$125 BILLION IN SAVINGS IGNORED: REVIEW OF DOD'S EFFICIENCY STUDY

HEARING

BEFORE THE

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM HOUSE OF REPRESENTATIVES

ONE HUNDRED FIFTEENTH CONGRESS

FIRST SESSION

MARCH 21, 2017

Serial No. 115–19

Printed for the use of the Committee on Oversight and Government Reform

Available via the World Wide Web: http://www.fdsys.gov
http://oversight.house.gov

U.S. GOVERNMENT PUBLISHING OFFICE

26–498 PDF WASHINGTON : 2017

For sale by the Superintendent of Documents, U.S. Government Publishing Office
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$125 BILLION IN SAVINGS IGNORED: REVIEW OF DOD'S EFFICIENCY STUDY

Tuesday, March 21, 2017

HOUSE OF REPRESENTATIVES,
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM,
Washington, D.C.

The committee met, pursuant to call, at 10:25 a.m., in Room 2154, Rayburn House Office Building, Hon. Jason Chaffetz [chairman of the committee] presiding.

Present: Representatives Chaffetz, Duncan, Issa, Jordan, Amash, DesJarlais, Massie, Meadows, DeSantis, Walker, Blum, Hice, Russell, Grothman, Hurd, Palmer, Cummings, Maloney, Norton, Lynch, Connolly, Kelly, Lawrence, Watson Coleman, Plaskett, Demings, Krishnamoorthi, Raskin, Welch, DeSaulnier, and Sarbanes.

Chairman CHAFFETZ. The Committee on Oversight and Government Reform will come to order.

And, without objection, the chair is authorized to declare a recess at any time. I appreciate you all being here. We have an important topic today to talk about the potential of $125 billion in savings that has been ignored, and we're going to have a discussion about the review of the Department of Defense's efficiency study.

On December 5th of 2016, The Washington Post reported on a Department of Defense study that found the Pentagon could potentially save $125 billion over 5 years on back-office, noncombat expenses. The Post's story detailed the desire of DOD leadership to squelch the findings of the Defense Business Board—sometimes referred to as the DBB, but the Defense Business Board—for fear that the Congress would ultimately end up cutting their budget. That is the concern.

The DBB is an advisory board commissioned by the Pentagon to provide independent advice and recommendations with regard to governance and management at the Department of Defense. For the study, the Defense Business Board was charged with finding savings the Pentagon could recapitalize into more troops, more ships, and more planes. Enlisting the management consulting firm of McKinsey & Company, one of the premier consulting companies we have in this country, the DBB spent months analyzing the Pentagon's business systems and back-office operations. The result of the report concluded the Department of Defense could save billions from overhauling its back-office functions, including contract management, IT, business processes, real estate, and human resource management. The savings could be reinvested to better equip our men and women in uniform. But the Department of Defense leadership squelched the report.

In response to the Post's story, 31 members of this committee from both sides of the aisle signed a letter to then-Secretary Carter asking for answers.

With the change in administration, the urgent need for reform at the Pentagon has not changed. There are a number of statistics that tend to support the DBB's recommendation for rigorous oversight. First, the Pentagon continues to expand its use of contractors. From 2001 to 2015, the Department of Defense increased the number of civilian employees by roughly 14 percent. Compared to our men and women in uniform, government contractors are less likely to be subject to oversight of the Pentagon. Some of the government's most effective tools for holding its employees accountable are not available when it comes to contractors.

Second, the Pentagon study noted the potential $125 billion savings could fund 50 Army brigades or 10 Navy carrier strike group deployments or 83 Air Force F–35 fighter wings. So, while our troops are engaging the enemy in Iraq and Syria and patrolling the South China Sea and really helping make sure that this world and the United States is a safe place, the Pentagon is resistant to back-office cuts that would better fund and equip these men and women who are doing the hard work on the front lines.

Given how dangerous our world is, we really, truly have to get this right. And if we're going to ensure our troops are the best equipped possible, it is our responsibility to oversee how this money is expended. It is a lot of money. It is the single biggest line item in our discretionary spending budget.

The Constitution delegates the Congress the role of providing the training and equipment of the Army and to, quote, "maintain a navy," end quote. It is our job to make sure that our warfighters are getting all the support that they need to do their jobs. We have a very astute panel, and we look forward to having discussions with them about this report and what can be done to save money at the Pentagon.

With that, I will yield my time back, and I now recognize the ranking member, Mr. Cummings.

Mr. CUMMINGS. Thank you very much, Mr. Chairman, for holding this critical hearing today. The Department of Defense is charged with the most serious mission there is: Protecting and defending every man, woman, child in our country. In this dangerous world, the readiness of our warfighters is essential to national security, and Congress has a duty to provide our military with all the necessary resources.

However, we also have a duty to ensure that every taxpayer's dollar is put to its most effective and efficient use. Every dollar that is squandered through waste, duplication, or fraud is a dollar not available for military training, advanced weaponry, and salaries and benefits for our uniformed and non-uniformed personnel. It is also a dollar we do not have for critical domestic programs like education, job training, and feeding the poor.

In January 2015, the Defense Business Board, a panel that provides management advice from a private sector perspective, issued a study finding, and I quote, "a clear path to saving over $125 billion in the next 5 years," end of quote. Last December, a Washington Post story written by Bob Woodward and his colleagues reported allegations that Pentagon leadership deliberately buried the study amid fears that Congress might reduce the defense budget.

On December 8, all committee Democrats and 31 total committee members signed a bipartisan letter requesting information about this report and these allegations. The Defense Department disputes the amount in the report, the $125 billion over 5 years, but nobody disputes that the Defense Department could save billions of dollars by streamlining the way it conducts business.

Senator John McCain and Representative Mac Thornberry, chairmen of the Senate and House Armed Services Committees, issued the following joint statement on the study, and I quote: "The Defense Business Board's key findings, that the Department of Defense could save as much as $125 billion over 5 years by limiting unnecessary back-office bureaucracy, are not a surprise," end of quote.

Nor are the problems identified by the Board new. We have known for many years that the Department's business practices are archaic and wasteful, and this inability to pass a clean audit is a longstanding travesty. In the United States of America, we have one department that just cannot get through an audit. That is amazing. This is also not new to this committee. We have done years of work examining wasteful spending at the Defense Department. Just last month, the Comptroller General of the United States testified before us that, and I quote, "probably a third of the areas on the high-risk list are DOD business management practices," end of quote.

The Defense Department is the only Federal agency that has never—never—passed an independent audit. I wonder if they're spending too much money to be able to do an audit. And then we hear that the President wants another $54 billion, and here we have a report that says we can save $125 billion in 5 years.

But President Trump's new budget ignores all of this. He proposes boosting defense spending by billions and billions of dollars. He proposes funding this increase by slashing dozen of programs that promote our national security and our Nation's most vulnerable communities, the elderly, children, and the rural working class. The President would slash funding for the State Department and the U.S. Agency for International Development, reducing contributions for U.N. peacekeeping, the International Atomic Energy Agency that monitors Iran's compliance with the nuclear agreement, and the World Bank's antipoverty programs. The President would decimate foreign aid for humanitarian efforts in Iraq, Afghanistan, and Nepal, as well as antidrug trafficking efforts in Latin America.

Last month, more than 120 former generals signed a letter to Congress warning, and I quote, "the State Department, USAID, Millennium Challenge Corporation, Peace Corps, and other development agencies are critical to preventing conflict and reducing the need to put our men and women in uniform in harm's way."

In 2013, Defense Secretary James Mattis, who was then serving as the Commander of CENTCOM, testified, and I quote: "If you don't fully fund the State Department, I need to buy more ammunition ultimately. The more that we put into the State Department's diplomacy, hopefully the less we have to put into a military budget," end of quote.

The President's budget also weakens our maritime, border, and airport security by redirecting billions of dollars from the Coast Guard and TSA to constructing an outrageously expensive wall on the border with Mexico. But to me, the most disturbing cuts are to critical, domestic programs. The President would eliminate Community Development Block Grants, which fund antipoverty programs like Meals on Wheels, which feeds approximately 2.4 million of our elderly citizens, veterans, and other homebound individuals every year. The President would also eliminate funding for the 21st Century Community Learning Centers, which helps fund afterschool programs, serving more than 1.6 million children across the country, many of them in low-income neighborhoods. The President's budget does not effectively serve our national security interests, nor does it serve the interests of the everyday American family.

The United States must invest in a strong national defense to face our global challenges. This means not just spending more, but spending wisely. So I want to thank all of the witnesses for being with us today and for their valuable contributions toward improving the Defense Department's effectiveness and the national security of all of our Americans.

With that, I yield back.

Chairman CHAFFETZ. The gentleman yields back.

I will hold the record open for 5 legislative days for any members who wish to submit a written statement.

We'll now recognize our panel of witnesses.

We're pleased to welcome Mr. David Tillotson III, Acting Deputy Chief Management Officer, from the United States Department of Defense; Mr. Scott Rutherford, senior partner at McKinsey & Company; Mr. Michael Bayer, current chairman of the Defense Business Board; Mr. Robert Stein, former chairman of the Defense Business Board; Mr. Kenneth Klepper, former board member of the Defense Business Board; and the Honorable Lawrence Korb, senior fellow at the Center for American Progress.

