Commercial Tourism Concessions: a means of generating income for South African National Parks

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Background and rationale

South African National Parks (SANParks) was established as a parastatal through an Act of Parliament in 1927, mandated to establish and maintain a system of national parks throughout South Africa. Although it receives an annual subsidy from Government, all revenues generated in national parks are retained and applied to the execution of its mandate, as determined by a Board of Trustees.

Over the last century SANParks grew into one of the three largest players in the tourism industry in South Africa, and the largest in eco-tourism or nature based tourism with in excess of 5200 beds and a further 1000 camp sites. Having many of the best natural areas under its management and control, SANParks had a significant influence on the development of the entire industry. However, this was not without its negative consequences which include the inefficient delivery of tourism products with often mediocre service standards; limited market segmentation and product differentiation; and prices that have not been determined by market forces. This has been compounded by other inefficient corporate policies and procedures, all resulting over the decades in significant opportunity cost to biodiversity conservation. In 1999 SANParks performed an internal review of its commercial operations which demonstrated these inadequacies when benchmarked against similar private operations.

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Commercialisation as a Conservation strategy

It is for these reasons that SANParks has come to believe that it should not itself be running commercial ventures. Generally speaking, the State does not have the skills, attitudes and incentives that drive successful businesses and SANParks is no exception. Even if these skills were to be acquired, SANParks is not able to access capital on a scale that would optimise tourism opportunities, with no shareholder base to call on for capital, and with legislation that restricts SANParks’ capacity to raise loans.

Regardless, since national parks are established and funded with public monies, it is now SANParks belief that it is inappropriate that taxpayers’ revenue be placed at risk in business ventures, or that the underlying conservation assets are placed at risk, particularly when alternatives exist in the form of private capital. Commercial ventures should be performed by the private sector, charging market-determined prices, within an appropriate regulatory framework designed to mitigate against impacts on biodiversity, and ensuring that there is a relatively risk free return to the conservation assets being leveraged.

This strategy was called ‘Commercialisation as a Conservation Strategy’. As the title implies, the intention is to generate additional revenue so as to better conserve South Africa’s national parks. This was to be done by re-focusing SANParks energies and resources on its core business of managing biodiversity in protected areas and only providing the foundation and regulatory framework for tourism and recreation – not necessarily performing the commercial operations. Consequently, the management of commercial operations or aspects of commercial operations in national parks is in the process of being transferred to commercial operators who are better qualified and equipped to run these facilities.

One of the main components of the commercialisation strategy was the concessioning of existing small camps (8 - 32 beds) in the Kruger National Park together with a number of new concession sites in Kruger and other national parks. It was anticipated that such existing camps and additional concessions could generate significant revenues for SANParks and make a significant contribution to the broader economic development objectives of South Africa. While there are other aspects of the commercialisation strategy, this paper focuses on the concessions only, providing an overview of the concession concept, the various issues encapsulated in a typical concession contract, a brief review of the process conducted, the results that were achieved and concludes with some basic lessons learnt from the experience.

The Concession Concept

A typical concession allows a private operator to construct and operate tourism facilities within a national park on the basis of a 20-year contract. Investors have either taken over or are upgrading specified existing lodge facilities, or they are in the process of building new ones. In most cases the Concessionaire is granted exclusive commercial use rights to a defined area of land, typically between 5,000 hectares and 15,000 hectares in extent within a national park, in return for payment of concession fees. At the end of the contract term all facilities revert to SANParks. The contractual mechanism is a concession contract which gives rights of occupation and commercial use of the land together with a set of obligations on the part of the Concessionaire regarding financial terms, environmental management, social objectives, empowerment and other factors. Infringement of any of these requirements carries specified penalties, underpinned by performance bonds, and finally termination of the contract, with the assets reverting to SANParks. All aspects of biodiversity management continue to be performed by SANParks, consistent with the park management plan.

