

# ISSUEBRIEF

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**SMARTER ALLIANCE INITIATIVE**

## NATO Agency Reform, Done Right

NATO's forthcoming 2012 Summit in Chicago gives the Alliance's senior decision-makers the opportunity to assess the health of transatlantic relations and to tackle a set of overdue internal issues that have been long postponed due to more pressing operational issues in Afghanistan, Iraq, and then Libya. Chief among these issues is the matter of reforming NATO's own headquarters and its many and varied agencies. A careful reform effort, with a special focus on shared services, restructuring and integration, NATO's human capital, and the procurement and capabilities development structure and process, could pay significant dividends for the Alliance and ensure the more efficient use of already limited resources. While not a panacea, this would go a long way towards preparing the Alliance for future challenges.

### The Opportunity for Reform

The challenge of "NATO reform" is not nearly as straightforward as it might seem. While many of the issues may appear mundane and well beneath the notice of presidents and prime ministers, the Alliance should not miss the most significant opportunity to overhaul its critical infrastructure since moving to Belgium. If proper attention is paid, it can do this while improving the efficacy of one of NATO's most vital functions—armaments and technology collaboration. This is absolutely a topic deserving of attention from heads of state; even cursory attention to this matter will discipline the pre-Summit process (which always strives to leave nothing to chance) and force important focus on the topic.

The opportunity cannot be understated. NATO will move into a desperately needed new headquarters in Belgium in 2015. The military hospital, which was rapidly converted to

### The Smarter Alliance Initiative

This issue brief is part of the Atlantic Council's Smarter Alliance Initiative in partnership with IBM. The Atlantic Council and IBM established the Smarter Alliance Initiative in response to the NATO Secretary General's call for NATO members to adopt a "smart defense" approach to leveraging scarce defense resources to develop and sustain capabilities necessary to meet current and future security challenges in an age of austerity. Working with recognized experts and former senior officials from Europe and the United States, the Atlantic Council and IBM have produced a set of policy-oriented briefs focused on NATO reform and cyber security, with the aim to provide thought leadership and innovative policy-relevant solutions for NATO's continued organizational reform and role in cyber security.

The publications and their findings will be showcased at public and private events for the defense policy and NATO communities on both sides of the Atlantic in the run-up to the NATO Chicago Summit. The events will coincide with reform and policy development milestones established by the November 2010 NATO summit in Lisbon, Portugal.

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house the North Atlantic Council (NAC) in 1967, is dilapidated; NATO's international staff is in a valiant, but losing struggle to maintain a physical plant well beyond its intended life span, serving at over capacity as the Alliance has grown. In addition, the current headquarters is bereft of many business-enabling amenities expected from any modern headquarters, government or corporate. The new headquarters design is state-of-the-art; as far as buildings go, it will offer all of the potential inherent in modern architecture. But, just as when a family moves into a new home and has the chance to do serious housecleaning, the question for the Summit is whether NATO, as it moves across the street, will seize the opportunity to take with it only the very best of things, and leave behind all of those things that have become substandard by modern metrics.

## Shared Services

Current debate surrounding reform of the NATO agencies has touched on an important, but as-of-yet-untapped opportunity: use of shared services. This is a principle that NATO should understand at a root level, since it is core to the whole theory of the Alliance. But so far, both national representatives and the international staff appear at risk of missing a rare chance to overhaul the way business services are provided to the headquarters and its agencies. It makes little sense, in a world of collapsing defense budgets, and economies on the brink, for NATO to maintain multiple offices devoted to core "back office" support functions such as finance and accounting, procurement, human resources, legal services, and information technology. These activities are crucial enablers, but there are a range of best business practices that can and should be employed to reduce NATO's costs while improving the quality of support.