We thank you all. Pursuant to committee rules, all witnesses are to be sworn before they testify. So if you will please rise and raise your right hand.

Do you solemnly swear or affirm that the testimony you are about to give will be the truth, the whole truth, and nothing but the truth, so help you God?

Thank you. You may be seated.

Let the record reflect that all the witnesses answered in the affirmative.

Mr. Tillotson, we will start with you, and we will go right on down the line. You'll each be recognized for 5 minutes. If you'd please limit your testimony to those 5 minutes so members have a chance to ask you questions. We have a big panel today. Your entire written statement and any attachments will be made part of the official record.

Mr. Tillotson, you are now recognized for 5 minutes.

WITNESS STATEMENTS

STATEMENT OF DAVID TILLOTSON III

Mr. TILLOTSON. Thank you, Mr. Chairman, Ranking Member, members of the committee. As my written statement will be entered into the record, I will keep my remarks brief in the interest of giving you time to ask whatever questions the committee chooses to ask. I will say a couple of things very quickly, however.

I think the one thing that I would take unequivocal issue with is that the report was in any way suppressed. It was actively discussed within the Department at the time. It has formed the basis of discussion since that time. It was posted in the public record. It was actually discussed with Members of the House and Senate back in 2015, shortly after it was issued, albeit not with this committee, but with the HASC and SASC. So the fact is this has not been suppressed.

The actions that led to the results of the DBB report, among other things, were actually kicked off by the current Deputy Secretary of Defense acting through my office. Two actions were taken: One, we initiated a contract through the DCMO office to Ryan Consulting to do some work on understanding where the costs of the Department rested in terms of back-shop activity. So this was a deliberate attempt on the part of the Department to, in fact, identify the opportunity space, not associate with the—directly associated with Defense Business Board. Ryan Consulting in turn subcontracted to McKinsey. So that's the relationship to that company.

The second activity was that the Deputy Secretary chartered the Defense Business Board at the time to do a corporate-style review, looking at the information generated by McKinsey and coming up with recommendations about how the Department might proceed to address opportunities generated by whatever the cost opportunities presented us. So those were the actions that were taken.

The question about moving forward on efficiencies is hardly new to the Department. Secretary Gates led a significant efficiency initiative that resulted in multiple billions of dollars repurposed within the Department. Secretary Hagel continued that tradition. Secretary Carter continues to do so.

After the study was published, several things got addressed. There were two concrete areas for recommendations in the report and a third recommendation that basically said: Go do some more homework. We acted on the two concrete recommendations, which were to address some IT efficiencies. We have not gone as far as the report would suggest we could. I agree with that. We also pushed ahead on some services' contract reviews, particularly on the OSD staff, the Defense Agencies and Field Activities, an area where, candidly, not as much attention had been rendered as needed to have been done in the past. When we look at the result of those sets of actions, that added an additional $7.9 billion in efficiencies to an already double-digit billions of efficiencies that we had put in place in prior years.

Having said all that, there is more to do. There is ample opportunity. The DBB report, the supporting McKinsey material would suggest there are things we can do.

There are two challenges to moving forward. I will be candid about both. There is an internal challenge. That's our job. We will go fight those battles. We have to have those discussions internal to the Department, and in some instances, we are assisted by actions on the Hill. So, in the most recent National Defense Authorization bill, in 2017, there was a very specific requirement for us to redirect and look at the management of the medical community in the Department of Defense. We agree from the DCMO's office that that is worth looking at. We certainly would endorse moving forward with that, and we appreciate the support of Congress in doing that.

Having said that, "efficiencies" means we take a look at moving money and activities from current activities into new activities. One of the areas that both the GAO and the DBB report and independent DBB reports have all pointed at is our use of leased property and owned real property. It's intriguing to me that, when we opt to let a lease contract for a building lapse—not terminate it, let the contract run out—that we spend three trips to a State delegation explaining why we can't close that contract. So I'm prepared and the Department is prepared to work on this going forward.

Mr. Korb in a recent article has suggested five steps that the Department should build on, including build on the DBB report. We agree. But his fifth recommendation is a recommendation the Department brings forward with regularity and which, candidly, at least one member of this committee in a prior testimony has asked me if we thought we needed, and that is, do we need a BRAC? And the answer is yes. So there are actions that we need to take, working in conjunction with Congress. By the way, BRAC is not the only action. I'm going to say that right now. It is not the only thing we should do. Thank you for your time, Mr. Chairman.

[Prepared statement of Mr. Tillotson follows:]

Statement of

David Tillotson III
Acting Deputy Chief Management Officer
Department of Defense

before the

House Oversight and Government Reform Committee

On

"Findings of the Defense Business Board Study 'Transforming DoD's Core Business Processes for Revolutionary Change'"

March 21, 2017

Good afternoon Chairman Chaffetz, Ranking Member Cummings, and Members of the Committee. Thank you for this opportunity to discuss the Department's progress in addressing institutional reform and improved business practices and, specifically, to address the January 2015 Defense Business Board (DBB) study related to transforming core business processes within the Department.

My name is David Tillotson, and I am the Acting Deputy Chief Management Officer (ADCMO) of the Department of Defense (DoD). Shortly after reporting to Deputy Secretary Work in 2014, the Deputy Secretary (in his role as the Department's Chief Management Officer) met with me and the DoD Chief Information Officer to revitalize work in reforming the Department's business practices and to put forward recommendations that would help free up funding to meet emerging needs in the current budget-constrained environment. He asked the CIO and me to initially focus on the OSD staff and Defense Agencies/Field Activities, but also wanted to establish a foundation for broader Defense reforms. To that end, my office put in place a contract to assess the opportunity space for broader reforms in terms of both functions and resources. The Deputy Secretary of Defense also turned to private sector advice through the use of discretionary, Federal Advisory Committee Act (FACA) committees, in this case the DBB. The DBB, established in 2002, is composed of private citizens with significant business experience, who volunteer their time to provide the Secretary and Deputy Secretary of Defense with independent advice on private sector best business practices for consideration and potential application to the Department. On October 15, 2014, the Deputy Secretary of Defense established a task group under the DBB to help determine the extent to which the Department could find opportunities for improved productivity and associated savings by applying applicable corporate business practices to the core business functions within the Department.

On January 22, 2015, the DBB task group's recommendations ("the 77-page summary report" referred to in the Washington Post article) were presented at a publicly-noticed meeting of the DBB[1] which was covered by the media.[2] Consistent with FACA, it has been (and remains) publicly available since that time on the DBB website and has been accessed over 2800 times.[3] Additionally, the report was widely socialized with Department leadership and external stakeholders. For example, in February 2015, task group members discussed the Board's findings with professional staff members (PSMs) of the Senate Armed Services Committee (SASC). That same month, I discussed it with both SASC and House Armed Services Committee PSMs.

On December 5, 2016, *The Washington Post* published an article by Craig Whitlock and Bob Woodward titled "Pentagon buries evidence of $125 billion in bureaucratic waste", citing the January 2015 DBB "77-page summary report". The article both misrepresented the details of the study and mischaracterized the Department's response to the study's recommendations.

First, *The Washington Post* article's headline and its accompanying graphic implied that $125 billion could be cut from the annual defense budget. This mischaracterized the potential savings as "waste" and misled its readers by presenting the potential savings as 23% of the Department's

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[1] Meeting Notice, 79 Fed. Reg. 76991(December 23, 2014).
[2] Press coverage of the DBB presentation included: (1) https://insidedefense.com/daily-news/dbb-pentagon-could-save-125b-early-retirements-contractor-reductions, and (2) http://www.defensenews.com/story/defense/policy-budget/budget/2015/01/23/pentagon-budget-defense-savings-dbb-work-modernize-retirement-retrain/22214201/.
[3] The report is available at http://dbb.defense.gov/Portals/35/Documents/Meetings/2015/2015-01/CBP%20Task%20Group%20Out-brief%20Slides_FINAL.pdf. The "77-page summary report" referenced is the full and complete report. The 77-page slide deck was bound and printed with the addition of the following sections:

1) Cover letter from the DBB Chair to the Secretary of Defense (SD) and Deputy Secretary of Defense (DSD) – dated February 9, 2015
2) Table of Contents
3) Terms of Reference (the memo from DSD directing the DBB to conduct the study)
4) Executive Summary (27 slides from of the 77-page slide deck)
5) 77-page summary report
6) Task group biographies
7) List of acronyms
8) Bibliography
9) List of DBB members

annual budget, when the study's projections were across the FYDP. Six days after the article, *The Washington Post* published an opinion[4] piece which acknowledged its misrepresentation of savings as waste and corrected the savings accumulation as FYDP versus annual. As acknowledged in the opinion piece, "... the plausible cuts are closer to 4 percent ..." Unfortunately, the opinion piece was not nearly as sensational as the original article.

Second, the task group applied assumptions to arrive at 4% based on corporate business processes that did not account for the realities of the Federal budgeting process, including the annual budget review cycle that takes place across the Executive Branch and with Congress. The assumptions also did not account for various requirements in law affecting major budget and resource reallocation decisions, personnel, and organizational changes. Further, the savings projections assumed the Department could apply changes additively to ongoing initiatives so that the next round of reforms would result in cumulative reductions. While the DBB's assumptions and recommendations provide insight into what might be possible based on private sector modeling and experience, we know the private sector benchmark is one we might not reach. However, the DBB study's recommendations and the data exercise conducted by my office identified for the Department a structured approach to defense reform, and identified the need for additional work.

