TE OHU
KAIMOANA

MĀORI FISHERIES TRUST

Undue Adverse Effects on Fishing

Regulations under section 186ZR of the Fisheries Amendment Act

28 September 2011

Introduction

1. Te Ohu Kaimoana welcomes the opportunity to comment on the Ministry of Fisheries' consultation documents on regulations to support the new arbitration provisions that relate to aquaculture and fishing. Our submission does not remove the responsibility for MFish to consult with Iwi and other stakeholders in the appropriate manner. Nor does it seek to undermine any submission that you may receive from individual iwi or iwi collectives.

2. This new arbitration provision represents a significant change in that it is very unusual for Parliament to provide a mechanism where one group of existing private right holders can be displaced by another private party without the first party's agreement. The use of this mechanism should be used sparingly so as to continue to provide strong incentives for quota owners to invest in fishing. Our comments and recommendations are set out below.

Who are we?

3. Te Ohu Kai Moana Trustee Limited (Te Ohu) is the corporate trustee of both the Te Ohu Kai Moana Trust and the Takutai Trust.

4. Te Ohu Kai Moana Trust was established under s.31 of the Maori Fisheries Act 2004 and has a key role in the Maori Fisheries Settlement. The purpose of Te Ohu Kai Moana Trust is to advance the interests of iwi individually and collectively, primarily in the development of fisheries, fishing, and fisheries-related activities, in order to:

   - ultimately benefit the members of iwi and Māori generally
   - further the agreements made in the Deed of Settlement and to assist the Crown to discharge its obligations under the Deed of Settlement and the Treaty of Waitangi
   - contribute to the achievement of an enduring settlement of the claims and grievances referred to in the Deed of Settlement.

5. In carrying out its role, Te Ohu works actively with iwi organisations who have received, or who will receive settlement assets under both the Aquaculture and Fisheries Settlements. We also work actively with the wider seafood industry (both fisheries and aquaculture) and participate in industry organisations to protect the interests of iwi and Māori as the beneficiaries of the settlements.

6. The Takutai Trust was established through the Māori Commercial Aquaculture Claims Settlement Act 2004 (the Aquaculture Settlement Act)[1]. The Aquaculture Settlement Act provides a full and final settlement of Māori commercial aquaculture interests since 21 September 1992 and provides for iwi to receive assets equivalent to 20% of the water space rights created in coastal waters between September 1992 and January 2005, and 20% of any new space approved after the commencement of the Aquaculture reforms on 1 January 2005.

7. The purpose of the Takutai Trust is to:

   (a) receive settlement assets from the Crown or regional councils;

[1] Aquaculture Settlement Act, s 34

(b) hold and maintain settlement assets on trust until they are transferred to Iwi Aquaculture Organisations (IAOs);

(c) allocate settlement assets to iwi on the basis of a model set out in the Aquaculture Settlement Act; and

(d) facilitate steps by iwi to meet the requirements for the allocation of settlement assets[2].

8. As trustee of both the Fisheries and Aquaculture Settlements with each affected by the UAE decisions - Te Ohu wishes to see clear mechanisms that provide incentives for all parties to work constructively to reach mutually agreed solutions. Where that is not possible and the arbitration mechanisms are invoked, the process must treat each party with respect and provide for aquaculture where the circumstances clearly justify it while providing full compensation to quota owners.

Background

9. The development of marine farms can impact on existing fishing rights. It has long been recognised that if there is to be investment in fishing, then such rights cannot be arbitrarily displaced[3]. For at least 40 years there has been some form of Undue Adverse Effects (UAE) test that assesses the extent to which aquaculture has an impact on fishing, and sets out various decisions based on the level of impact. The test recognises that aquaculture established at a location could displace some fishing and that in some circumstances, the effect of that displacement may be "undue".

