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Fishing for a fee: Resource rent taxation in Iceland's fisheries

Stefan B. Gunnlaugsson^{a,*}, Dadi Kristofersson^b, Sveinn Agnarsson^c^a Faculty of Business Administration, University of Akureyri, Iceland^b Faculty of Social Sciences, University of Iceland, Iceland^c Faculty of Business Administration, University of Iceland, Iceland

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ABSTRACT

In 1990, Iceland established a comprehensive fisheries management system based on individual transferable quotas (ITQs). Simultaneously, low-cost licence fees, which the fishing industry paid to the government, were introduced. As the ITQ system became more mature and the financial performance of the fisheries improved, there was increasing public demand for the sharing of its resource rent. A special resource committee was set up in 1998 to address these views and concluded that a new fishing fee should be established to cover the cost associated with managing and supervising the use of marine resources, as well as making certain that a visible share of the resource rent accrued to the public. Although the fishing fee has changed since its introduction in 2004, the basic principles behind the taxation remain the same. Five issues have made the introduction and implementation of the fishing fees difficult. The first regards the fee amount for different species. The second relates to the variance in profitability between harvesting companies. The third concerns measurement of revenue and profits from harvesting in vertically integrated firms. The fourth issue is related to how to deal with the debt burden that became quite large for many Icelandic harvesting firms after the financial crisis of 2008. Finally, obtaining reliable data has been a major challenge. This paper provides a background to the implementation of the Icelandic fishing fee, describes and investigates fishing fees issues and their address by the government. In 2014, the fee amounted to 52 million euros, 6.0% of the catch value of Icelandic fishing vessels and around 1.2% of the total revenue of the Icelandic Treasury.

1. Introduction

A large and growing literature shows that catch share management systems, or quota systems, have positively affected efficiency and profitability in fisheries in New Zealand (Deweese, 1989; Annala, 1996; Batstone and Sharp, 1999) Australia (Kompas and Che, 2005; Thebaud et al., 2014), Norway (Hannesson, 2013), Denmark (Andersen et al., 2010), Chile (Pena-Torres, 1997; Gómez-Lobo et al., 2011), USA (Matulich, 2008; Gauvin et al., 1994; Agar et al., 2014; Ropicki et al., 2018) and Canada (Gardner, 1989; Casey et al., 1995; Dupont, 2014). Introducing quotas ends the race to fish, leading to effort reductions and increases the efficiency of the fishing fleet (Dupont et al., 2002; Standal and Aarset, 2008; Asche et al., 2014; Grafton, 1996; Emery et al., 2015; Hannesson, 2013). The transfer of quotas, permitted under individual transferable quotas (ITQs), will—over time—move fishing rights from less profitable to more profitable firms, improving economic performance even more. Research also suggests that introducing quotas may increase catch value because fishers are no longer under pressure to maximise catches and can organise fishing to obtain the highest

value of their landings (Asche et al., 2008, 2009; Andersen et al., 2010).

Iceland was one of the first countries to implement a management system based on ITQs. Quotas were introduced into the pelagic fisheries in the 1970s and the most important demersal fisheries in 1984. Six years later the various quota systems were knitted together into a comprehensive ITQ system that currently covers almost all commercial fisheries. Studies have demonstrated that the ITQ system has yielded considerable economic benefits in Icelandic fisheries (Arnason, 1993, 2005, 2008; Matthiasson, 1997; Knútsson et al., 2016; Eythórsson, 2000; Yagi et al., 2012; Gunnlaugsson and Saevaldsson, 2016): harvesting costs have declined, fishing effort has been reduced considerably, and the consolidation of quotas has increased (Arnason, 2005; Agnarsson et al., 2016; Saevaldsson and Gunnlaugsson, 2015). The firms have become larger and many are now vertically integrated; that is, they are engaged in harvesting, processing, and marketing (Knútsson et al., 2016; Saevaldsson and Gunnlaugsson, 2015). Taken together, these developments have led to increased profitability in the industry.

Although the Icelandic fisheries are now conducted in both a

* Corresponding author.

E-mail addresses: stefanb@unak.is (S.B. Gunnlaugsson), dmk@hi.is (D. Kristofersson), sveinnag@hi.is (S. Agnarsson).

responsible and efficient manner, the Icelandic ITQ system has right from the beginning been controversial and has never received full public and political backing (Saevaldsson and Gunnlaugsson, 2015; Sigurðardóttir, 2012). Opposition to the way the fisheries are managed has grown stronger through the years, not least because profits have become more visible as operators have learned to take advantage of the virtues of the ITQ system. To pacify critics of the ITQ system and raise a new form of tax revenue, the Icelandic government introduced a fishing fee in 2004, which the industry pays for access to the fishing resource around the island. The fee is levied on all Icelandic commercial fisheries, which are managed by Icelandic authorities and under Icelandic legislation, both those conducted inside Iceland's exclusive economic zone (EEZ) and in more distant waters. Thus, the fee applies both to fisheries which are conducted under the ITQ system and those that are managed in a different manner, such as the coastal fisheries that take place in the summer and the lumpfish (*Cyclopterus lumpus*) fishery in the spring and early summer. The fee is levied on landed catches and varies significantly between fish species. The purpose of this fee is two-fold; to finance the direct cost which the government incurs from managing the resource, and provide the public with a fair share of the resource rent generated by the Icelandic fishing industry. Resource rent is the income from resource extraction in excess of costs, including opportunity cost and return on capital employed (Grafton et al., 2008). Therefore, the fee is both a licence fee and a form of resource rent taxation. This fee might be viewed as a success in fisheries management because it demonstrates the profitability a fisheries resource can produce when well managed under an ITQ system, and the fishing industry's ability to pay increased taxes that benefit the public. The fee has partially transformed the political discourse in the country from discussing the basis and fairness of the ITQ system into a debate about the fishing fee, its associated methodology, and its amount. Thus, this fee is controversial and under considerable political scrutiny and debate.