One of the immediate insights gained from the DCMO data work that supported the DBB effort was the need to have comprehensive, accurate, and available data on our core enterprise-wide business related functions. The task group looked at the number of personnel and budget resources dedicated to core enterprise-wide business functions, and elicited advice from senior business leaders on alternative ways to look at how the Department conducts its business. They

[4] https://www.washingtonpost.com/opinions/just-cutting-waste-at-the-pentagon-wont-cut-it/2016/12/11/8e16a61e-be45-11e6-91ee-1adddfe36cbe_story.html?utm_term=.4c36365928b1

did not identify specific systems or processes that should be changed to increase the Department's productivity levels. Instead, the study identified metrics and benchmark levels that could be seen as efficiency goals for the Department based upon similar private sector goals. My office used the data and information collected by the task group, and its subsequent recommendations, to look into opportunities for actionable streamlining and efficiency actions. More specifically, the Deputy Secretary of Defense leveraged the recommendations to inform his approach to business process optimization and reform. I would like to share four examples of how the study's recommendations assisted in the development of specific efficiencies.

First, based upon the Deputy Secretary's 2014 direction, my office has been conducting Business Process and Systems Reviews (BPSRs) along organizational lines to identify potential efficiency initiatives. The task group focused instead on six core lines of business within the Department: human resources management, health care management, financial flow management, supply chain and logistics, acquisition and procurement, and real property management. Capitalizing on the core business concept, the Department added two (2) additional lines of business: Defense Resale and Information Technology. By using this focus on core lines of business rather than organizations, the Department has improved select business practices which will result in cost savings over the next 8 years.

Second, while not a specific recommendation from this study, the Department has adopted a comprehensive new definition of DoD major headquarters activities (MHA), which was subsequently codified in the FY 2016 NDAA, and the Department is working to ensure that MHA data is incorporated into authoritative data systems to increase information fidelity for accounting, tracking, and reporting. The new definition and revised baselines are being built into programming and budget elements, enabling the Department to track headquarters costs consistently across organizations and over time; this was a broad data issue identified and thus validated by the DBB review effort.

A third efficiency effort, which was informed by the study's recommendations on Contract Optimization, was the application of the practices similar to those in place in the Military Departments to review the requirements for, and assess potential redundancies of, service contracts supporting the OSD and DA/FAs. This process, known as Service Requirements Review Boards (SRRBs), is aimed at validating requirements and streamlining contracts. The SRRBs require organizations to review their service contract requirements and find opportunities for efficiency by eliminating non-value-added services and duplicative requirements, better aligning requirements to mission, and using strategic sourcing opportunities. Savings can be realized over the FYDP and available to re-invest into higher priority requirements. My office is currently estimating that the Department can save $1.9 billion across the FYDP through the use of SRRBs.

As a final example, the DBB study recommended a focus on IT efficiencies. With the DoD CIO as the lead, we are conducting a dedicated review of the IT needs and assets of the Department to provide better service and integrated approaches across all mission areas. This approach consists of a top-down/bottom-up review of all IT enterprise licensing agreements to ensure the Department is obtaining software and hardware at a consistent cost; the consolidation and potential reduction of data centers as a means of focusing the Department's infrastructure support in a few targets areas versus multiple, underutilized locations; and the consolidation of disparate and redundant IT networks into a single Joint Service Provider approach. At present, the

Department is on track to reach its efficiency target of $1.9 billion by FY 2021.

These are just a few of the efficiencies the Department is pursuing that have been informed by the DBB study. The Department is also preparing for horizontal, cross-component reforms that should yield additional savings and may allow the Department to see potential savings similar to comparable private sector metrics and benchmarks. Such changes will require support from Congress and many will be sensitive and difficult because of the potential impact on jobs and resources. These new initiatives will consider divesting work the Department does not need to do, changing information practices to make better Department-wide decisions about resource use, and changing organization structures to perform at an enterprise level.

Mr. Chairman, the Department is firmly committed to continuing efforts to improve our management practices and business processes. The Department has always taken its duty to be an excellent steward of taxpayer dollars very seriously. I thank the Chairman, Ranking Member and the Committee for the opportunity to address misunderstandings associated with the DBB's Core Business Process study and to provide tangible examples of the Department's accomplishments to date. This concludes my prepared remarks and I defer to the Chairman for further questions.

Chairman CHAFFETZ. Thank you.

Mr. Rutherford, you're now recognized for 5 minutes.

STATEMENT OF SCOTT RUTHERFORD

Mr. RUTHERFORD. Chairman Chaffetz, Ranking Member Cummings, and members of the committee, my name is Scott Rutherford. I'm a senior partner at McKinsey & Company, and I'm the managing partner of the Washington, D.C., office. I'm pleased to be here today to discuss McKinsey's work for the Department of Defense under contract with the Department's Deputy Chief Management Officer.

From the fall of 2014 to the spring of 2015, we were engaged by the Department to conduct a comprehensive assessment of its spending in six core business functions: human resource management; healthcare management; financial flow management; logistics and supply chain; acquisitions and procurement; and real property management.

Our work began with the development of what we called a cost baseline, which assembled data on existing spending across the entire Department in these six areas. To our knowledge, that kind of crosscutting analysis of back-office spending at the DOD had never before been conducted. McKinsey's work has since been used by the Department in a number of important ways.

First, the Deputy Chief Management Officer shared our baseline with the DBB, and that baseline was used by the Defense Business Board in its own analysis and report released in January 2015. Although the McKinsey baseline was a starting point for the DBB's efforts—and McKinsey is one of many inputs into their approach—the projections, assumptions, and analysis of the potential cost savings were those of the DBB.

Second, McKinsey's work for the DOD continued using the cost baseline into what we would call benchmarking, which compares the Department against other large companies, and roughsizing, which began the process of estimating the magnitude of the savings that might be achieved in different categories.

So, in May of 2015, McKinsey estimated that the Department could achieve about $4 to $5 billion in new savings per year over a 5-year period across the six functional areas we examined. That translates into cumulative savings of between $62 billion and $84 billion over a 5-year period.

Third, it's our understanding that the Department has used our baseline, our benchmarks, and our cost savings estimates to implement changes on its own that are generating actual cost savings. The projected cost savings we identified are somewhat different than those estimated by the DBB's January 2015 report because, while both estimates started with the McKinsey baseline, McKinsey had the benefit of working collaboratively with the DOD, allowing us to drill down further and do additional analytic work for a couple months afterwards. Based on that work, we also assumed a somewhat slower pace of change than the DBB assumed. This resulted in a lower estimate of how much savings could be achieved over the first 5 years relative to the DBB's projections.

We're very proud of our work. We have been helping private sector and government agencies identify opportunities to reduce costs for many years and have accumulated a body of proprietary databases and methodologies that allow us to bring that experience to bear in very concrete ways. And in this case, we provided the Department with a set of tools and approaches to move forward on realizing cost savings opportunities, and we believe the Department's potential return on that investment it made in our effort is substantial.

Thank you for the opportunity to be here today, and I'm happy to answer any questions you might have.

[Prepared statement of Mr. Rutherford follows:]

McKinsey&Company

Statement of
Scott Rutherford
Senior Partner, McKinsey & Company
before the
Committee on Oversight and Government Reform
U.S. House of Representatives

March 21, 2017

Chairman Chaffetz, Ranking Member Cummings, and Members of the Committee, I am pleased to appear before you today to discuss McKinsey's work for the Department of Defense, and our work with the Department's Deputy Chief Management Officer to evaluate the Department's spending on core business processes.

In the fall of 2014, McKinsey was engaged by the Department of Defense to conduct a comprehensive assessment of the Department's spending in six core business areas. From the fall of 2014 through the spring of 2015, a team of McKinsey consultants developed a detailed compilation of the Department's spending in these areas, assessed the overall potential for cost savings in these areas, and conducted two targeted proofs of concept to demonstrate an approach to achieving savings in services contracts. We are very proud of this work, and we continue to believe that the Department of Defense and the public sector can benefit from McKinsey's unique skills, developed through decades of private sector experiences, in evaluating organizational efficiencies with a goal of reducing costs.

Our work with the Department began with the development of a cost "baseline" that assembled data on spending across the entire Department in six important areas: human resource management; healthcare management; financial flow management; logistics and supply chain; acquisitions and procurement; and real property management. The McKinsey baseline was, we believe, a more comprehensive look at spending in these areas than previously existed.

The McKinsey baseline has been important to the Department's cost cutting efforts in a number of important ways:

First, the Deputy Chief Management Officer shared McKinsey's baseline with the Defense Business Board, and the baseline was used by the Board in its own analysis and report, released in January 2015, which estimated $125 billion in potential cost savings over five years. Importantly, although McKinsey's baseline was used by the Board as the baseline for its effort, the projections, assumptions, and analysis related to potential cost savings are those of the Board, not McKinsey.