Although the primary objective of the Concessioning process was to generate more revenue for the organisation, the processes were designed to encourage partnerships that exhibited the correct mix of financial strength, requisite experience and strong empowerment credentials. The focus of empowerment was on promoting and providing business opportunities for historically disadvantaged entrepreneurs, in particular those from local communities living adjacent to national parks. This was particularly necessary because South Africa’s history has been such that the majority have been excluded as users and beneficiaries of the national park system. In order to encourage a constituency for conservation and
support for national parks among the majority of South African citizens their empowerment is considered by SANParks to be vital. The SANParks concessioning process placed an emphasis on effective, grassroots empowerment at the community level, by providing profitable opportunities for community-based businesses and individuals with less emphasis on existing Gauteng-based empowerment funds (Gauteng is South Africa's wealthiest province). For the purpose of the concessioning programme, economic empowerment comprised three principal elements: shareholding, affirmative action and training, and the economic empowerment of communities through the development of small, medium and micro-enterprises (SMMEs).

To date, a total of eleven concessions have been awarded to private operators, seven of which are in the Kruger National Park, two in the Addo Elephant National Park, and two in the Cape Peninsula National Park. In addition an agreement has been entered into for a private company to manage the one hotel that SANParks has in its portfolio -- the Brandwag hotel in the Golden Gate Highlands National Park.

The Concession contract

The contract that governs private operators in a national park is understandably a comprehensive legal agreement that covers all aspects of a commercial operation within a national park. The main components of the contract are as follows:

**Conceptual issues**

- The contract does not alienate national assets as the concession areas remain an integral component of the park real estate contributing to the overall biodiversity objectives of the park. All improvements built by the Concessionaire become the property of SANParks on a Build, Transfer, and Operate basis.
- It is a balanced set of rights and obligations on both the Concessionaire and SANParks with each party having recourse if the other fails to meet its obligations.
- It sets the rules that will apply through the life of the concession governing how each party will act. These rules are detailed, and, as a result, the concession contract is a lengthy document of approximately 150 pages.
- Since one can never predict the future precisely, the contract anticipates the unexpected in that it also sets out the process and rules by which, when the unexpected occurs, the parties will sit down and resolve how to handle the situation.

**Concessionaire qualifications**

- SANParks requires a single purpose legal vehicle to be created in order to operate the concession so that other activities of operators do not affect the viability of the Park operation. This can be a project company, a joint venture or a Trust.
- Whilst shareholdings in the legal entity may change, the Concessionaire must continue to exhibit the qualities by which it prequalified throughout the life of the concession. In particular, one of the shareholders (owning at least 20% of the equity) must have the appropriate eco-tourism experience (refer to section on prequalification).
- Similarly the sponsors of the project need to demonstrate and maintain a specified level of financial solidity in order to be an acceptable partner for SANParks.

**Legal aspects**

- The guests the Concessionaire brings into the Park are the Concessionaire’s responsibility. The Concessionaire therefore needs to indemnify SANParks so that if guests are injured they cannot sue SANParks; it is the Concessionaire who is accountable.
- Related party transactions are controlled within the contract preventing the Concessionaire from siphoning revenues off to related parties (sister companies) for various services provided e.g. travel agents or management company, thereby reducing the turnover based payments to SANParks.
• If the Concession is terminated through the Concessionaire’s fault, the Concessionaire gets kicked off the site, at no cost to SANParks. However the financial institutions that financed the physical developments have the right to appoint a new Concessionaire, provided that that Concessionaire is acceptable to SANParks. This provision is necessary to enable the physical developments to secure financing.

**Financial**

• The Concession Contract is 20 years in length with no right to renew or right of first refusal. This was deemed to be a sufficient term to encourage real investment in infrastructure and allow enough time to generate an adequate return on investment. SANParks will have the option of rebidding the concession after the 20 years. Assuming that such opportunities will become increasingly scarce over time the value to SANParks is likely to increase. If the Concessionaire has been successful, he will be well placed to win a re-bid contest.