10. As the decision creates 'winners' and 'losers', the test has often been contentious and the subject of litigation.

11. The way the test has operated under previous legislation has been:
    - if the impact of the aquaculture proposal does not go beyond the threshold of a UAE, aquaculture is allowed and quota owners (and fishers) were not compensated; but
    - if the impact does exceed the threshold, a reservation was placed on the area and aquaculture cannot proceed unless agreement was reached with the quota owners.

12. Prior to the latest reforms, the agreement of the owners of 90% of quota shares was required in order for aquaculture to proceed despite a UAE. The recent legislative reforms have reduced the level of agreement required from quota owners to 75% but with measures to ensure that quota share owners who did not agree are treated (including compensation) in the same way as the quota owners of the 75% of shares that did agree.

13. The new regime goes further, however, and addresses Government concerns that – in some cases - where a UAE is determined, but agreement is not reached between quota holders and the aquaculture developer, 'New Zealand Inc' will miss out on the materially

[2] Aquaculture Settlement Act, s.35

[3] While the regime for assessing the effect of proposed aquaculture activities on fishing also applies to customary and recreational fishing,changes made in the new regime apply only to commercial fishing and the views expressed in this submission deal only with effects on such fishing.

greater value that aquaculture could produce from the space in question than fishing in the same area.

14. To address this, the legislation now provides that, in these circumstances, the aquaculture applicant/developer can seek to have the appropriate level of compensation payable to quota owners determined through arbitration that is binding on quota owners.

15. There will be two steps to the arbitration process. First, the arbitrator must determine that the proposed aquaculture activities would have a materially greater economic value than the fishing activities they would displace. Only if that question is answered in the affirmative does the second step in the arbitration process occur, in which the arbitrator will determine the level of compensation that must be paid to quota owners to mitigate the impacts of the aquaculture proposal, over and above the UAE threshold.

16. This compensation is to recognise and mitigate the losses in quota value arising from any reduction in economic returns to quota owners if aquaculture uses the area involved. Those losses may be direct, where the removal of an area from fishing results in a reduction in catch, or may be indirect, where the same catch is possible but the location and intensity of catching must change and this causes increased costs for the same level of catch.

17. Once the arbitrator has determined the appropriate level of compensation payable, the aquaculture applicant can choose whether to pay that amount or not. If the applicant decides not to pay compensation (and, therefore not to proceed with the aquaculture proposal), the applicant is liable for the costs of the quota owners who participated in the process.

18. The statutory provisions on the UAE are to be implemented subject to additional regulations. The options for the content of those regulations are what are being consulted on.

Principles

19. In our view, the outcomes from these processes should be fair and equitable to both quota owners and aquaculture applicants. Iwi frequently have interests in both aquaculture and wild fisheries, and are the beneficiaries of settlement assets in both sectors. Iwi are therefore in a good position to determine a balanced solution and provide important feedback to questions currently being addressed by government.

20. Agreement between the parties is much more preferable and will be better tailored to suit the participants than any imposed solution. Ideally agreement between quota holders and an aquaculture developer would be reached early in the development process (although it can still be reached at any point in the process). Thus the arbitration option should operate as a back-stop that is only used in limited circumstances.

21. The regulations (and processes followed by any arbitrator) should provide incentives for affected parties to agree to solutions themselves rather than go to arbitration – and to agree during that process even if that agreement is only reached late in the process.

22. Where decisions on fairness and equity arise the compensation outcome should be biased in favour of quota owners. This reflects the fact that the arbitration process is an extra–ordinary mechanism that can force quota owners to change their businesses. The arbitration binds quota owners while aquaculture proponents who instigate the process can choose whether to proceed or not once a determination has been made by an arbitrator. If there is a small margin of bias to quota owners, this should also enhance

the likelihood of negotiated solutions and early agreement, enabling an earlier development of the aquaculture venture – a positive outcome for the applicants who could otherwise face costly and lengthy protracted processes.