Second, under the Deputy Chief Management Officer project, McKinsey's work continued into the areas of "benchmarking," to compare the Department to other large enterprises and identify potential areas for savings, and "roughsizing," where we began the processes of estimating the savings that might be achieved. At the end of that process, which extended to May of 2015, McKinsey's roughsizing analysis estimated that the Department could achieve savings between $62 billion and $84 billion over the five years between 2015 and 2020.

Third, we understand, from informal conversations with the Department since concluding our work in 2015, that the Department has used our baseline, benchmarks, and cost savings estimates to implement changes that have put them on the path to generating actual cost savings.

Mr. Chairman, I would like to focus for a moment on the different cost savings estimated by the Defense Business Board in its January 2015 report, and the cost savings estimated by McKinsey in its work delivered to the Deputy Chief Management Officer in May 2015. Given that both estimates were based on the McKinsey baseline, it may seem strange that the Defense Business Board estimated $125 billion in savings over five years, and McKinsey estimated between $62 billion and $84 billion over five years.

There are two primary factors that underlie this difference:

First, from reviewing the Defense Business Board's report, I understand that its cost savings estimates were based on metrics of productivity improvements that have been observed and achieved in past cost savings efforts, primarily in the private sector. This is understandable and appropriate given the Board's role – it was created to give the Department advice that reflects a private sector perspective on effective best business practices. Although McKinsey's process similarly included benchmarking against existing metrics, we had the additional benefit of several months more work within the Department, where we performed additional analytical work that informed our projections, particularly with respect to the pace of achievable change.

Second, specifically regarding that pace of change, the differences between the Board's projection and McKinsey's projection are largely driven by the projected pace of change. Because both projections encompass a five year period, a total savings projection is highly sensitive to savings predicted in the early years. For example, if a projection includes an estimate of a large saving in the first year – which would accrue again in year two, three, four, and five because it has been achieved – the total cumulative savings over the five year period can be significantly higher than if the estimated initial savings are more modest.

Finally, it is important to distinguish between the cumulative cost savings and the reduction to the amount that the Department spends on these costs in any given year. McKinsey's projection of $62 billion in savings, for example, was based on a projected reduction in annual spending of about $4 billion each year. Over five years, the annual spending in that scenario would reduce from $134 billion (in 2015) to $113 billion (in 2020).

McKinsey & Company

McKinsey is a global firm that, for almost 100 years, has helped leading businesses, nonprofits, governments, and others achieve their most important goals. We have more than 10,000 consultants and experts, along with about 2,000 research and information specialists working across the globe. Our people include doctors, business managers, engineers, research scientists, civil servants, and entrepreneurs. We focus on high-value consulting, supporting organizations' most high-value, high-risk, and complex priorities for organizational change.

McKinsey takes a team-based approach to our projects. When we are engaged, we identify a team to work on the project and identify an estimated timeframe for completion. In addition to the teams assigned to the project and the partners leading the effort, our clients have access to our worldwide network of experts and support staff and to our proprietary knowledge, tools, and analyses on which we invest more than $400 million annually. McKinsey contracts with clients for a firm fixed price – we do not bill by the hour.

McKinsey is recognized for its leadership and expertise. We are thought leaders in both the public and private sector. Our consultants often help organizations identify problems and provide input on options for solving them, including sharing best practices and possible approaches. We also frequently publicize our views. For half a century, we have published the McKinsey Quarterly, which sets the agenda for top global managers. We also publish materials specific to key sectors, such as McKinsey on Government, McKinsey on Defense, and others. We operate the McKinsey Global Institute, a business and economics think tank, and McKinsey Center for Government, a global hub for research, collaboration, and innovation in government performance.

McKinsey has served the U.S. government for many years, and we founded our firm's U.S. government-serving entity about a decade ago, specifically focused on serving the U.S. public sector. As with our private clients, our public sector practice focuses on solving the big problems. In serving our public sector clients, we use our proprietary research, tools, and approaches as well. For example, the McKinsey Center for Government performs independent research on management in the public sector that we can apply in our public sector work.

McKinsey's Approach to Cost Savings Studies

One of McKinsey's key strengths is conducting cost savings studies. For both private and public sector clients, we apply a series of phases for cost savings studies. A McKinsey cost savings project can encompass some or all of the phases, as determined by the client. Our contract with the Defense Department covered phases one through three.

Phase one is "baselining." The baseline is the starting point for a cost savings analysis. McKinsey works closely with the client and the client's data to determine the types and amounts of costs that currently exist. Baselining includes analyzing the costs, resources, and assets that are responsible for delivering a particular function or capability. For some clients baselining can be simple and straightforward; for others, such as the Department of Defense, it is highly complex and more challenging.

Phase two is "benchmarking." In benchmarking, McKinsey compares the client's efficiency and effectiveness to other relevant businesses or industries, to McKinsey's view of the best practices, and the client's internal organizations. McKinsey's proprietary processes and databases add significant value because they reflect years of institutional knowledge and experiences. Frequently, McKinsey's broader view across a variety of industries is unique and not replicable from other sources.

Phase three is "roughsizing." In this phase, McKinsey develops a high level estimate of the savings that may be possible. In broad strokes, this estimate reflects the difference between the existing actual costs (quantified in the baseline) and the best practices in the applicable area or industry (developed in the benchmarks). Roughsizing results in high level estimated savings, and it gives an organization the ability to quantify the potential and prioritize the actual cost savings initiatives to be pursued. Roughsizing may also include conducting some targeted proofs of concept to validate the opportunities and refine the savings estimate.

Phases four and five, which the Department of Defense did not ask McKinsey to perform (as it was not in the contract), would have involved the development of a specific set of recommendations of cost savings initiatives to pursue to achieve the estimated savings, and the implementation of those initiatives to achieve actual cost savings, respectively.

Contract with the Department of Defense

In September 2014, McKinsey and Ryan Consulting entered into discussions about subcontracting under Ryan on a project of the Department of Defense's Deputy Chief Management Officer to conduct a core business process cost evaluation.

Earlier, in August 2014, members of the Defense Business Board who were familiar with McKinsey's expertise in cost savings studies had asked McKinsey for perspectives on conducting a cost savings analysis of the Department's core business activities. McKinsey provided perspectives on best practices in the industry concerning cost savings studies.

McKinsey's work with the Department of Defense provided for phases one and two (baselining and benchmarking) and an option for phase three (roughsizing). McKinsey performed this contract, with Ryan as the project manager, using our GSA-approved MOBIS rates ($2,734,227.05 for phases one and two, and $5,693,323.45 for phase 3, following the exercise of the option).

McKinsey conducted phase one from approximately October 2014 to January 2015. McKinsey delivered its final results for this phase in January 2015, identifying a baseline of more than $130 billion in annual costs, including $40 billion in contracted services, $45 billion in civilian salaries, $29 billion in military salaries, $11 billion in contracted goods, and $7 billion in information technology. This baseline included costs associated with more than 260,000 contractors and about 450,000 civilians.

McKinsey conducted phase two, which developed the benchmarks, primarily in January 2015. Benchmarking an institution as unique as the Department of Defense is very challenging. In some cases, McKinsey recommended that the Department benchmark against its own productivity metrics, particularly in areas where no private sector comparison is possible. Additionally, McKinsey excluded some portions of the baseline from the benchmarking because we could find no reasonable analogs to those spend categories in the public or private sectors.

In February 2015, the Department exercised the option for phase three, and McKinsey began work on the roughsizing process to estimate potential savings. McKinsey delivered the results of this phase in May 2015, which estimated potential savings in a range of $62 billion to $84 billion over five years. McKinsey also provided two targeted proofs of concept to demonstrate the approach and offered perspectives on approaches to further phases designed to achieve the potential savings. The Department did not extend the contract for these purposes.

Defense Business Board

In the early parts of McKinsey's work for the Department of Defense under the contract, the Deputy Chief Management Officer requested that McKinsey keep the Defense Business Board apprised of our baselining efforts. At the request of the Secretary of Defense, the Board was conducting its own cost savings study. We understand that the results of McKinsey's development of a baseline was shared with the Board, and the McKinsey baseline is thus also the baseline underlying the Board's report on projected savings, which it issued in January 2015.

As noted in the Board's report, the Board interviewed dozens of current or former military leaders, civilian leaders, and others familiar with cost savings efforts, such as private sector leaders, academics, and think tanks. In this context, McKinsey also provided the Board with its perspectives on best practices and advice concerning cost savings models.

The Board's report reflected its own analysis and projections regarding the potential for cost savings. The Board delivered its report in January 2015, and McKinsey continued with phases two and three of our work for the Department through May of 2015.

* * *

Mr. Chairman, thank you for the opportunity to appear before you today, and I would be happy to answer any questions that you or the Committee Members have for me.

Chairman CHAFFETZ. Thank you. I appreciate it.

Mr. Bayer, you're recognized for 5 minutes.

STATEMENT OF MICHAEL BAYER

Mr. BAYER. Thank you, and good morning, Chairman Chaffetz and Ranking Minority Member Cummings and members of the committee.

My last engagement with this committee was many years ago when my then-boss, Bud Brown, was the ranking minority member of the then-named Government Operations Committee. But today I appear before you as the fifth chairman of the Defense Business Board.

As are all the members of the Business Board, I am a private citizen, not a paid government employee. We all volunteer our time to serve the Department of Defense by offering our collective advice on how to manage the Department more efficiently in order to enable the Secretary and the Deputy Secretary to maximize the allocation of scarce resources for the warfighter.