• The Concessionaire’s right to operate in a national park is paid for by an annual concession fee that is determined by a percentage of turnover bid by the Concessionaire during the tender process. All concessions are also subject to a minimum rental payment. In order to discourage “over-bidding”, Concessionaires have to pay a minimum of 65% of the fee payment projected for each year in their bids.

• During the first twelve months, the Concessionaire is held to a Bid and Development Bond of R250,000 which is designed to ensure that the Concessionaire actually goes ahead with its proposals. If the Concessionaire fails to implement the project within a specified period, it forfeits the bond.

• There is a system of financial penalties in force throughout the life of the concession for breaking rules, damage to environment, non-respect of empowerment obligations, etc.

• The whole relationship is backed up by a performance bond set at R20,000 per bed, which SANParks can draw on in the event of the Concessionaire failing to respect the contract (financial, empowerment, environmental).

• Ultimately, the Concession can be terminated for persistent or serious breaches, including empowerment commitments, and the rules for this are clearly set out including financial settlement.

**Environmental**

• The National Parks Act and the Park Regulations govern the operations of the Concessionaire in the park together with a comprehensive set of Environmental Guidelines drawn up especially for each of the concessions. In particular each concession is subject to a site-specific Environmental Impact Assessment and the development of an Environmental Management Plan. These guidelines apply to both construction and operational phases and may change over time to reflect new policies and approaches. The rules and regulations include the appointment of an environmental control officer (ECO), protection of cultural and natural resources, biosphere manipulation, site carrying capacity, visual impacts including lighting, bulk infrastructure (e.g. electricity, water, communications, waste management), the siting construction and maintenance of roads and tracks, fire management, provision of artificial water points, staff accommodation and health and safety, park access and SANParks access to concessions, standards for concession vehicles, and codes of conduct for drives, walks and off-road driving.

• This set of rules are supplemented by the fact that all the operators have previous eco-tourism experience, as required by the prequalification criteria. There are various reporting requirements on the above regulations, together with regular monitoring of compliance with the regulations.

• As with other aspects of the contract there is a system of penalties if the Concessionaire or one of its employees or sub-contractors, commits a breach of the regulations or the EIA and even termination in the case of persistent or repeated breaches.

**Empowerment**

• The obligations in terms of empowerment were determined by the bidders themselves in the sense that 20% of the award mechanism was based on empowerment commitments. To get points, the bidders had to commit to progress in economic empowerment - shareholding,
affirmative action and training, and creation of economic opportunities for local communities via outsourcing. These commitments are quantifiable in terms of extent, value and time. The Winning Bidder is held to these commitments, which form part of the concession contract.

- Concessionaire is obliged to report on progress made to achieving these obligations every six months.
- Failure to realise the objectives results in financial penalties of up to R1m and persistent failure results in contract being terminated.

Process

Prior to SANParks commercialisation initiative there had been previous attempts at commercialisation in at least one Provincial Parks Board that was marred with controversy and claims of corruption. It was therefore all the more important for the SANParks process to be totally transparent and hence SANParks employed the International Finance Corporation (IFC), the private sector arm of the World Bank, as lead advisors. In addition to being recognised leaders in transactions where public interests are paramount, IFC was able to mobilise donor funding which covered the costs of various specialist sub-consultants. The process that was followed is summarised as follows:

Marketing and structuring review

The aim of this first phase was to examine all the issues and chart the way forward. It included selection of the concession areas, mapping them, establishing carrying capacities, performing a legal review, designing the contract, developing the environmental guidelines, determining how to approach the social and empowerment issues, and modelling the operations to establish viability and minimum rentals.

Information Memorandum and Expression of Interest

SANParks issued an Information Memorandum to the public and to potential investors providing basic details of the concession opportunities, their location and size, and a synopsis of how the process would be run. This documentation was used as a basis for consultations with the public on both the concept and some of the specifics. Interested investors were requested to express interest in specific sites and provide basic bidder information. The information on the number and quality of operators served as a guide to establish appropriate levels for the prequalification criteria.