The relative value of aquaculture and fisheries

23. The statute requires that regulations are developed for the arbitrator for the following (s186ZP)

> “(1) Before determining the compensation to be provided to quota owners or a class of quota owners, an arbitrator must first determine the question in subsection (2).
>
> “(2) The question is: which of the following is of ***materially greater economic value to New Zealand***[4]:
>
> (a) the proposed aquaculture activities; or
> (b) the fishing in relation to which the chief executive has made a reservation.
>
> “(3) The arbitrator must determine the question on the basis of data and analysis provided by—
>
> (a) the holder of the coastal permit; and
> (b) the quota owners concerned.

24. The regulations to be developed in respect of this section are to prescribe a methodology for determining the question in section 186ZP(2) that sets out the type of data and analysis required for that determination.

25. The Ministry’s document sets out options for developing regulations that are fixed, semi-flexible or fully flexible. In our view, key questions that need to be addressed are:
    - What is the scope of matters that need to be considered in valuing each activity?
    - On what basis should comparisons be made?
    - At what point can it be demonstrated that the value of aquaculture is materially greater than that of fishing?
    - Are there different circumstances in which a mix of approaches is warranted?

    We provide comment on each of these questions below.

Enable broad scope to be applied to assessing value to New Zealand

26. The basis for this new compulsory arbitration mechanism to be used is that aquaculture in an area will provide materially greater economic value to New Zealand. It is important that the methodology assesses this preliminary question fully. In determining the relative value to New Zealand, it is not sufficient to only consider the relative value of fishing to the quota owners involved, compared to that of aquaculture space to a marine farming applicant. The broader economic contexts must be considered for each – but this will not necessarily require complex modelling in every case.

27. There are a number of questions that relate to the fish stocks that will no longer be able to be fished in the area concerned – bearing in mind that some will have triggered the UAE threshold, but that other stocks caught alongside them may not have done so. How

[4] Emphasis added

should "fishing of any fishery", as is considered when undertaking the UAE, be interpreted when assessing relative value:

- on a stock by stock basis?
- on the collective of stocks fished in that area?
- on the mix of species that are caught as part of the harvest of the reserved species. For example the reserved fish stock may be one of a number of fish stocks that might be caught using a trawl –even though the Ministry has judged those some of those stocks are not sufficiently affected to have gone beyond the threshold to require a reservation?

28. In our view, all relevant fisheries affected by the proposed development (including those that are caught in association with reserved stocks) should be considered in determining relativity. It is this full range of fishing activity that will be displaced by an aquaculture proposal. That said, it needs to be made clear that this does not infer that all those stocks will be relevant to the determination of compensation.

Provide a clear threshold for identifying materiality

29. The value of aquaculture must be materially greater than that of fishing if the arbitrator is to determine compensation. This raises a number of questions:
    - should the arbitrator be given a relative value over which materiality is defined?
    - what should that be?
    - should there also be a substantive threshold?

30. You would not expect this extraordinary binding arbitration to be used if the difference between two activities in overall dollar values is small, ie there is NOT a material difference. What would be an appropriate threshold to be material? Based on the intrusion into existing businesses that have legitimately invested and the examples provided in the consultation documents we suggest a relative value of at least a factor of five would be needed to demonstrate materiality; and unless the dollar value assessment suggests the value of aquaculture will be at least $500,000 greater, then the arbitration provision should not be triggered.

Compare "apples with apples"

31. In making comparisons of relative value it is essential that an equivalent approach is used for both quota and aquaculture. For any new aquaculture venture, its value must be determined from future projections. While current data on the value of fishing will be available, it is important to undertake an assessment that also represents the future value of that activity, on the same time scale as the projection used for aquaculture.

Fixed and flexible approaches can be used depending on the circumstances

32. The consultation documents discuss fixed, semi-flexible and fully-flexible methods of determination. As we understand it a fixed method would rely on existing data sets with essentially mechanical processing of information. A semi-flexible method would consider a wider range of data sets, with more discretion as to how they influence decision making. A fully-flexible method would allow wide discretion, including for instance receiving submissions from the parties. Again these raise various questions. In determining relative value, are there sufficient robust data sets to enable an effective fixed method? If not, would a semi-flexible method provide a workable solution? If a semi-flexible or fully-flexible method was used, would its strengths be outweighed by the time and cost involved?