The men and women of the Business Board and its sister advisory boards, Policy and Science, who donate their time and energy to help the Department, each consider it a tremendous honor and a great responsibility.

As I've communicated to you and your staff, I have no direct knowledge about the effort at hand. My first meeting after returning as chairman of the Defense Business Board was in July of 2015, more than 6 months after this study had ended and its presentation publicly in January of that year. As this was under the direction of a previous chairman and long before I became chair, I have no particular insight or access into the actions and decisions made about how this effort was conducted or delivered.

I can say in the year and a half since I became chairman, the board has been very busy. It has completed eight studies, and our most recent effort, "Focusing a Transition," was a product of every member of the board, of the Defense Business Board, and it was very well received by the Department's leadership at the time and the incoming leadership of Secretary Mattis' team.

But there is more work to be done in the months and years ahead as we all strive to support Secretary Mattis' priorities, particularly his third, and I quote, "bringing business reforms to the Department of Defense," which we believe are essential for his ability to deliver the other two.

I will close with saying that this hearing appears from its title to be focused on what the Department did or did not do with a particular study. And speaking for the Department is an inherently governmental function, and I as a private citizen am strictly prohibited from assuming that role, which makes appearing before you to discuss a study of this which I wasn't part of a bit challenging. My duties include speaking for the Business Board to the Department and others but not speaking for the Department of Defense to anyone.

Thank you, Mr. Chairman. This concludes my opening remarks, and I look forward to your and Mr. Cummings' and the rest of the members' questions.

[Prepared statement of Mr. Bayer follows:]

Statement of

Michael J. Bayer
Chairman, Defense Business Board

before the

House Oversight and Government Reform Committee

On

"$125 Billion in Savings Ignored: Review of DoD's Efficiency Study"

March 21, 2017

Good morning Chairman Chaffetz, Ranking Member Cummings, and members of the committee.

I appear before you today as the fifth chairman of the Defense Business Board.

As are all the members of the Defense Business Board, I am a private citizen; not a paid government employee. We volunteer our time to serve the Department of Defense by offering our collective advice on how to manage the Department more efficiently, in order to enable the Secretary and Deputy Secretary to maximize the allocation of resources to the warfighter. The men and women of the Business Board, and its sister boards, Policy and Science, who donate their time and energy to helping the department, consider it a tremendous honor and responsibility.

As I have communicated to you and your staff, I have no direct knowledge about the study at hand. My first meeting after returning as chairman was in July 2015, more than six months after this study was completed and presented publicly, in January of 2015. As this study was under the direction of the previous chairman, and long before I became the chair, I have no particular insight or access into the actions and decisions made about how this study was conducted and delivered.

I can say that in the almost two years since I became chairman, the Board has completed eight studies. Our most recent effort – Focusing a Transition - was a product of every member of the Board and was very well received by the Department's leadership and the policy community. There is more work to be done in the months and years ahead as we strive to support each of Secretary Mattis' priorities – particularly bringing business reforms to the Department of Defense.

I will close with saying that this hearing appears, from its title, to be focused on what the Department did or did not do with a study. Speaking for the Department is an "inherently governmental" function. As a private citizen, I am strictly prohibited from assuming that role, which makes appearing before you to discuss a study that I was not part of, particularly challenging. My duties as chairman include speaking for the Defense Business Board TO the Department of Defense. It does not include speaking FOR the Department of Defense; ever. This concludes my opening statement.

Chairman CHAFFETZ. Thank you, Mr. Bayer.

I now recognize Mr. Stein for 5 minutes.

STATEMENT OF ROBERT "BOBBY" STEIN

Mr. STEIN. Chairman, Ranking Member, and members of the committee, thank you for inviting me to provide testimony today.

Congressman Cummings, it is great seeing you again since our time on the Naval Academy Board of Visitors.

My name is Bobby Stein, and I'm here to discuss the Department of Defense efficiency study commissioned by Secretary Hagel and created under my leadership as former chairman of the DOD Defense Business Board, known as the DBB.

I was honored to serve as a member of the DBB between 2010 and 2014, and chairman from 2014 to 2015. As you know, the DBB is an advisory panel comprised of a select group of our Nation's business leaders. Our purpose was to provide advice to the Secretary and Deputy Secretary of Defense and other senior leaders on best practices that could be applied to DOD. My priority for the DBB was that members be not selected for any partisan reasons, but based on tried and true experience results in the business world.

I was honored to serve because I understood our mission to be strengthening the defense of our country. I was appointed as chair of the DBB by then-Secretary Hagel in 2014. After becoming chair, I went on a listening tour of senior retired uniformed and non-uniformed leadership to determine areas where the DBB could support the agency.

During the listening tour, we took note of key facts and figures about how money was being spent. It generated concerns because, as a retired Chairman of the Joint Chiefs of Staff said, the biggest threat to our national security is our national debt.

Key takeaways included our national debt is $20 trillion. Our Federal Reserve has taken their balance sheet from 800 billion to 4.5 trillion. At the Pentagon, overhead and support comprise 40 percent of spending, or $240 billion. This equals twice the combined total budgets, defense budgets, of France and England. The expenses on DOD headquarters alone amounts to $40 billion, more than the German defense budget.

At the same time, since 2001, DOD civilian personnel has increased over 15 percent, but military personnel has decreased by 5 percent. While everyone wants reform in the Pentagon, the status quo remains. The antibodies get you every time. Indeed, clean audits and services continue to fail. In some estimates, we have spent $6 billion to try to get clean audits in our different departments. This listening tour predated the commissioning of the efficiency study but highlights the importance of the effort. The DBB efficiency study was one of many reports undertaken by the DBB under my leadership. This study was the first effort ever in DOD history to comprehensively evaluate labor cost data and create a picture of how much money is being spent on noncombat operations at the agency.

As the chair of the DBB during the study, I felt that my role was to help ensure that the study was done accurately so we could meet our ultimate goal of identifying inefficiency and cost savings that could then be moved to better uses. In particular, I helped to identify the people with the right experience to handle this type of project. For something like this, you need a heart surgeon if you have a heart problem, not a country doctor, as said by one of the retired CNOs. And I've spent time looking for who that right person is and who can help that path to work with the Department of Defense to get these savings. And the name that kept coming up was Kenny Klepper. Kenny has done this in a Fortune 50 company. He understands that the DOD is not a business. It is government, and there's not easy efficiency opportunities. So, with that, we got Kenny to lead this study.

The study succeeded in its goal in highlighting inefficiency that, if remedied, could generate significant cost savings to the Department. This cost savings could then be transferred to other priorities, like improving readiness, modernizing our defense, and creating jobs.

The study was presented to the full DBB at public hearing January 25 and won a unanimous approval for its findings and recommendations.

The General Accountability Office also reviewed the study and found the methodologies and analysis adequate to confirm its conclusions. At the completion of the study, along with other members of DBB, we were ready to move forward to assist the DOD in reviewing the study's findings and recommendations. I believe the DBB efficiency study represents a quality analysis of costs and inefficiencies at DOD, and it is my hope that it will be useful to the agency's efforts to streamline.

It was an honor to lead the DBB during the creation of the study, and I'm proud of the work achieved in support of a strong national defense. Thank you for your time, and I'm pleased to answer any questions the committee may have.

[Prepared statement of Mr. Stein follows:]

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
U.S. HOUSE OF REPRESENTATIVES
115TH CONGRESS

HEARING CONCERNING
$125 BILLION IN SAVING IGNORED: REVIEW OF DOD'S EFFICIENCY STUDY

WRITTEN TESTIMONY OF ROBERT STEIN:

Chairman Chaffetz, Ranking Member Cummings, and members of the Committee, thank you for inviting me to provide testimony today.

My name is Robert ("Bobby") Stein, and I am here to discuss the Department of Defense (DoD) efficiency study commissioned by Secretary Hagel and created under my leadership as former Chairman of the DoD Defense Business Board (DBB).

As you know the DBB is an advisory panel comprised of a select group of our nation's business leaders. The DBB was established to provide the Secretary and Deputy Secretary of Defense, and other senior leaders, with independent advice rooted in private sector perspective for application to the agency.

I was honored serve as a member of the DBB between 2010 and 2014 and Chairman from 2014 to 2015, and I brought a strong business background to the job. Throughout my career I have founded the successful investment and growth of many businesses in a variety of sectors, including real estate, oil and gas, technology, and healthcare.

The DBB efficiency study was one of many reports undertaken by the DBB under my leadership. The purpose and ultimate goal of the efficiency study was to help grow and protect the landscape of our nation. This study was the first effort **ever** in DoD history to comprehensively evaluate labor cost data and create a picture how much money is being spent on non-combat operations at the agency.

The efficiency study was commissioned at the request of then Secretary Hagel and carried out with the support of both military and civilian leadership. DBB member

Kenny Klepper led the project along with other DBB members, and was supported by some of the best business minds in the country. To conduct this study, the DBB set about to identify areas of productivity and measure accountability, no small feat. It is important to note that there are not many people in this country capable of effective transformational change of business processes, and we were very fortunate to have had Kenny Klepper on board who has successfully undertaken similar tasks at Fortune 500 companies.

