

Review of Percentage Revenue Framework

Summary of Issues and Options

Introduction

The Department of Conservation (DOC) supports the Minister of Conservation in looking after public conservation land. DOC seeks to protect native wildlife, manage the natural and historical resources public conservation land contains and provide for recreation and tourism.

DOC's Outcome Statement in its Statement of Intent is "New Zealanders gain environmental, social and economic benefits from healthy functioning ecosystems, from recreation opportunities, and from living our history."

Businesses and commercial activity can be undertaken on conservation land through the granting of a concession and the payment of an "annual activity fee".

One of methods used to determine the fee for some (but not all) concessions is the *Percentage Revenue Framework*.

Purpose of this review

DOC is reviewing its Percentage Revenue Framework to:

- ensure it remains relevant as it has been operating in its current format for around 5 years
- improve transparency of this method and how it is applied
- improve the consistency of the percentage rates determined
- improve the connection between its fee setting structure and the provision of a fair return to the Crown.

DOC is seeking your input and feedback on the Percentage Revenue Framework.

Background and context

DOC is authorised under [s17Y of the Conservation Act 1987](#) to charge businesses that operate on conservation land. Section 17 specifies that this fee, also called a rent or a royalty, can be fixed at the market value having regard to certain matters. In the case of conservation land, most concession fees based on the PRF involve non-extractive or non-depletive uses of the land and are thus termed a resource rental.

A percentage revenue method is a common approach to determine a royalty or resource rental payment. It is a return to a resource owner for the right of another to use of that resource (in this case conservation land). The Percentage Revenue Framework accounts for 30% of third-party Crown revenue from conservation land.

The revenue generated from the annual activity fee is referred to as third party crown revenue and belongs to the Crown. The Crown allocates this revenue to DOC, but DOC does not have an automatic right to it. DOC invests the revenue generated from the annual activity fee back into conservation for specific uses based on its management priorities.

DOC sought independent advice from Deloitte on the Framework, involving the consideration of issues and options. The paper prepared by Deloitte can be found on the review webpage.

The Percentage of Revenue Framework – current state

The Percentage Revenue Framework is primarily used for assessing fees for accommodation, retail, general tourism, guiding, ski fields and hydro power schemes. It has five factors that are used to determine a percentage (%). This percentage is then applied to the Gross Revenue, that a concessionaire has earned from the use of conservation land, to calculate the annual activity fee.

This review is examining the ongoing relevance of this formula and its component factors. The formula below shows these five factors:

$$\text{Annual activity fee} = \text{Percentage} \times \text{Gross Revenue}$$

$$\text{Percentage} = B + P + DI + E + EC$$

The percentage revenue formula factors are outlined below:

- **Base (B)** – the base rate ranges between 3.5% and 7.5%. It recognises the capital investment the concessionaire has made. If they have made a larger investment the base percentage is lower.
- **Premium (P)** – the premium varies 0% and 2.5%. It recognises the uniqueness of the site where the business is undertaken. The higher the uniqueness the higher the added percentage.
- **Department Infrastructure (DI)** – is between 0% and 1%. If DOC has developed and/or maintained the local infrastructure that benefits a business, a contribution to the cost of the infrastructure is required. The larger the investment by DOC the higher the added percentage.
- **Exclusivity (E)** – ranges between 0.5% and 1.5%. If a concessionaire has exclusive access to an area, with the right to keep the public out, an exclusivity premium is added to the base. The larger the exclusive area, the higher the added percentage.
- **Environmental Compensation (EC)** – varies between 0% and 4%. This factor is to compensate for potential residue adverse impacts of activities on conservation values. The larger the potential effect, the higher the added percentage.

In theory, the lowest and highest percentages the Framework can produce are 4% and 16.5% respectively. However, the Percentage Revenue Framework contains benchmark percentages to guide the final determination of the percentages for some specific activities.

Considerations for the review

With any fee there is a tension between simplicity (one approach for all) and bespoke (every concession is negotiated). The existing fee setting structure was developed to provide greater certainty and efficiency for all parties. The Percentage Revenue Framework also:

- recognises the matters to 'have regard to' in s17Y of Conservation Act 1987
- is straightforward to calculate the fee once the percentage is determined
- shares business risk– returns fluctuate with good and poor seasons
- a percentage of revenue approach is an internationally well recognised and used approach

- relies on revenue or volume information being readily available for all businesses (degree of complexity of information extraction will increase for more complex businesses).

Although the Percentage Revenue Framework provides a basis for calculating fees, Deloitte suggested there are several areas where improvement could be made. These include:

- Changes to the fee setting structure to help address issues of subjectivity, clarity and complexity.
- Consideration of alternative methodologies, for example direct charges.
- Methodologies which would address concerns with 'locking up' land through unused concessions
- Improved ability to recognise the complexity of some business' revenue arrangements (e.g. 'outsourcing' parts of the concession business).

There is also the benefit-cost trade-off for all parties in providing the necessary information for accurate fee determinations.

Questions:

DOC would like some feedback from you on the current system.

Do you think the Percentage Revenue Framework provides a fair market fee?

What parts of it do you agree with?

What issues do you think DOC should address in the review?

The Percentage Revenue Framework – future state - other potential methods

DOC is now seeking your feedback on other potential methods. Deloitte identified four potential methods for consideration, these include:

1. **Status Quo.** The Percentage Revenue Framework in its existing form
2. **Royalty.** A variation of the existing framework (not include DOC investment or environmental factors) and market evidence applied to support the royalty rate
3. **Market (auction).** Using auctions to set the value of the rights as they come up for renewal
4. **Economic Value Added/Excess Returns.** Returns over and above a specified 'normal' return on investment are treated as excess and attributed to conservation land as a rental.

Deloitte considered the possibility of a separate method for complex or high capital investment concessions. These would essentially be negotiated outcomes. However, Deloitte do not recommend this option because it may result in inconsistency and lack of transparency.

Question:

DOC would like feedback from you on these other methods –

Do you agree/disagree with these methods?

What do you see as the costs and benefits of these various methods?

Are there any further methods you think DOC should consider?

Other potential enhancements suggested by Deloitte included:

- more consistency in **collecting the financial/other information** from concessionaires required to assist in determining the fee and providing overall market or industry benchmarks
- rationalise the **fee setting process** rather than a case by case basis. For example, a standard fee or percentage is set by regulation rather determined by DOC on a case-by-case-basis
- put in place an **external Governance structure** to overview the fee setting process. This would provide industry confidence that the Department is delivering to its state policies and practices.

Questions:

DOC would like your feedback on other potential enhancements to the Percentage Revenue Framework

Do you have any comments on the above potential enhancements?

Are there any further potential enhancements you think DOC should consider?

We welcome your feedback on the above issues and options.

If you have any questions, please email Steven Kerr at prfreview@doc.govt.nz.