There are four kinds of fees and taxes in world fisheries. Firstly, normal corporate taxes, which apply to fisheries and all other industries, include taxes on profits and payroll, value added tax and other taxes levied on firms in the economy. The second form of taxation are fees to cover administrative costs arising from managing the resource and the fishing industry. This form of fee is common in many countries and often represented as a licence fee. An example can be found on the Canadian Atlantic coast (Sigurður Steinn Einarsson, 2014), and in Namibia (Kirchner and Leiman, 2014). Those fees are, however, low and only cover part of the administrative cost. Thirdly, some countries impose fees for access to the resource. These fees are lump sums that do not consider the profitability and rent generated by those utilising the resource. Such an agreement is for instance currently in place between Morocco and the European Commission (2016). Finally, there are pure resource rent taxes. Resource rent taxes in fisheries are taxes, which specifically target the resource rent that can be generated through careful utilisation of the fishing resource. This form of taxation is uncommon in world fisheries. New Zealand experimented with a resource rent tax, initially based on quota value, but those taxes were abandoned as part of a dispute settlement between the government and the industry (Grafton, 1992; Hannesson, 2005).

Implementing and determining the Icelandic fishing fee has been difficult. This Icelandic experience can be highly valuable for other countries considering introducing a similar resource taxation, because these countries are likely to face many of the same problems as Iceland did. Therefore, it is worthwhile to review some of the controversies and difficulties associated with the establishment of the fee: How high is the Icelandic fishing fee? What are the main problems connected with setting this type of fee? What do you levy the fee on? How do you protect small firms from this fee? Who has paid the fishing fee? All these questions have been addressed while implementing the fishing fee in Iceland since its introduction in 2004. The purpose of this paper is to answer the aforementioned questions and explain the methodology and

process applied when formulating this form of taxation.

A previous study discusses the setting of the fishing fee in 2004 and developments in the next few years. During this period, the fee was low and its purpose was more to recover costs than to tax resource rents (Matthiasson, 2008). This paper, however, spans a much longer time period, during which time the methodology behind the fee has changed drastically, and the level of the fee has increased considerably. Today, the Icelandic fishing fee is an important source of tax revenue and a considerable expense for the Icelandic fishing industry. In 2014, the fee amounted to 52 million euros, 6.0% of the catch value of Icelandic fishing vessels and around 1.2% of the total revenue of the Icelandic Treasury (Ríkisreikningur, 2018).

This paper is organized as follows. In section two, the implementation of the fishing fee is described in four phases, while section three examines the five main issues, which have arisen when setting the fee. Section four, tabulates what companies have paid the fees and section five contains discussion. The final section concludes the paper.

2. Implementing the Icelandic fishing fee

Fisheries have been the main engine of the Icelandic economy for the last 150 years, and still constitute the backbone of economic activity on the island, not least in the small coastal communities. In 2014, harvesting and processing accounted for 8% of gross domestic product (GDP), and 23% of exported goods and services, second only to earnings from tourism which represented 29% of exports. Harvests of the Icelandic fishing fleet totalled 1.1 million metric tonnes with an export value of 1.9 billion euros. Cod (*Gadus morhua*), is by far the most important specie (37% of export value), but the value shares of mackerel (*Scomber scombrus*) and capelin (*Mallotus villosus*), 10% and 6%, were also considerable (Hagstofa Íslands, 2015a).

The annual total allowable catch (TAC) for each stock is set every year by the Ministry of Industries and Innovation based on scientific advice given by the Icelandic Marine Research Institute. Its recommendations are based on systematic research on the distribution, size and yield potential of main species. Thus, the TAC is based on conservation and optimal harvesting (Iceland Responsible Fisheries for the benefit of future generations, 2018).

It is worth noting that there was little or no profitability in the Icelandic fisheries before the introduction of the ITQ system in 1990. This is clearly illustrated in Fig. 1, which shows the developments in the profit ratio (profit/revenue) of the Icelandic fishing industry from 1980 to 2014. Profitability was so poor in the 1980s that the average loss of the fishing component was approximately 7% of revenues during that decade. When the ITQ system was introduced, economic performance began to recover, albeit slowly at first. Since 2000, the harvesting sector has on average enjoyed a profit of 12.7% but profits in the processing industry have been slightly lower, or 8.9%. The improved financial performance of the fishing sectors and visible profitability is one of the fundamental factors that allowed for the implementation of the Icelandic fishing fee.

The implementation of the Icelandic fishing fee may be divided into four phases of different characteristics and fee structures. The first phase covers the years 1990–2003 and comprised licence fees which were intended to partly cover costs associated with the administration of the fishing resource. The fishing fee was introduced in 2004 and then raised each year in 2009–2011. Finally, the fee was increased significantly in 2012, making it a crucial expense item. Fig. 2 traces the development of the fees in 1993–2014, while Table 1 provides a more detailed overview of the changes in the license fees and fishing fees.

2.1. Phase 1: licence fees, from 1990 to 2003

This phase was characterized by low but increasing profitability. The average profit ratio (profit/revenue) in harvesting amounted to 4.8% but only 2.2% in the processing industry (Fig. 1).

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