After twelve months and many hours of commitment, research, data analysis, interviews, and briefings the efficiency study was completed in early 2015. The study was presented to the full DBB at a public hearing in January 2015 and won unanimous approval for its findings and recommendations. The Government Accountability Office also reviewed the study and found the methodology and analysis adequate to confirm its conclusions.

After the completion of the study, I along with other members of the DBB were ready to move forward to assist the DoD in reviewing the study's findings and recommendations and begin the process of applying them to the agency's systems. I believe that the DBB efficiency study represents a quality analysis of costs and inefficiencies at DoD, and could be useful to the agency's efforts to streamline operations. In 2017, I met with current Defense Secretary Mattis to discuss the efficiency study, and hope that its findings and recommendations can be used to support the DoD in the future.

It was an honor to lead the DBB during the creation of the efficiency study, and I am proud of the work achieved in support of a strong national defense. Thank you for your time, and I am pleased to answer any questions the Committee may have.

Chairman CHAFFETZ. Thank you.

Mr. Klepper, you're now recognized for 5 minutes.

STATEMENT OF KENNETH "KENNY" KLEPPER

Mr. KLEPPER. Good morning.

Chairman CHAFFETZ. If you can move that microphone up close. Just straighten it out. There you go. Thank you.

Mr. KLEPPER. Thank you. Good morning, Chairman Chaffetz and minority Ranking Member Cummings. It's a pleasure to be here. I've served as adviser on the CNO's executive panel for five CNOs, and this is a first for me for over a decade. So I am happy to be here to tell the story of the work that we have done.

The effort that we embarked on for the Defense Business study is something I took very, very seriously. Just briefly, a little of my background: I spent 40 years with the tradecraft of organizational modernization and change. I spent about 20 years in chemical plant refinery operations out in Texas. And I spent the second 20 years in health care. And I chose in my written remarks that I submitted to the panel an example that I think has a lot of stark parallels. Even though, as Bobby said, I understand that the Defense Department is not a business, there are some very strong parallels.

I was asked to come in and help do a turnaround for a company in New York called Empire Blue Cross Blue Shield. It was financially insolvent at the time, not enough reserves to pay for claims, the largest health plan in the Northeast of the United States. One of the things we did as part of the recovery of that company was understand that we had no money, and we had an obsolete legacy infrastructure running it, and we were losing millions of members a year. The company was in a death spiral. Since we didn't have cash to spend, the only way we could fund the things that urgently needed to be addressed to improve the performance of the business was to self-fund those things through productivity.

So we put in place an opportunity to take productivity savings as a way to generate the money to invest in the platforms and automation and the improvements to recover the company, which we did, and we were doing really well. And then, on September 11, we were the second-largest tenant in the World Trade Center. And through all the things that we did to improve speed, agility, optimize our operations for the private sector, to improve our service to our members and the physicians, we never recognized the inherent ability that it gave us to survive a devastating disaster for our facility. We had over 2,000 people in the building at the time, and with great pride I can tell you, if we can separate the human tragedy for just a moment—we lost 11 people that day—that when the Tower collapsed, we were able to maintain the operation of the business. We lost three call centers, two large server farms. They all failed over to other operations, and the company continued to operate.

The Kennedy Business School did a case study that we included in my written remarks. And the reason I bring that up is, when you look at the state of the operation of DOD, the obsolescence of the legacy infrastructure is not just a bad cost situation and not just creating bad service. I think it increases the vulnerability of the operation to other threats. Whether it is a kinetic attack, an

EMP attack, cyber attack, it is almost impossible to harden those types of legacy cores. So part of what I hope that we can achieve through the modernization of these assets is not just improve the cost basis and not just improve the service, but to also harden and provide a much more resilient infrastructure for the Department of Defense.

The last thing I would mention is the $125 billion savings. We did something that had never been done before—and I give great credit to the Deputy Secretary, Bob Work—is, whenever I talk to him, that the one thing that we had to have to really start was we had to have transparency of where the money was, where the cash flows were. He did something I think has never been done before. He sponsored presentations by Bobby and myself to the DEXCOM, the Defense Executive Committee. He described the process of evaluation that we wanted to do and that we advised him to do, and to his credit, he got approval from all the civilian leadership to let us get the money. And we brought in—I actually asked to have McKinsey brought in because I've done this study before with them, and they did a great job for me. We had over a hundred people pulling data out of these systems. And people before that had said: The data is not there. The data is no good. The antibodies will get you.

What we found was the data was there, and the data was not perfect, and believe me, the study is not perfect, but I believe that the savings that we identified are there with a high degree of certainty.

So I think the debate and the big question for us is, and I think it was stated by Mr. Tillotson and Mr. Rutherford, is—the money is there—it is, can we get the institution out of the way to help us do the things that can obviously help us improve the operation of the business? And that's the purpose of us being here. Thank you.

[Prepared statement of Mr. Klepper follows:]

Testimony of Kenneth Klepper
Former Member of the Defense Business Board

Before the
U.S. House of Representatives
Committee on Oversight and Government Reform

For a Hearing Concerning
$125 Billion in Savings Ignored: Review of DoD's Efficiency Study

March 21, 2017

Chairman Chaffetz, Ranking Member Cummings, and members of the Committee, thank you for inviting me to discuss my work as a former member of the Defense Business Board ("DBB").

My name is Kenneth Klepper, and I was honored to serve as a member of the DBB from August 2014 to May 2015. As you know, the DBB was established in 2001 under the provisions of the Federal Advisory Committee Act to provide the Secretary and Deputy Secretary of Defense, as well as other senior leaders, with independent and objective advice on effective best business practices for application to the Department of Defense ("DoD"). The DBB is comprised of private sector leaders with proven track records in leading large organizations and top-level experience in executive management, corporate governance, audit and finance, human resources, economics, technology, or healthcare.

In joining the DBB in 2014, I brought significant private sector experience in organizational efficiency and resiliency. As an Executive with three Fortune 500 companies, I have practiced the tradecraft of enterprise business transformation in both the energy and healthcare industries for over 40 years, and specialize in large-scale organizational change.

My experiences in bringing private sector practices to our nation's defense efforts began on September 11, 2001. I was serving as the Senior Vice President for Systems, Technology and Infrastructure of Empire Blue Cross and Blue Shield, a major insurer with offices in the World Trade Center. Prior to the attacks, we had put in place a business operations technology foundation designed for speed, agility, and resiliency that held up in the face of the attacks that day, demonstrating the utility of bringing private sector practices to the defense and homeland security spheres. I am including a Case Program created by the Kennedy School of Government discussing these events to supplement my testimony.

Based on this experience, I became involved in nationwide disaster preparedness initiatives in both the private and public sectors, including becoming a member of the Chief of Naval Operations Executive Panel in 2002 and serving until this year. In this role, I worked to provide independent advice to the Secretary of the Navy and the Chief of Naval Operations on issues related to the effectiveness and efficiency of that branch of our Armed Forces.

Testimony of Kenneth Klepper
Former Member of the Defense Business Board

It is with this background that I became a member of the DBB and joined with private sector leaders to bring our collective experience to bear in the furtherance of smart, efficient DoD policies and processes.

DBB Core Business Processes Study

After joining the DBB, I became a member of a Board Task Group charged with undertaking an agency-wide study to evaluate the DoD's core business processes. The goal of the study was to assess the agency's bureaucracy to identify inefficiencies and areas for improvement so that resulting savings could be transferred to combat operations. The DBB Task Group was comprised of me and a number of other DBB members. We were assisted by consultants from McKinsey and Company.

To conduct the study, the DBB Task Group needed to understand how DoD funds were allocated and used, and we requested access to financial data throughout the agency. This request was approved by Deputy Secretary of Defense Robert Work and the Defense Executive Committee. Financial data was provided by numerous DoD employees representing all of the separate non-combat business units within the Department. The DBB Task Group requested and received confirmation from DoD leaders throughout the agency that the data sets used in the study were comprehensive and accurate.

Using this data we utilized a proven private sector approach to analyze it. We also reviewed relevant literature and past DoD studies and reports, interviewed approximately 85 private industry and current/recent DoD senior military and civilian leaders on business processes, and researched best business practices. We identified outdated and inefficient structural and management processes, and developed actionable recommendations to address these inefficiencies. Our ultimate recommendation was to present a clear path to saving DoD over $125 billion over five years.

The study report was completed and presented to the entire DBB during a public meeting held on January 22, 2015. The DBB unanimously approved the recommendations developed during the study, which included recommendations to modernize agency business processes, create an enterprise shared services organization, and leverage industry practices, among others.

Following the public meeting, I along with other DBB members, began meeting with DoD leaders to discuss the study and answer questions, and our findings and recommendations received positive feedback from military leadership. However, to the best of my knowledge, no further significant action was taken to review the study or its application to the existing DoD structure or processes at the time.

In 2017, I was pleased to join a positive and constructive discussion on the DBB study with current Defense Secretary Mattis. It is my hope that the DBB's work will prove helpful to any future DoD efforts to become more effective and efficient.

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Testimony of Kenneth Klepper
Former Member of the Defense Business Board

I am extremely proud of the work undertaken by the DBB during my tenure, and am honored to have had the opportunity to serve our country in this role. It would be my pleasure answer any questions that the Committee may have.

