

# Private Finance Constructions for Defense

*An interview with LCol Drs RJ Berkhout RC (RNLA)*

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## Introduction

*Following the footsteps of the United States, the United Kingdom and many European countries, The Netherlands' government is implementing Public Finance Constructions (PFC) as a means of financing and realizing public infrastructures. Being preceded by the Ministry of Traffic, Public Works and Water Management, the Dutch Ministry of Defense (MoD) is picking up on this trend of having private parties finance assets for Defense. The new Headquarters for the Army is going to be built in a PFC-way. We interviewed Lieutenant Colonel Berkhout who works at Central Staff and he is one of the only officers having experience with private finance because he is a member of the working group to realize the new army Headquarters.*

**Why do the armed forces use Private finance, although they have approximately one billion euro per year to invest?**

“Before answering this question, first, let me explain what PFC means by telling you about the example of the “Kromhout” project. The army needs a new headquarters, to accommodate 2,000 civilian and military employees. To fulfill this need, a PFC-construction is decided upon. Not only does the private consortium that will be selected finance and deliver the building, but also the consortium will take care of supporting services, such as maintenance, catering, child care, cleaning and reception. So, actually, the army does not request only the building by itself, but we concentrate on the whole range of requirements: room to work for 2,000 persons, according to specific standards and definitions.

PFC-financing is based on the notion that civil enterprises are better suited to supply specific services and goods and therefore, will, eventually, be cheaper than projects fully financed by the government. Simply put, the government should stick to its core business and hire others for support. The Ministry of Defense will select the consortium of enterprises that makes the best offer, in terms of costs and quality. As soon as the

product is ready for use, the MoD will pay the consortium a preset amount of money for a preset period of time.

PFC-financing benefits the efficiency of the MoD; by PFC-financing, the maximum result can be achieved from using public funds. The MoD also saves on its allocated budget. Most of these savings will have to be returned to the Ministry of Finance. However, the MoD and the Ministry of Finance have agreed that a certain percentage of money saved by PFC will be returned to the MoD. This percentage also works as an incentive for efficiency to the MoD.

In my opinion, PFC is an excellent way to employ public funds in an efficient manner. Within the MoD, PFC is most useful for purchasing long lasting assets.”

#### **PFC-contracting does not sound easy ...**

“Drawing up a profitable PFC contract takes a considerable amount of time. As soon as the MoD decides to contract out a project, an offer is placed on the international market (in accordance with international and national economical policy). Several consortiums formed for the project at hand can make their offers and propose original solutions. These consortiums usually consist of -at least- some banks, architects, contractors and logistical enterprises.

Usually, the process of selecting a consortium will be divided into several phases. First of all, consortiums have to give a presentation introducing their ideas and a scale model. The MoD will be especially interested in the extent to which the presented plans prove to be unique and in the originality of solutions to problems. Secondly, based on the price-to-quality ratio, a selection will be made. The presented plans have to fit within the MoD's pre-set financial boundaries. Eventually, the consortium that fits in best acquires the contract and starts production.

From the first phase of selection onwards, enterprises have to invest a lot of money in designing exact and real plans, thinking up and defining solutions and creating presentations and scale models. As the project develops, the civilian consortium will also be confronted with interest and exploitation costs. Besides, the consortium entirely finances the services it provides. This means, the stakes are high, which puts additional pressure on the process.

Not only are the stakes high to the consortia concerned, but the same applies to the MoD. Dealing with PFC contracts is completely new to us and we are relying heavily on our PFC-advisers. To decrease the transaction costs, the Ministry of Finance has decided to introduce PFC-knowledge. These specialized centers will act as consultants to assist governmental departments in their search for additional knowledge and expertise to exploit the governmental assets.”

**Do enterprises show a lot of interest in this new method?**

“In spite of the financial risks involved in taking part in the selection for a PFC project, enterprises are more than willing to take their chances. The MoD is a part of the government, so the consortium is almost certain of payback. Moreover, a public contract enhances the reputation of the enterprises within the consortium.”

**Does MOD already have a policy to deal with PFC?**

“There are many possibilities to acquire services outside the armed forces themselves. The idea is that you do not need to own the assets. Actually, we are forced to look for other ways to provide us with necessary services. Due to down-sizing, the armed forces can ill afford, for instance, the same level of in-company maintenance they used to have. Therefore, we are looking to cooperate with commercial and public partners to provide such services, which should be mutually beneficial. Possibilities are outsourcing, operational leasing or partnerships with other armed forces and PFC. PFC, therefore, is seen as just one of the possibilities, but certainly not the only one.

Let me give two more examples to illustrate the abovementioned. First, maintenance of military transport vehicles used to be done in Defense workshops, but not any more. For a period of 10 years, we have contracted a commercial firm to maintain the vehicles and train military personnel to be able to maintain the vehicles during operations. Secondly, another interesting development is the so-called “partnerships with other armed forces”. Within NATO, the European Union and the United Nations have decided to team up to find out whether their combined efforts may lead to less costly services. The best example in this field may be aircraft maintenance.”