33. We think it is worth exploring a mixed approach that might involve a series of thresholds for moving from a fixed to a more flexible approach, depending on the certainty associated with available information, and the proximity of the relative values involved.

34. A fixed method is less costly and quicker to implement, and its process less prone to judicial review. In cases where the data shows a large relative differential and where the materiality threshold is exceeded, the costs of a more flexible method would not be justified. However, if a relative value determined by fixed methods was close to the trigger value (such as five suggested above), say between two and ten, then the arbitrator could be given discretion to call for submissions from the parties.

35. The arbitrator (and the parties) should also access to independent information, such as from the Ministry, if they wish. In our view the Ministry should be able to provide material to the parties and to the arbitrator. Clearly this should include the analysis and decision on the UAE. However it could also include indicative modelling of likely aquaculture ventures and affected fisheries for different regions at both a simple level (direct asset values) and a complex level (including employment and other multiplier effects where these can easily be predicted). We would not expect that this could be meaningful if it was reduced to a simple on-line 'push the button' calculator but the work would inform both sectors of the industry. It could provide an indication of both the sensitivity of such modelling and some ability to judge in what circumstances it might be expected to be very clear-cut from both a simple and complex modelling viewpoint as to whether that type of aquaculture enterprise is likely to easily clear the thresholds set out above. Over time it might be possible to provide on-line open access models that participants from each sector could use with their own data to better inform their situation and this assist pro-active negotiation.

36. Where a fixed approach is to be taken, methods for determining market value of both quota and of aquaculture space would need to be determined. There are difficulties with data for both quota and aquaculture space. Though FishServe records quota sales and itself grooms data as part of its exercise in estimating the value of quota, the number of sales for many fish stocks is small and with the exclusions and thin markets, alternative cross-checks are required to develop robust values. Here the use of ACE prices (a thicker market) along with appropriate industry discounting factors could provide useful benchmarking. Correspondingly while there are a number of sales of aquaculture farms there is no register and no requirement to disclose the price. This led the Crown along with iwi to undertake a detailed valuation exercise to estimate the value of the Crown's pre-commencement space obligation to iwi. The final results of this exercise used a number of methods to arrive at robust values. Under the aquaculture reforms the settlement will be delivered to iwi through regional agreements – these agreements could provide authorisations for space or cash or other measures agreed between iwi and the Crown. For this to work the Crown (and iwi) will continue to need a valuation model for water space for different aquaculture ventures in different regions. This could provide values that the arbitrator could use. In all cases this will require the Ministry to work with iwi and the rest of industry – both fishing and aquaculture - to develop robust models.

37. The time-frame for considering values is also a key issue. Quota is held in perpetuity. Marine farming coastal permits have limited duration and some have staged development. The UAE, agreement and arbitration processes form a single process that is intended to identify and if necessary resolve any UAE on fishing. It is not repeated at the end of the period of the consent if a new consent is obtained for the same aquaculture activity. Over what period should the relative values be assessed?

38. If the direct simple comparison of asset values is used, it is unlikely that a time period need to be considered – these values set out in the current price seller and buyers perceptions of future value. If more complex analysis is used eg Net Present Value, based on a discounted cashflow approach we consider the timeframe for analysis should be the duration of the consent or 20 years, whichever is longer.

39. As noted in paragraph 26 above, it is not sufficient to only consider the relative value of the assets. While it is important that this simplistic analysis set out above is robust, a supplementary view of the merits that looks at the "relative value to New Zealand" needs to be included. Te Ohu Kaimoana considers that the use of the export price adjusted for industry average costs of harvest (and processing) and discounted as appropriate for each enterprise.