Kennedy School of Government
Case Program

C16-02-1654.0

"The Worst Thing That Could Happen": How Empire Blue Cross and Blue Shield Survived September 11

On the morning of September 11, 2001, some 1,900 employees of Empire Blue Cross and Blue Shield reported for work at the World Trade Center in lower Manhattan. There, on ten floors it leased in the North Tower, the firm housed its corporate headquarters, as well as its development center for web-based technology, three customer service call centers, its membership and billing operation, and a battalion of over 260 servers that formed the hub of its internal networks and its internet-based operations. Altogether, Empire occupied over 480,000 square feet of space, filling hundreds of offices and cubicles, which were outfitted with thousands of desktop computers, monitors, telephones, and other equipment.

By mid-morning on that terrible day, all of it had disappeared forever. As the world watched in disbelief and horror, the landmark twin towers of the World Trade Center were struck full force by two hijacked commercial jetliners and erupted into flames. Soon after, they collapsed into gigantic heaps of rubble, taking with them thousands of lives and hundreds of businesses. Like many of the firms with offices in the World Trade Center, Empire was faced with two agonizing uncertainties: whether it had lost any of its employees in the inferno, and whether its business had been destroyed.

In the anxious hours following the terrorist attack, the grim facts slowly emerged: nine employees of Empire, and two long-time consultants, had been killed; several more had been severely burned. The rest of those who had been in the North Tower when it was hit were reeling from the chaos they had witnessed, displaced from their offices and widely scattered throughout the city as they literally ran for their lives. Every scrap of Empire's equipment in the World Trade Center was lost, leaving a gaping hole in the company's technology grid.

This case was written by Esther Scott under the direction of Howard Husock, Director of the Kennedy School Case Program, for use at the John F. Kennedy School of Government, Harvard University. Funds for the case were provided by Empire Blue Cross and Blue Shield. The Kennedy School of Government is solely responsible for its content. (0502)

Yet, on September 11, most members or health care providers who called the company with a question about benefits or payments reached a customer service representative with little, if any, delay; claims continued to be processed and mailed out in clockwork fashion; Empire's state-of-the art website—whose nerve center was located in the North Tower—was up and running, offering customers an array of "self-service" options. In short, Empire Blue Cross and Blue Shield was still in business. "If it hadn't been in the papers," says David Snow, Empire's president and chief operating officer, "[customers] would never have known we were hit at all."

Later, Empire officials offered a variety of reasons for the company's remarkably quick comeback: luck, teamwork, sheer will power, and, above all, a management philosophy that stressed reliability and "operational excellence." Whatever the precise reason, however, all agreed on one thing: if the September 11 attack had happened just a few years earlier, it would have had, in Snow's words, "devastating consequences for us."

Background: A Faltering Giant

For much of the preceding decade, Empire Blue Cross and Blue Shield had been in terrible shape. One of the oldest of "the Blues," as the member plans of the national Blue Cross and Blue Shield Association were known, it traced its lineage back to 1934 as a pre-payment plan that provided hospital coverage for group members in New York City. In 1935, it joined 16 other plans in adopting the Blue Cross logo, later adding the shield when it merged with a local Blue Shield plan in 1974.[1] Under state enabling legislation, Empire was established as a not-for-profit firm, and became essentially the "insurer of last resort," providing indemnity coverage to individuals regardless of age, sex, or medical history in return for exemption from state and local taxes and deep discounts, set by statute, in hospital rates. By the end of the 1980s, it had grown, aided in part by a merger with another local Blue, to encompass 28 eastern New York counties, from Albany to the metropolitan New York City area. With 11 million members—or about 60 percent of the state's population—and almost 10,000 employees, it was the largest nonprofit health insurer in the US.[2] It was also one of the most troubled.

Like many other Blue Cross and Blue Shield plans, Empire found itself struggling to adjust to major changes in the health insurance industry that began cropping up in the 1980s. The most notable of these was the advent of pre-paid managed care and new competitive pressures from for-

1 "The Blue Cross and Blue Shield Plans: Past, Present and Future," Conning and Company, 2000, pp. 14, 20; Empire Blue Cross and Blue Shield website, online at http://www.empireblue.com/about_empire/company_info/our .../history.shtm, 2/14/2002. The name "Empire" was not adopted until 1985, when two Blue Cross and Blue Shield companies merged.

2 Milt Freudenheim, "Empire Blue Cross seeking to become for-profit group," *New York Times*, September 26, 1996, p. 1A. Jane Fritsch and Dean Baquet, "Big insurer's path to crisis is study in mismanagement," *New York Times*, March 29, 1993, p. 1B.

profit insurers—such as Aetna, CIGNA, US Healthcare—who specialized in providing it.[3] As the advantages of their nonprofit status started to erode—beginning with the repeal of their federal tax-exempt status in 1986—Blues across the US found themselves losing ground to commercial insurers who, thanks to ready access to capital, grew aggressively and soon dominated the burgeoning managed care market. By 1992, with Blues' enrollment declining nationwide, about a dozen Blue Cross and Blue Shield organizations were placed on a "financial watch list" when their reserves—essentially, a pot of money put aside to cover excess losses—dipped below minimum standards set by the national association.[4]

Empire was nearly at the top of that list.[5] In 1992, its reserves tumbled to $40 million, millions of dollars below the minimum set both by the state and by the Blue Cross and Blue Shield Association, which threatened to strip the company of its much-prized cross and shield logos. Over the previous six years, according to a 1993 Senate staff report, Empire had lost a whopping $600 million; and in 1993 alone, over one million dissatisfied customers left the company—an exodus that showed no sign of slowing down.[6]

While Empire's CEO at the time, Albert Cardone, blamed the commercial insurers' practice of "cherry-picking" the healthiest customers, leaving the company to cover the sickest, oldest, and most expensive individuals, critics pointed the finger at Empire's own managers for its dismal performance. In a series of scathing critiques in 1993—by the *New York Times*, which spotlighted the company in a three-part report; by state officials; and by the Senate Permanent Subcommittee on Investigations—Empire was assailed for its "extraordinarily poor management" and "abysmally poor service."[7] The company's initial foray into managed care, the *Times* reported, was a fiasco, thanks in good part to a "failed computer system" that led to "huge losses"; other computer problems were blamed for Empire's mishandling of "national accounts"—i.e., businesses based in New York but with employees stationed across the US. These and other misadventures created an aura of incompetence that only hastened the departure of valued customers.[8]

Empire's reputation took a further beating over ethically questionable practices. In its series on the company, the *Times* devoted an entire article to the "high corporate living" of its senior management, particularly CEO Cardone, detailing his lavish office furnishings and expensive perquisites while Empire was tottering on the edge of financial ruin. Another piece scrutinized the company's "sweetheart contracts" with board members, former executives, and

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3 Conning, pp. 20-21.

4 Fritsch and Baquet, March 29, 1993.

5 According to a May 13, 1994 report in the *New York Times*, only the Washington DC area Blue plan was in worse financial shape than Empire.

6 *New York Times* editorial, July 2, 1993, p. 14A.

7 Jane Fritsch, "Review panel calls insurer poorly run," *New York Times*, September 25, 1993, p. 28; Elizabeth McCaughey, "Pricing healthcare: A Blue gets the blues," *Wall Street Journal*, September 16, 1994, p. A10.

8 Fritsch and Baquet, March 29, 1993.

other insiders. Worse still, the company became mired in scandal in 1993, when its chief financial officer at the time, Jerry Weissman, was dismissed on charges that he had falsified financial reports; the following year, Weissman was indicted by a federal grand jury, and ultimately convicted of perjury and obstruction of justice and sent to prison. To add to its woes, one of its major clients, AT&T, dropped Empire in 1993, reportedly after accusing the company of fraudulently overcharging it for hospital bills.[9]

The cumulative effect of bad news and bad publicity eventually caught up with Cardone, who was dismissed by Empire's board—itself excoriated in the press—in May 1993.[10] He was replaced in August of that year by Robert O'Brien, a former executive with the for-profit insurer CIGNA, who, with the aid of new board chairman Philip Briggs, began tackling the company's many daunting problems. But O'Brien's tenure at Empire proved short-lived: in August 1994, he abruptly resigned as CEO to take a position elsewhere. Two months later, Empire announced that Michael Stocker, MD, also an executive at CIGNA, would take the reins of the troubled company.

The Road to Recovery

When Stocker arrived at Empire's headquarters, then on Third Avenue in midtown Manhattan, in November 1994, he found a workforce that was both demoralized and rudderless. "They had a really wounded management team," he recalls, "that had been through three CEOs and a bunch of acting CEOs, so morale was really terrible." Senior and middle managers had seen a number of strategic initiatives come and go in recent years, and were left with a sense that "whatever they tried to implement was a failure." Top managers had been aloof from the rest of the organization; the management style at Empire, says John Remshard, an 18-year veteran of CIGNA who joined the company in early 1995 as its chief financial officer, was "very autocratic" and secretive. Below them, employees were disaffected and unmotivated. "People had jobs for life," Remshard notes. "There was no pressure: they would get around to doing things. It wasn't a company known to be able to execute promptly and accurately." Even the "basics" got botched. "We couldn't get ID cards out on time," recalls Gloria McCarthy, who joined Empire in 1974 and became senior vice president for operations under Stocker—one of the few Empire veterans to be named to the new CEO's senior management team. "... We weren't paying claims accurately or timely. ... We couldn't answer telephone calls. We were a fat organization, in terms of number of employees, but we just didn't have a discipline." The company still did not have a viable managed care plan, and continued to lose market share at a rapid clip. By early 1995, membership had declined by 60 percent from the 1980s, dipping below five million, and reserves fell to $35 million, bringing Empire to the brink of insolvency. "The place," Remshard sums up, "was really a mess."