Prequalification

The objectives of a prequalification phase are two-fold. First, it is to ensure that the companies that emerge from the prequalification process all have the financial strength and proven experience in eco-tourism operations to give confidence that they can be entrusted with the development of lodging facilities in a national park. Secondly, it is to ensure that there is a healthy level of competition for every site being offered, say between two and six competitors. Criteria related to the empowerment of previously disadvantaged groups were not explicitly used during the prequalification stage. By contrast, during the bid evaluation process, empowerment proposals figure explicitly and clearly with a significant number of points being allocated to empowerment. To prequalify for a typical concession, the Submitting Company had to meet the following criteria:

- **Financial strength**: The asset value of the Submitting Company had to be at least R20 million. If the Submitting Company was a newly created company or partnership, then it could meet this criterion with reference to the asset value of its parent shareholder(s) or partners, weighted in proportion to their shareholding or participation. In addition, the relevant company had to be commercially solvent;
- **Proven eco-tourism experience**: The Submitting Company had to demonstrate proven eco-tourism experience having operated an eco-tourism facility of at least 30 beds, for at least 3 years. If the Submitting Company was a newly created company, then it could meet this criterion with reference to the qualifications of any one of its parent shareholders or partners, provided that the shareholder or partner held at least 20% of the total company equity or interest.
**Due diligence and “ground-truthing”**
The purpose of a due diligence process is to give all prequalified bidders the opportunity to ascertain all
the information they need to present informed and competitive bids for the sites they are qualified to bid
for, including physical facilities, ecological information; and to ensure that such access to information is
equal for all prequalified bidders. To this end SANParks made available a data room with copies of all
relevant documents and policies which could possibly have a bearing on the concession. Similarly
bidders conferences were held during which the concession contract was distributed, explained and
discussed in detail and where bidders were able to pose written questions, the answers of which were
distributed to all bidders. Importantly the concession contract is finalised during this phase so that bidders
have full knowledge of the contract before bidding. All bidders had to include signed copies of the
concession contract in their bid submissions.

All bidders were given the opportunity to conduct helicopter fly-overs of the concession areas, looking at
the features, setting and context of the concession and for selecting possible sites. In addition all bidders
were allowed to book dedicated time with the relevant ranger to allow detailed ground truthing of the sites
and concession areas.

**Bidding Memorandum**
The bidding memorandum sets out in detail the manner in which the actual bidding process is conducted,
including what information is required, the opening of bids, how the technical components are to be
evaluated, how the financial bids will be evaluated, the procedure for the announcement of winning
bidders, closure of the concession contract, requirements in terms of the bid and development bond,
payment of execution fees and of course the timetable.

Each bid submission contained two sealed envelopes. The first envelope, the “Technical Offer” contained
all the non-financial aspects of the submission including:

i. signed copy of the final form Concession Contract;
ii. all the information relating to the constitution of the company, joint venture or trust;
iii. a notarised Deed of Attestation signed by the authorised Legal Representative confirming a range
   of representations and undertakings made by the Concessionaire, including compliance with
   prequalification criteria
iv. three copies of a Development and Environmental Proposal, conforming to a specified outline;
v. three copies of a Business Plan, conforming to a specified outline
vi. three copies of an Empowerment Proposal, conforming to a specified outline
vii. a Bid and Development Bond as specified

The second envelope contained the “Financial Offer” also according to a predetermined format. Bidders
were provided with a detailed explanatory note on the format of the financial bids, as well as a
spreadsheet model.

Immediately after the passing of the deadline for bid submission, the bids were opened in a public forum.
Technical envelopes were opened immediately and the unopened Financial envelopes were placed in a
locked strongbox and turned over to the legal advisors for safekeeping.