Determining compensation for loss of value of quota

40. The statute requires in section 186 ZR (3) that regulations are developed for: "a methodology for calculating the loss in value of affected quota due to the aquaculture activities authorised by a coastal permit", with that methodology to:

"(a) provide for compensation to be calculated in proportion to the impact on fishing, including—

"(i) increased fishing costs and any consequential disruption costs as a result of the proposed aquaculture activities, including a sum by way of solatium to fishing interests for any adjustments required as a result of the impact of the aquaculture activities; and

"(ii) any complementary uses that might exist for the site in accordance with any submissions made under section 186ZQ(2); and

"(iii) the loss in value of affected quota, but only in relation to that part of the relevant average annual catch that is estimated would be reduced if the proposed aquaculture activities were to proceed; and

"(b) provide for the calculation of compensation to be based on the size of the affected quota holding and the corresponding loss of quota value, including by reference to any recent transfers of the quota or associated annual catch entitlement."

41. We note that the legislation refers to "increased costs of fishing" and "disruption costs…". However we consider that the reference to "business costs" contained in the Ministry's material confuses the relationship between them. We think the most constructive way of approaching this process is to consider the following matters, including those referred to above:
    - The relationship between the UAE assessment and the arbitration process
    - The loss in value of affected quota (in relation to that part of the relevant annual average catch that could be reduced) (section 186ZR (3) (a) (iii))
    - The extent that the aquaculture proposal will result in increased fishing costs (section 186ZR (3) (a) (i))
    - The approach to establishing an appropriate solatium payment to acknowledge the costs of disruption as a result of the proposal (as distinct from increased fishing costs) (section 186ZR(3) (a) (i))
    - Any complementary uses (section 186ZR(3) (a) (ii)).

Clarify the relationship between the UAE assessment and the arbitration process

42. Compensation is for the effect on specific fish stocks where a UAE has already been determined. The regulations are to determine the amount of compensation to be provided in this instance. Though it appears clear from the law, for the absence of doubt and to minimise litigation on this point, we consider it would be sensible that the regulation provide that the arbitration process is bound by the UAE decision, that its substance cannot be re-litigated and that compensation is payable only in respect of the effects of the aquaculture activity in question over and above the UAE threshold and/or the effects of any pre-existing aquaculture.
43. With this mechanism now to be part of the process, it may also be necessary to ensure that the way UAE decisions are set out can assist both private parties in negotiation, and if necessary the arbitrator to reaching decisions. While outside the scope of these regulations, we would urge the Ministry to review its processes for implementing the UAE to ensure the way its decisions are reported can best assist the parties and any arbitrator. This should include quantification of the impact on quota owners beyond the UAE "threshold".

Ensure all relevant factors are able to be used to assess the loss in value of affected quota

44. A determination of market value for quota or aquaculture is an estimate of the capitalised stream of future income minus costs. There is some concern that robust data is not always available. In addition, quota in some circumstances can have enhanced or reduced value from associated factors which we consider should be included in the value of the quota.

45. The consultation papers propose a range of data sets to assess different factors. In our view, the method for valuation of quota needs to take all those factors into account, as would any robust market determination. How far a fixed or more flexible approach is required will depend largely on the availability of relevant data. As suggested earlier, it may be possible to structure a mixed approach that begins with a fixed method, but enables more flexibility to be applied depending on the availability of datasets and the robustness of the result. This suggests that a regulated fixed approach will not be suitable in all circumstances. A semi-flexible approach is needed. The arbitrator must be able to inquire directly themself or provide opportunity for the parties to present material along with reasoning on its appropriateness

Increased fishing costs

46. Increased fishing costs must be considered as part of the process of assessing the loss of quota value. These could vary widely and not easily be determined through a fixed method or prescriptive approach. The potential increase in costs will affect fishers in different ways. For instance those directly affected may have to find new areas to fish resulting in cumulative displacement that will affect all fishers. This will result in lower ACE prices. However the reduction in the ACE will be difficult to predict before it happens. For this reason it may be simpler to assume the affected quota will not be caught. Such an approach could be simpler – and also bias the outcome towards quota holders.

