

STATEMENT OF STEPHEN P. MARTIN
DEPUTY DIRECTOR
NATIONAL PARK SERVICE
DEPARTMENT OF THE INTERIOR

BEFORE THE SUBCOMMITTEE ON NATIONAL PARKS, HOUSE COMMITTEE ON RESOURCES, REGARDING
THE IMPLEMENTATION OF THE NATIONAL PARK SERVICE CONCESSIONS MANAGEMENT IMPROVEMENT ACT
OF 1998

APRIL 6, 2005

Mr. Chairman and members of the committee, thank you for the opportunity to provide an update on the implementation of the National Park Service Concessions Management Improvement Act, Title IV of the National Parks Omnibus Management Act of 1998 (Public Law 105-391). We are pleased to discuss the status of the National Park Service (NPS) concessions management program, including the issues which we understand are of interest to you, the improvements we are making, and the ongoing development of working relationships with our external partners.

The NPS concessions program administers approximately 591 concessions contracts in 130 parks. These contracts, which range from under \$100,000 to over \$100 million in annual gross receipts, currently generate approximately \$800 million in annual revenues. The overall objective of our concession program is to enhance the visitor experience by allowing third parties to provide food, lodging, and recreational services to visitors, and to provide a fair return to the Federal government for allowing the provision of these services. We do this in concert with our industry partners. We appreciate the involvement of the Congress in attaining these objectives and look forward to working with you to continue to improve our program.

Concessions in our national parks predate the formation of the National Park Service. Most of the large concessions operations in our Western parks were built in the late 1800s by the large railroads or companies looking to serve the growing demands of travelers from the eastern U.S.

The Concessions Policy Act of 1965 (Public Law 89-249) provided certain protections for incumbent concessioners. These protections included a preference in the renewal of their contracts, contract terms of up to 30 years, and possessory interest (PI), which recognized a right of compensation for real property improvements made by the concessioners.

By the early 1990s, Congress began to recognize that the concession system required substantial reform. In many cases, visitor services were lacking in quality, facilities were not being well-maintained, prices were higher than they would be for comparable goods and services outside the parks, and some concessioners were making much larger profits than would be expected from a competitive private-sector market. Most observers attributed these problems to the fact that competition for concession contracts was virtually non-existent. The desire to transform the concessions program into a more competitive, business-like operation was the driving force behind passage of the NPS Concessions Management Improvement Act of 1998. To accomplish that goal, Congress repealed the preference in renewal provided by the 1965 law, providing instead a preference primarily for small concession operations, shortened the maximum contract term to 20 years, and replaced PI and its valuation formula with leasehold surrender interest (LSI) and a new valuation formula.

We are beginning to see the benefits to visitors of the 1998 law in cases where incumbents and potential operators have had the opportunity to compete fairly and equally for a concession contract. For example, at Denali National Park, the new contract includes provisions for a performance-based system for maintenance of the large bus inventory. This has improved the visitor experience by reducing the number of bus breakdowns and increasing the reliability of buses. Similarly, at Mount Rushmore National Memorial, the new contract includes provisions for improvement to food services for visitors and for the reduction of visitor waiting time for meals.

Although it has taken the NPS longer than initially expected to award new contracts, we are making significant progress. Five years ago, the NPS concessions program was in poor shape. The program had been criticized in numerous reports by the Department's Inspector General, the Government Accountability Office, and outside auditors, and it was facing a huge backlog of expired or soon-to-be-expired contracts. For the first time in NPS history, the agency needed to award almost all of the approximately 591 concession contracts.

The NPS took this challenge seriously. We conducted a top-to-bottom review of the concessions program and engaged a top business consultant, PricewaterhouseCoopers, to bring best business practices to our efforts and develop protocols that focus on the key business processes of contracting and contract oversight in all concession contracts. We began developing a standards evaluation and rate approval process to better meet our contract oversight responsibilities and ensure visitors receive the best possible services. In addition, we began to professionalize our work force by hiring staff with master's degrees in business administration and by developing business training courses with Northern Arizona University. These steps are yielding returns in the quality of service and improved program performance.