Forty plus years ago, the concept of shared services did not exist. Today, it is a mainstream business strategy that has repeatedly demonstrated its value to both governments and companies across the globe. There are decades of collective knowledge and experience that can be tapped to inform NATO's shared services effort. NATO urgently needs to minimize replicated processes, systems, and functions. Creating an Office of Shared Services (OSS) is a good first step, if it is based on a solid business case analysis, with a clear strategy, defined performance metrics, and unambiguous authority assigned by the North Atlantic Council (NAC). When done right, shared services are

proven to not only cut costs, but they also reduce complexity, improve oversight, and provide increased consistency in results.

## Restructuring and Integration

NATO's planned consolidation of agencies into three that are functionally organized along procurement, logistics, and C2 functions, is essentially a corporate restructuring. Generally, two forces dictate when and how a company must restructure—either in response to a specific event (such as a merger or acquisition, new regulation, disruptive technology, innovation, etc.) or in pursuit of improved financial performance. In this case, the motivation for NATO appears to be the latter.

If the goal is improved financial performance, NATO will benefit from working with business leaders who understand merger and acquisition (M&A) processes, and how to achieve stated business objectives. This is an inherently difficult challenge, even for experienced professionals. A number of studies suggest that over the past twenty years, nearly 75 percent of all major M&A deals failed to meet the value targets expressed to financial markets. Many of NATO's heads of state (as well as foreign and defense ministers) have significant corporate experience, and should intuitively grasp the importance of using leading business practices to drive agency consolidation. No corporate board or CEO would entrust a multi-million dollar merger and restructuring to personnel without requisite experience, nor should the NAC and secretary general. NATO should either bring the requisite experience "in-house," or should bring in outside professionals to jumpstart the organization's knowledge on how to drive the effort. Above all, a clear and balanced set of performance measures should highlight what the integration teams should focus on, measure, analyze, and report to stakeholders. An effective scorecard, required by the NAC, can help define success and keep the integration on track.

## Improving NATO's Human Capital

As reform proceeds, there is enormous potential to reshape the character and composition of the staff within these agencies and within the international staff more broadly. NATO has the opportunity to break with outdated and unaffordable employment policies, pay bands, and compensation packages by remapping against comparable positions in the private sector. Just as the US military

services have “throttled back” on recruitment and retention bonuses for servicemen when economic conditions made this unnecessary, NATO needs to fundamentally overhaul its human resource strategy. At the most simplistic level, top heavy management structures need replacing; certain A6 and A5 positions can be disbanded in favor of multiple, more junior A2s (and the rarely used A1 category). As was proven with the defense investment staff from 2003 to 2006, this can dramatically increase productivity while also radically altering staff demographics, bringing in younger talent, and creating opportunities for qualified citizens from newer NATO-allied countries to find jobs in a stratified marketplace.

## Procurement and Capabilities Development

Throughout this process, a critical lesson from M&A transactions needs to be observed – “protect and preserve” the key drivers of success while integrating everything else. Several NATO agencies are focused on defense procurement and technological collaboration. What should be protected at all costs is the overall capacity of the alliance to launch major new multinational capabilities. This is a point that appears to be lost on some. There is great risk to NATO if decision-making on multinational projects (i.e., efforts by a subgroup of NATO allies) is subordinated to cumbersome “at 28” procedures, requiring involvement of all allies. In the armaments world, almost nothing is ever done “at 28.” Disparities in size, budget, and national priorities often result in capabilities being developed by coalitions of the willing operating within the NATO framework.

The Alliance’s technological edge has been secured over the past sixty years because, among other things, NATO served as a hospitable environment where national armament directors could meet and agree to share financial burdens in pursuit of new capability, often in groups of three, four or five countries. Most of the largest examples of collective capability, such as the NATO Airborne Warning and Control System and the C-17s, do not have full participation by all allies. The great advantage of multinational programs is that smaller nations can access a capability, such as an AWACS or a C-17, which they could never afford on their own. Meanwhile, larger nations (that may have such capabilities organically in their militaries) are free to directly participate, or to contribute “in kind” as they see fit.

