order of £90-100K per vessel, including discounts of up to 20% for vessel history (loyalty) and early payments. If it is assumed that whole *Illex* (green weight) sell for \$700/tonne, and at an exchange rate of \$1.6 per GBP (£), then on a licence fee of £90K, the target fee/revenue ratio of 10% implies a catch per vessel of c. 2000 tonnes. This sort of catch was achieved in 2006-2008, and was well exceeded in 2007. The evidence of 2009 shows that around half the customers had little difficulty paying, whilst a fair number of the remainder were likely to have some difficulty. *Illex* fees are probably at the high end of what the market will stand. Whilst a target licence fee of 10% is what has guided FIG fee levels, for *Illex* in particular, this has limited applicability to the value of a licence. In round terms if the cost of a FI licence equates to 200 tonnes of *Illex*, then a FI licence is of value if the catch per vessel in FI zones is 200 tonnes better than remaining on the high seas. The greater the positive disparity the better the value.
- 4.5** The '*Illex* industry' has been consulted on this issue. The number of companies involved with *Illex* is low and locally includes Fortuna Ltd., Seafish (Falklands) Ltd., and JK (Marine) Ltd. The responses received represent a combination of views from the local industry, Korea and Taiwan. The Korean fisheries association also responded directly. In undertaking the consultation it was suggested that there were 3 obvious options to consider:

a) Clear Refund Policy:

A clear statement on refund policy in the event the fishery fails. FIG's stated position has usually been that it will be the ultimate arbiter on refunds.

The industry sees this as high risk as they could pay the c. £90K licence fee, not catch much and not necessarily get any refund. Whilst some full refunds have been given, there have also been refunds at levels which the industry has viewed as insufficient. Hence, having no clear refund policy results in a high risk for the industry.

b) Access fees based on catch:

This would entail a variable fee based on actual catches. It could be extended to include real sales value information although that might be a step too far. Sales data is likely to take a long time to collect and verification would be a problem. In limiting the scheme to catch, the actual catches would need to be verified possibly involving verification at FIPASS. There would also be problems in guaranteeing or paying uncertain fees. The flow of information from jigger owners in relation to catches is limited, and is unlikely to be reliable for price information.

c) Access fee based on fishing time:

This would divide the season into periods with a proportion of the full fee for each period. Boatowners might have to purchase a minimum of 70% of the full season. In essence this provides an option for reduced fees. Customers could apply for 70-100% of the season.

4.6 The consultation document made it clear that for FIG there were two key aspects of any modified system. Firstly, any system had to be capable of being monitored if it was based on catch. Secondly, licence fees had to be guaranteed.

4.7 The feedback included:

- Clear Refund Policy: Universal support for this. At least one respondent suggested the refund should kick in for any catch less than 2000mt. Whilst this seems high compared to decisions on refund levels taken previously it does fit with the fee/revenue calculation set out in 4.4.
- Some support for access fees based on fishing time, with payment being made throughout the season.
- Reduce fees by 20-30%.
- Licence more than 8 vessels per day (this limit is imposed to undertake safety inspections).

- Close season early if no squid (this relates to the refund policy in that in 2009 the season stayed open to see if there was a late season. Some boatowners felt compelled to stay in the fishery as in some years refunds have not been given to vessels which had already left).
- Reduce Medical/Harbour/Licence fees.
- Free berthing for jiggers transshipping at FIPASS.
- Make progress towards a two tier structure with old style licences and new style ITQ.

4.8 The conclusion from the feedback is that in terms of improving conditions for customers for 2010, and with limited downside for FIG, the least which should be done is to set out a clear policy on refunds. Other measures can also be implemented to address customer concerns, although impact on revenue is more difficult to gauge. Additional measures which effectively reduce fees and make payment terms easier should encourage more customers. That may be proven in due course if implemented; on the other hand if the number of customers remains static or declines, it will be difficult to know whether the numbers would have been the same on the previous higher licence fee. It is also difficult to predict whether lower fees and easier payment terms will generate sufficient new interest to compensate for the lower fees. Once fees are reduced it is quite difficult to raise them again. Equally, the trend on licence numbers and revenues suggests some change is worth trying.

4.9 The range of possible options for 2010 include the following:

- a) Clear Refund Policy:
 - i) A clear refund policy will be set out based on catch achieved in the season. This will require some monitoring through catch reporting, observers, inspections and possibly some additional measures. The average catch per vessel is likely to have to be assessed on a fleet basis rather than an individual vessel basis, and FIG's assessment is likely to have to be final.
 - ii) The relationship between refunds and catch could be based on the Taiwanese proposal:

FI Catch	Refund
> 2000mt	No refund
2000 - 1750mt	5%
1750 - 1500mt	10%
1500 - 1250mt	20%
1250 - 1000mt	30%
1000 - 750mt	40%
750 - 500mt	50%
500 - 250mt	70%
< 250mt	90%

In some respects starting at a catch of 2000mt to trigger refunds seems quite high. However, as indicated at a price of \$700/mt, the fee/revenue target of 10% requires a catch of c. 2000mt, so it is consistent with that. If the catch is less than 2000mt the fee/revenue ratio for a set selling price will increase. That calculation could also be used to set refunds. However, at \$700-\$800 per tonne and if applied for any catch less than 2000 tonnes, the schedule set out above is preferable from FIG's viewpoint than the fee/revenue option (Fig 1). For comparison average catch per vessel in the last 3 'normal' years were:

Year	2006	2007	2008
Catch (mt)	1931	2763	2388

Statistics going back further would show that refunds would arise in a number of years.