Solatium

47. Compensation can include "a sum by way of solatium to fishing interests for any adjustments required as a result of the impact of the aquaculture activities". This is an extra payment, in excess of the direct losses in quota value and increased fishing costs,

to compensate for the fact that, without having a choice, an unwanted change in the fishing business will have to be made. The consultation documents do not clearly distinguish between this and compensation for increased costs of fishing. It is essentially a payment for the unseen and indirect impacts on the business eg loss of opportunity, an 'acknowledgement' of the losses to other fishstocks that are a real result of the proposal but below the threshold as well as the "disruption and nuisance value" of having to participate in processes and make unwanted changes, irrespective of their direct costs.

48. Questions are raised as to whether a solatium payment should be made as of right, or whether there a need to determine it on a case by case basis. In addition, if a solatium is to be paid, should it be at a standard rate? For instance, should a percentage of the other compensation be the solatium value? If so, what is an appropriate percentage?

49. We consider a solatium payment should be made as of right and it should be fixed at 20% of the quota asset value loss compensation. We note that submissions from the parties would not be needed to determine a solatium if this fixed method is used.

Complementary uses

50. Compensation must consider "any complementary uses that might exist for the site".

51. Preferably, if there can be complementary use of a site which could minimise the impacts of the aquaculture proposal on fishing, that would be best agreed between the parties prior to the application for a coastal permit and/or in the assessment of the effects of the aquaculture proposal on fishing. Changes such as distance between lines could allow some fishing activities to continue in part or fully, and a consequent change to the detail of the consent application could be made.

52. However it is easily conceivable that in the early stages both the aquaculture applicant and quota owners would assert that there could be no meaningful joint use so as to maximise their own business opportunities. Nevertheless when faced with the reality that aquaculture may be established at the site but only if substantial compensation is paid then both parties may have different incentives and there might be accommodations able to be made to the detail of the aquaculture activity, with the marine farmer preferring to sacrifice some productivity for the sake of a lower cash compensation payment. It could also reflect in some cases partial use of the site where development is staged. Such changes could only occur if agreed mutually between the parties – it could not be imposed by the arbitrator, though they might facilitate such an agreement.

53. The implementation of this provision would result in an agreement between the two parties specific to complementary use. We believe the parties should submit their proposals for complementary use, and the extent to which it offsets the need for any other form of compensation. To work this must be a joint proposal of the parties. If there is variation between the parties on any points, the arbitrator could encourage a joint resolution but not impose it.

54. Should there be guidance on how to quantify the financial equivalent of the provision for complementary use, or should this be determined by the parties? In our view a template for agreements, which did not limit their scope but specified some required content, would be desirable.

Other matters

55. It is not clear whether compensation payment under these provisions would be treated as taxable or non-taxable income? The tax status of the compensation needs to be

properly allowed for in determining value of the compensation. For most iwi organisations tax may not be relevant factor.

56. The choices to be made in the development of the regulations are important if the final set of measures are to :
    - assist the achievement of the outcomes desired from the aquaculture reforms,
    - maintain incentives for investment in fisheries in New Zealand; as well as
    - provide incentives to promote direct negotiation between the parties and minimise the use of these regulatory measures to decide on allocation and compensation between the two sectors of the industry.

57. To achieve these outcomes Te Ohu Kaimoana recommends that the Ministry advance this work and circulate the set of regulations in draft form for comment by both sectors.

58. It is also clear that there will need to be more detailed consideration on the detail of how any compensation agreement will work between the parties. Fishing losses will start immediately that catching is precluded from an area and while the viability of aquaculture may be strong, every venture starts with high capital requirements - in many cases there is unlikely to be an ability for any significant immediate lump sum transfer of compensation by the aquaculture farmer. The Ministry may be able to assist both sectors explore useful models for transfer.

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