NATO’s acquisition community is at its best when nations honor the “pay to play” tradition and flexibility afforded by the Conference of National Armament Directors (CNAD), the assemblage of the top weapons development chiefs from across the Alliance. It can be at its worst when one nation tries to prevent others from cooperating by using “at 28” procedures to block progress, as was tried with the C-17 initiative at the NATO Maintenance and Supply Agency, and as was done recently to the fledgling Allied Ground Surveillance program. It is crucial that NATO not empower that type of behavior and inadvertently sacrifice the procedural flexibility that has historically typified defense investment programs. Often, when corporations restructure business segments, painstaking care is given to ensure the “voice of the customer” is not lost. Several of NATO’s agencies are procurement organizations such as the NATO Helicopter Management Agency which makes the NH-90 helicopter, and the NATO Eurofighter and Tornado Management Agency which oversees Eurofighter production. Their customer is not the secretary general, the North Atlantic Council, or even the Military Committee. Their customers are the individual national armament directors who decided to team with others and fund these organizations to develop military capability. For this reason, the decision by some nations to insist that NATO conduct more due diligence before trying to form a single integrated procurement agency is a positive development. By remanding this topic to the CNAD, they have given an important opportunity for the “voice of the customer” to be heard and understood.

At the same time, another customer’s voice deserving of attention is that of the military operator. In areas such as command, control, and communications (C3) and intelligence, surveillance, and reconnaissance (ISR) there is a need to overhaul ponderous acquisition processes. These are areas driven by fast-paced commercial innovation, and NATO’s current processes cannot keep up. These also are areas that often fall in the “no man’s land” between capabilities that nation’s are expected to provide, and those that NATO should commonly fund. The integration of the two main C3 and ISR service providers, NC3A and NCSA, should yield real benefits for the operator in terms of faster deployment of solutions, if the voice of the NCSA signal battalion operator is not lost in the process.

In the midst of any major commercial re-shuffle, customer concerns are sure to emerge. In the case of NATO reform,

one of the biggest management challenges will be reassuring stakeholders that their requirements will be met without interruption or interference by third parties. NATO's newly-joined entities should pay attention to this important issue, and address customer concerns and needs rapidly. At a minimum, because each of the three agencies will be a combination of three or more smaller entities, by the time day one of the integrated structure arrives, each should have a plan for how to market its expanded portfolio of products and services to its new larger, and perhaps unfamiliar, customer base.

But the most significant thing that the heads of state and government, as NATO's corporate board, could do at the Summit to ensure the continued feasibility of multinational armaments cooperation would be to roll out a new capability. Doing this will dispel growing suspicions that transatlantic armaments cooperation is moribund, and would stress-test the new structure to ensure that the ability to rapidly field new systems has been preserved. A concrete new capability is all the more urgently needed in light of Canada's withdrawal from the AWACS program, which has created significant political anxiety and financial challenges to NATO's oldest, and best known, symbol of multinational capability. There are many promising candidates for collaboration, but perhaps the most attractive is the well-developed initiative by the NATO special operations headquarters to field a multinational helicopter capability, perhaps with two squadrons of aviators flying a mix of European and North American aircraft. However, no matter what the capability is, as long

as it forces the new system to prove its responsiveness to national direction and interests, it will be an important Summit contribution.

## What Reform Can Achieve

Finally, it is critical that all involved parties manage their expectations, and that we be very clear what NATO reform will not achieve. Agency reform involving sharing of services across both the agencies and the international staff and international military staff will generate financial savings and simplify business operations. But it will not solve the underlying malaise that threatens the very health of the Alliance. If, at the Summit, heads of state and government limit themselves to emphasizing the importance of agency reform (or even take the step of announcing a set of capability initiatives), and don't shore up defense spending, or enforce the obligation of nations who bid on military posts to actually fill them, NATO will have done little more than treat the symptoms of the problem. The underlying disease is the failure by the vast majority of NATO allies to make adequate defense investments. Absent tangible demonstration of a renewed commitment to defense spending by three quarters of the allies, reform of NATO agencies largely just papers over the far more dire phenomena of a two-tiered Alliance, with a handful of nations serving as providers of security with the majority acting as pure consumers.

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