- iii) The policy could include a statement that vessels 'giving up' and leaving the fishery due to unprofitable catches would be entitled to any refund subsequently declared.

iv) It is proposed that the Taiwanese proposal be modified so that refunds will only be applied if catches are less than 1500 tonnes per vessel on average. This potentially raises the fee/revenue ratio to 12% in place of the target of 10% which does not seem excessive. The refund schedule will need to be adjusted to take account of this.

b) Split the season into periods:

This essentially offers a reduction in fees. Customers select and pay for the period in which they think they will operate profitably. It reduces overall expense and may facilitate payment. If it increases licence take-up, revenue to FIG may be maintained or improved. If take-up is static then revenue declines, if customers opt for a proportion of the full season. This option was included in the consultation document and it was envisaged that the season might be divided into 10-15 day periods. The rules might have been that periods selected had to be continuous and a minimum of 70% of the full season purchased. The fee per period might have been weighted according to likely catch. The Koreans have proposed splitting the season into:

15 February – 15 March	15% fee
16 March – 15 May	70% fee
16 May – 15 June	15% fee

This may be simpler although ‘analysis’ of catches suggest the split of fees should be 5/80/15% respectively for the 3 periods. If implemented it is likely that most vessels will opt for the middle period (80% would be the minimum allowed), which could result in a 20% drop in fees if licence take-up is limited to this period.

c) Fee Payments:

The Koreans suggest that fees should be guaranteed 15 days in advance of any period. This spreads out expenditure to some minor extent. This could also be agreed although it would still be over-laid with the early payment discount, which might require some revision. Deadlines for payment of fees have been set, however if there are late applications they are accepted. There is some risk that if the deadline is set close to the season, and the high seas fishery is experiencing good results that FI licences will not be taken or paid for. The early payment discount might overcome some of this.

d) Fee Structure:

It is proposed that the fee structure remain the same as at present; a formula based on vessel size and number of jigging lines. In the past 2 formulas have been used; one for vessels with recent involvement in the fishery and one for newcomers. The disparity between the formulas used to be 20% in favour of recent participants, but that was reduced to 5% for 2009. The rationale for the reduction was that previous participants also get a 'loyalty discount' of 1% per year up to 10 years in the fishery, and that if the aim is to encourage new participants the disparity was a deterrent. As licence numbers have dwindled encouraging what are likely to be newcomers is becoming the bigger game. It is therefore proposed to use the lower fee formula for all applicants.

e) Exploratory Licences:

If the proposal on fishing periods set out at 4.9b) is adopted it is quite possible that no one will take the initial period, albeit that it only incurs 5% of the licence fee. One or two exploratory licences may have to be issued at no cost for brief periods to allow operators to establish whether it is worth purchasing this initial period. Whilst the exploratory periods would have to be at nil cost they could potentially generate some scientific information.

5.0 Financial Implications

5.1 Whilst largely a financial issue any estimate of financial consequences is likely to be quite speculative and of dubious utility. The revised fisheries revenue estimate for '09/10 anticipates c. £4 million of *Illex* revenue or c. 44 licences. If the changes outlined above are implemented and if the take-up of licences remains unchanged, but customers opt for the middle period only, thereby paying 80% of the full fee, then revenue would fall to £3.2 million. However, it could equally be argued that current arrangements aren't viewed favourably by a number of licence customers, so maintaining the status quo could also lead to reduced revenue. The point of the changes is to encourage licence take-up so increased revenue could also be an argument, although the proof will be seen in due course if implemented.

5.2 If these proposals are adopted then as set out above the most likely outcome is that customers dispense with the first (5% of current fee) or last (15% of current fee) periods. A total reduction of 20% on current fees might be a reasonable estimate of the decline if no action is taken.

If the changes generate additional interest in licences then increases of the order of 10-30% at 80% (minimum middle period) or 100% of current fees (full season) might be realistic. Using the current budget estimate based on 44 licences the following fee scenarios are forecast:

Potential Licence Fees (£millions)

Periods (% of current fees)

Licences	2 (80%)	2+1 (85%)	2+3 (95%)	1+2+3 (100%)
- 30%	2.24	2.38	2.66	2.8
- 20%	2.56	2.72	3.04	3.2
- 10%	2.88	3.06	3.42	3.6
Current 44	3.2	3.40	3.80	4.0
+ 10%	3.52	3.74	4.18	4.4
+ 20%	3.84	4.08	4.56	4.80
+ 30%	4.16	4.42	4.94	5.20

6.0 Legal Implications

There is no particular legal impediment. The refund policy could be stated as a policy it need not be the subject of regulations, although the decision to refund does currently require an ExCo decision. The ability for officers to implement the refund policy should ideally be sanctioned during consideration of this paper. Deferring the decision to a point at the future creates some of the delay and difficulties which licence customers are arguing against. The splitting of the *Illex* season and fee arrangements should ideally be the subject of regulations.

7.0 Human Resources

None.

8.0 CMT

An earlier version of this paper was considered by the Corporate Management Team in early October. The recommendations were generally supported.

Fig 1.