In addition to improving the administration of the concessions program, we have also made a great deal of progress in awarding new contracts. Since 2001, with the assistance of four top business consultants, we have awarded 322 contracts and expect to award 125 more this year, for a total of 447. This will reduce our backlog to approximately 100 contracts. A chart showing the awarding of contracts from 2001 through 2005 is attached to this testimony.

As we have worked to implement the new law, we have found that moving from a non-competitive to a competitive system poses enormous internal and external challenges. We underestimated the significant cultural change that this new approach would require of NPS leaders, employees, and concessioners. We are working closely with our concessioners to form a stronger partnership. Together we will create an improved concessions program for our visitors with high quality contracts and operations.

Issues that are of continuing concern to concessioners and the NPS include franchise fees, possessory interest negotiations and leasehold surrender interest rules, preference, performance based contracting, contract length, feedback to offerors, and commercial use authorizations.

Franchise fees

Franchise fees are one of several factors that NPS is required by law to consider in awarding a concessions contract. The 1998 law specifies that a franchise fee established by a contract reflect the probable value to the concessioner of the privileges granted by that contract. This value is based upon a reasonable opportunity for net profit in relation to the capital invested and the obligations of the contract.

The franchise fees, which represent a percentage of gross receipts, vary widely among the contracts. Market forces are one reason for this variance. For example, the law allows a prospective concessioner to propose a higher franchise fee in an effort to compete against other offerors. Another reason is that larger contracts typically require higher up-front capital investments (including the buyout of the previous concessioner's possessory interest) as well as higher ongoing facility maintenance expenditures which generally result in a lower franchise fee. An example of this is the Yellowstone National Park lodging and food service operation in which the draft contract obligates the concessioner to invest capital and maintain the facilities to the highest standards. Because the franchise fee is based on the obligations of the contract and the capital to be invested, our analysis suggested a lower minimum franchise fee was appropriate. A third reason is the type of concession business involved. Some types of concession operations are more profitable than others; for example, the transportation business is generally more profitable than the lodging business, and the lodging business is generally more profitable than the food and beverage business.

Transition from Possessory Interest to Leasehold Surrender Interest

Possessory interest (PI) is the term used in concession contracts issued under the 1965 law to provide a contractual right of compensation to park concessioners for improvements to facilities they acquired or constructed on park lands for use in their businesses. Individual contract language defines the method by which PI is valued, and generally provides for a value determination process similar to arbitration to settle differences either between the previous concessioner and a new concessioner, or between the United States and the new concessioner.

The 1998 law introduced the concept of leasehold surrender interest (LSI) to provide a contractual right of compensation for capital improvements made by concessioners under a concession contract. The value of LSI in a capital improvement is the amount equal to the initial value of the construction cost of the capital improvement, adjusted by changes in the Consumer Price Index, minus depreciation of the capital improvement. In a Special Rule for Existing Possessory Interest, the law also provided that a concessioner that obtained a PI under the terms of a concession contract is entitled to receive compensation for such PI improvements as provided in the concession contract. This amount carries over into a new concession contract as the initial value of LSI for that contract.

In practice, there are two ways of establishing the ending PI value (and, hence the initial LSI value for the new contract): through binding value determination processes, and through negotiations between the current and new concessioner. For example, binding value determination processes were used at Grand Canyon and Yellowstone, and negotiations between a current and new concessioner occurred at Crater Lake.

Another way of establishing PI, which several concessioners have requested, is through negotiations with the NPS to determine the PI value prior to the release of a prospectus. Although existing concession contracts do not provide for the NPS to require negotiations, we can choose to enter into such negotiations if requested by the current concessioner. We are supportive of this approach whenever possible. It helps to provide more certainty for both the NPS and the current concessioner, and helps provide a clearer financial picture for prospective concessioners. It also has the potential

of saving time and money for both the concessioner and the NPS by avoiding costly and time-consuming arbitrations with unpredictable outcomes. One successful negotiation completed last year was for Trail Ridge Store at Rocky Mountain National Park. Several other negotiations are in process. The NPS is looking at requests for similar mutual negotiations in other areas.