Separate and externally appointed teams of technical experts evaluated all the technical offers. The
Empowerment proposal was the only proposal, other than the Financial Offer, to receive points that
contributed to the award of the concession. Accordingly these proposals were evaluated blind with no
reference in the proposals to the identity of the bidder. Twenty out of a total of one hundred points were
allocated to the bidder's empowerment proposals, which, in the subsequent Concession Contract, were
translated into quantifiable obligations to be met by the Concessionaire throughout the term of the
Contract. Proposals failing to achieve a minimum hurdle of 8 points out of the possible 20 were failed. At
least one submission was failed on this basis and the Financial Envelope was returned unopened.

The Development and Environmental Proposals were evaluated and scored on a pass-fail basis. The
purpose of the evaluation of these proposals was to ensure that Bidders understood the minimum
environmental standards contained in the Environmental Guidelines provided and had factored those standards into their plans. This approach was deemed to be more transparent and less open to subjectivity than attempting to evaluate the relative merits of differing environmental approaches. In the event of a proposal being declared non-compliant according to specifications provided, the overall bid would have been declared non-compliant, and the Bidder's Financial envelope would have been returned unopened. As it happened no submissions were failed.

The Business Plans were also evaluated and scored on a pass-fail basis. The purpose of the evaluation of the Business Plans was to check that Bidders had fully developed all business aspects of the proposed eco-tourism project, and were proposing credible schemes based on generally accepted business principles applicable to eco-tourism projects. Again, assuming that Concessionaires knew their own business better than anyone else; that they continued to satisfy the prequalification criteria, and with the financial risk being transferred almost entirely to the Concessionaire, this mechanism was thought to be more appropriate than a subjective assessment and allocation of points. In the event of a proposal being unsatisfactory, the overall bid would have been declared non-compliant, and the bidder's Financial Offer would have been returned unopened.

With regard to the opening of the Financial Envelopes, a public meeting was convened in the presence of the media. At this meeting the Chief Executive Officer of SANParks announced the empowerment scores that were entered into a computer and displayed publicly. The Financial Offers were opened in the presence of the meeting and inspected by SANParks' financial advisers to verify that they had been submitted in the correct form. Each Concessionaire had to submit the forecasted annual turnover for the operation, together with percentages payable to SANParks. This was termed the Forecast Annual Concession Fee. In order to ensure that bidders submitted realistic bids, 65% of this forecast was taken as the Fixed Concession Fee Commitment. These fixed commitments were entered into a computer programme and a discounted net present value (NPV) was determined. For each site, the bid presenting the highest Committed Net Present Value received a financial score of 80 points. Other bidders then received proportional scores.

For each site, the computer model aggregated the Empowerment Scores and the Financial Scores of each bid to calculate an overall winner. SANParks simply countersigned the contracts making each contract effective.

The Results

The results were beyond the expectations of SANParks. The total number of new beds arising from the process is approximately 380 and the total capital investment is estimated at R270 million. In terms of the bidding system SANParks can depend, with a high degree of certainty, on the guaranteed minimum stream of income over the concession period, equivalent to the 65% of the projected fees. Starting with the guaranteed income, the Net Present Value (at a 5 per cent real discount rate) of the concessions amounts to R253 million, in constant 2003 Rands for the 20 year period. The undiscounted, un-inflated equivalent of this amount is R436 million. The actual total amount forecast to be paid to SANParks (undiscounted) over the 20-year period is R677 million. This represents a major contribution to the future finances of the organisation. Similarly, from a tax perspective, it is estimated that at maturity, tax receipts will be in excess of R60 million per annum, which exceeds the annual operational subsidy that SANParks receives from the State.