A potential issue of concern to the National Park Service is the possibility of government debt obligation in relation to concessioner PI. It is important to note that the compensation for concessioner PI is ensured. Generally, the newly selected concessioner provides this compensation. However, ensuring payment of PI reflects a governmental obligation. While we believe the concessioner is entitled to possessory interest as defined in the contracts and in the 1965 act, we are concerned that some valuations may exceed the fair value and result in potentially uneconomic future contracts.

Valuation of LSI is also an issue. The NPS Concessions Management Advisory Board recently reviewed current LSI rules to find ways to simplify the management of LSI and provide more certainty and transparency as to the value of LSI over the term of a concession contract. An Advisory Board working group was formed and included NPS concessioners. The Advisory Board has accepted the working group's recommendations on three issues: how LSI credit would be achieved, how to allocate LSI to buildings, and how to track and value LSI over the life of the contract and has forwarded them to NPS.

One of the Board's recommendations is that the NPS revise the "50 percent rule" which currently may be perceived as a disincentive to concessioners to invest in needed improvements in a facility. The Administration is now reviewing these recommendations and will be happy to provide the Committee with the results of this review once it is completed.

Preference

While the intent of the 1998 law was to make the concessions process more competitive, it provided that all incumbents grossing \$500,000 or less, and all outfitters and guides, would be provided a preference in the renewal of their contracts, if the concessioner has operated satisfactorily during the term of its contract and has submitted a responsive proposal for a proposed new contract which satisfies the minimum requirements. Approximately 455, or about three-quarters of our contracts, fall into this category.

We are aware that some interest exists in changing the right of renewal preference threshold. The right of renewal preference threshold is a key component in ensuring a competitive process in the concessions program. We want to explore ways to promote and encourage the participation in concessions of small businesses, including those that are locally owned and operated, without reducing competition. The competitive process that the 1998 law engendered has resulted in multiple quality proposals on most prospectuses and concessioners who are providing quality services to the public.

Other contracting issues

Another area that we believe deserves careful consideration is a method to reward a concessioner for outstanding contract performance. The Federal Acquisition Regulations allow for "performance based contracts" where contractors can receive benefit for providing outstanding service or products. We have begun to evaluate this system to see if it has applicability to concession contracting.

We are also very interested in developing a system to provide feedback to those who submit proposals for a contract and are not awarded that contract. A process that provides unsuccessful offerors with appropriate feedback will enable them to understand why they were not successful and help them improve their future proposals.

Commercial Use Authorizations

Commercial use authorizations (CUA) are replacing the use of incidental business permits for businesses located outside of parks that conduct business within parks – tour guides, for example. The NPS is planning to issue interim guidance this spring that will provide, among other things, for an evaluative process for selecting CUA holders, rather than a lottery, in those cases where the number of CUAs needs to be limited. This interim guidance will remain in place until the NPS finalizes CUA regulations.

The initial proposed rule for CUAs published by the NPS for comment in November, 2002 provided, among other provisions, for the use of a lottery system for cases where the number of CUAs need to be limited. After receiving significant public comment on the proposed rule, we asked our Concession Management Advisory Board to establish a multi-disciplinary work group to consider the comments. Following that process, NPS is revising the proposed rule. The NPS hopes to publish the new proposed rule for comment this year.

One of the provisions of the 1998 law called for the Department to submit a report to this committee and the Senate Energy

and Natural Resources Committee within seven years following its enactment. We anticipate having a comprehensive report to the Congress no later than December of this year.

The NPS leadership is dedicated to providing the very best concessions program possible, consistent with the NPS Organic Act of 1916 and the Concessions Management Improvement Act of 1998. We are continuing to award contracts as quickly as possible, simplifying the smaller contracts to expedite the opportunities these contracts present while also developing enhanced capabilities to more effectively manage the assets associated with the large contracts. Over the last two years, with the help of our staff, superintendents, consultants, and concessioners, we have made a great deal of progress toward enhancing the quality of our concession program. We will continue to work toward improving the contracts and increasing the pace at which we award those contracts.

This concludes my testimony. I would be happy to answer any questions you might have.