In general, the empowerment results achieved by the bidding process were also good. Three of the successful bidders were black-controlled consortia, and all the other bidders have significant percentages of black shareholding with some specifically focused on communities adjacent to the park in question. This is considered to be an excellent result in a tourism sub-sector in which black representation in ownership has hitherto been virtually non-existent. In total, the new game lodges are projected to create 683 new permanent jobs, excluding employment created during the construction phase. In terms of the detailed schemes for affirmative action, according to agreed timetables, the Concessionaires have
undertaken that a minimum of 79 per cent of their employees will be recruited from historically disadvantaged communities, most of which will be those living adjacent to national parks. Finally, Concessionaires have undertaken to outsource minimum guaranteed Rand amounts of contracts with local historically disadvantaged business people for the supply of various services. The total of these commitments is R7.8 million per annum by the third year (in 2003 terms).

**Performance to date**

Some of the concessions have had two years since bid award, while others have had three years. Generally speaking the Environmental Impact Assessments, anticipated to take six months to conclude took on average twelve months. Six of the eleven are operational with a seventh expecting to open its doors for business by November. The designs and styles of the developments are all very different and cater to different market segments. Of the remaining four, one Concessionaire withdrew from one site with the second place bidder taking over the contract causing unexpected delays, while two are still in the EIA process although these were awarded at a later date. The fourth is taking an unnecessary long time to complete, a consequence of inexperience. All of them are paying their minimum committed rentals.

SANParks has had to develop a small, but strong contract management function which is critical to the continued success of the approach. Any number of issues from shareholder disputes to environmental breaches has arisen which have needed to be managed carefully and being able to do so has maintained the integrity of the overall process. In resolving issues and monitoring compliance, SANParks has attempted to be fair-minded but firm in its approach and flexible when necessary. On several occasions SANParks has ordered Concessionaires to correct deficiencies such as the removal of a radio tower, moving board walks and upgrading of roads and in other cases has fined Concessionaires for misconduct. Interestingly, the Concessionaires complain regularly that SANParks does not adhere to the same level of environmental standards as applicable to themselves. This was anticipated, and rather than relaxing these standards, SANParks will over time have to comply with its own regulations.

**Lessons learnt**

Although still early on, it is possible to make some preliminary observations:

1. Good quality sites are required to attract good quality operators and good quality bids (financial and empowerment).
2. Good quality operators are essential for quick and responsible delivery achieving the anticipated financial and empowerment objectives. The prequalification process must screen out poor quality operators. This is particularly the case when the operator is under enormous pressure with a limited period contract and with fixed rentals payable regardless of whether the lodge is open for business.
3. For a competitive bidding system to be effective it does require more demand (or at least apparent demand*), for sites than supply of sites. In a situation where there are a number of opportunities but there is an unsophisticated market, a different approach should be considered.
4. When incentivised, operators can come up with imaginative and far-reaching empowerment schemes.
5. “Balanced” contract management is essential to the continued success of the process
6. Some of the “hard and fast” environmental rules such as carrying capacity have been altered in the light of experience. Flexibility is required, but without departing from established standards.

**Conclusion**

SANParks wilderness assets have significant economic value which can be captured through a responsible Concessioning process combined with firm contract management. Since all revenues are retained by SANParks, the concessions are, in a meaningful way contributing to the core function of
protecting biodiversity. The process has greatly expanded the range and extent of sustainable economic activity generated by the national parks, without sacrificing their biodiversity objectives. The private ecotourism sector has “stepped up to the mark” in accepting higher environmental standards and have proposed imaginative schemes, with real benefits to local communities and employees. Initial external fears that the Government would remove its subsidy as a result of the generation of additional revenue have proven to be of little substance, and in fact the converse has happened. The process has vastly improved SANParks’ image in eyes of the South African Government who are seeing that national parks are being put to sensible and sustainable use for the economic development of the country. Correspondingly the South African Government has increased its annual financial commitment to SANParks specifically for the creation of new parks and the expansion of existing parks. Finally, the process has been a two-way street and in time SANParks will be forced to meet the same high standards that apply to Concessionaires, which can only be to the overall benefit of conservation.

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