9 Elisabeth Rosenthal, "Empire is emerging from a cloud," *New York Times*, September 26, 1996, p. 20D.

10 One August 1993 *Times* editorial, entitled "The Sound of Snoring at Empire," castigated the board for its failure to monitor Cardone's performance.

In view of this bleak picture, Stocker scratched his early efforts to "set a strategic direction" for Empire. "I started off to do that," he says, "and it just became obvious that we weren't in a place to really talk about strategy initially." Instead, he concentrated on restoring the organization to a basic level of competence. "Early on," Stocker explains, "we installed a very elaborate continuous quality improvement system," which became known within Empire as SMI—strategic management and implementation. SMI was essentially a project management system which provided a standard format for organizing and closely monitoring a project, and keeping the company informed of its status along the way to completion. Each project came up for regular review in weekly senior management team (SMT) meetings that included not only top-level managers, but project leaders and members—as many as fifty people could sit in on an SMT meeting. In addition, once Empire acquired the technology, the SMT sessions were broadcast to desktop computers, so that every employee in the company could listen in.

Stocker recruited Kenny Klepper, who had worked with him at CIGNA, to be the "process champion" at Empire, promoting SMI and its goals within the organization. It was not, initially, an easy job. "A lot of people," recalls Stocker, "didn't believe it was worth it." This was especially true of jaded veterans. "I was one of the people who had been here a long time," admits Gloria McCarthy, "who said, 'What do we need that for?'" It was, in her and others' eyes, just "another management program ... the flavor of the week." But McCarthy quickly changed her mind. SMI, she says, turned out to be "a phenomenal system," bringing structure and accountability to Empire's operations, and a new openness to its proceedings. In the past, she explains, "we were very much siloed. People were just focusing on their own little piece." Another company veteran, Grace Messina, who worked her way up from Grade II clerk to become Empire's chief information officer under Stocker, believed that the policy of broadcasting SMT meetings had a transforming effect on the organization. "It opened doors," she reflects, "for people at all levels to say, 'We are one, and we're going to function this way.'" Finally, Stocker notes, the discipline of SMI made it possible for employees at all levels to take initiative and act independently. "Everybody knew what their priorities were," he says. "... So people relatively low in the organization from multiple disciplines could work on projects without a lot of interference from senior management." This would later prove to be an indispensable element in Empire's ability to bounce back from disaster. In the near term, however, SMI was "hugely critical," as Stocker puts it, in providing a framework for recovering from years of decline.

Stabilizing Empire. Looking back on the first couple of years of Stocker's tenure, John Remshard recalls "working seven days a week, till two, three o'clock in the morning. We had hotel rooms across the street; we'd go over there and sleep for an hour and come back. ... It was not like a job—it was more like some kind of crusade." Almost every aspect of Empire's operations needed fixing, but the areas requiring most urgent action were the company's product line and its processing systems.

When Stocker took charge of Empire, its "book of business" was still largely "indemnity-based"—i.e., most of its offerings were traditional fee-for-service health plans, which, Remshard points out, were no longer "affordable" in an era of soaring medical inflation. This was particularly true after the New York state legislature rescinded Empire's special hospital discount rate, which had helped it compete with lower-cost managed care plans.[11] "The entire product list of Empire had to be redesigned," says Remshard. The company scrapped its first, failed HMO plan and embarked on a feverish effort to put together an array of new managed care plans that provided a range of options for members; it also worked to build up its physician "networks" to make its products more attractive to customers.[12]

Meanwhile, Kenny Klepper, whom Stocker would later name senior vice president for systems, technology and infrastructure, took charge of an initiative, already in progress, to rationalize Empire's "core systems"—membership, billing, claims, and managed care. In part because of various "merger activities" in the 1980s, the company operated separate systems for each process.[13] Moreover, within each function, there could be several different systems; so, for example, Klepper notes, "we had six claims engines—one product was on one, another product was on another. They were all different. It was spaghetti." Over the next several years, Klepper and his staff worked to complete the "migration" of Empire's core operations into one "consolidated enterprise system," and to simplify individual processes (including reducing the number of claims engines down to two). The new streamlined system, says Grace Messina, "brought a lot of economy to the table. People don't have to know this system and that system." The simplification reduced errors, saving time and improving Empire's woeful customer service record. After a few years, according to McCarthy, the company began "getting better at the fundamentals. We had gotten to the point where we could manage claim inventories, we could answer telephones, we could pay claims. We could do the things that were really our core business."

By 1997, as Remshard recalls, Empire had succeeded in stanching the flow of customers and red ink. "We stabilized the enrollment of Empire," he says. "No longer were we losing business." Its new managed care products had been well received and were beginning to attract new customers. After years of operating losses, Empire began showing modest gains; in 1997, for the first time in its history, the company sought a credit rating from Standard and Poor's, and was pegged at B+—between "weak" and "marginal." It was a start. Reviving a company "the size of Empire," says Remshard, "is sort of like turning an aircraft carrier around in a harbor. It's a huge task."

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11 The 1996 Health Care Reform Act deregulated hospital rates in New York and also required all health insurers in the state to offer coverage to individuals, including the chronically ill—a group that previously only Empire was obligated to insure.

12 Most of those who bought Empire's products were employers who provided health insurance coverage for their workers. Of Empire's roughly 4.4 million members—i.e., insured individuals and their families—only 250,000 purchased their health coverage directly from the company.

13 Geoffrey E. Bock, "Empire Blue Cross and Blue Shield Delivers Customer-centric Services over the Web," draft case study, The Patricia Seybold Group, 2001, p. 2.

Empire was by this point a much smaller organization. "We turned over, forcibly, ... probably 25 percent [of Empire's workforce]," Remshard estimates. From a high of about 10,000 employees, the company had slimmed down to about 6,500. Its board had shrunk as well, decreasing from 44 to 14 members. At the same time, there were new faces at the top level of management. "We moved out the [former] senior management pretty much," says Stocker. Empire had repaired its soured relations with the state Department of Insurance, and rehabilitated its reputation in the press. "Things were on the road to recovery," says Public Affairs Vice President Deborah Bohren, who came to Empire in 1996, "in the sense that it was a new management team; there was a commitment to ethical behavior, sound management, no excesses ... and at the same time, a very open management process." It was at this point in its still shaky recovery that the company's leaders made a bold decision: they would sell Empire's building on Third Avenue in midtown Manhattan and move into new quarters at the World Trade Center.

New Digs, New Tools

In a sense, there were two distinct views within Empire on the purpose of the move. There was general agreement that it was a good time for Empire to sell its high-rise property. Midtown Manhattan real estate was "sizzling," says Klepper. "We sold a building that was [about $92 million] on the books for $174 million. Downtown [where the World Trade Center was located] was giving incentive packages to go in." But there was debate within the company over how best to use the financial windfall from the sale. To General Counsel Linda Tiano and others who kept an anxious eye on the company's bottom line, the money was needed to shore up Empire's reserves, which were, she points out, "still very low. And really, the primary reason we were doing the sale was to give our reserves a bump they very, very badly needed. So finances were just a huge issue at that point. Obviously, the whole model doesn't work if you end up spending all the money." For Klepper and others with a role in Empire's systems development, however, the sale and the move provided a golden opportunity for capital investment—to "refresh [old] technologies." In its old building on Third Avenue, he says, "they had every piece of old junk PC. Nothing was standard; the network was not very good; all kinds of different phones—just this gobbledygook of stuff that had accumulated over all the years." Klepper wanted to use some of the funds from the sale to modernize the company's technology; he and his staff envisioned a complete infrastructure overhaul, upgrading every system and piece of equipment to "state-of-the-art technology," and bringing Empire, in Klepper's words, "from the Flintstones to the Jetsons."

Behind the debate over how best to use the proceeds from the sale lay some stark truths about Empire's position as a nonprofit in a largely for-profit world of health insurers. "It's a very competitive marketplace," Klepper observes. "... When you go to talk to Merrill Lynch about [insurance] products, you're right in there with the for-profit companies. It's dog-eat-dog. There's no, 'Oh, you get a little bit of slack because you're a nonprofit.'" Health insurance—particularly managed care—in the 1990s was a capital-intensive industry, requiring large infusions of cash to develop and manage good data systems and—in order to take advantage of significant economies of scale—to grow through acquisitions.[14] In this intensely competitive environment, Empire struggled to keep up with commercial insurers, who could raise capital by selling stock. "We don't have access to capital," Tiano observes. "... We have virtually no source of capital other than a regular loan and, as a nonprofit with no source of capital, our credit rating is lower than it would be if we were a for-profit, so we'd have to pay more for a loan."

Empire, in fact, hoped to put an end to its handicap in the health insurance marketplace. In September 1996, Stocker announced that the company would follow in the footsteps of several other Blues and seek for-profit status. This would be no easy task: Empire would need the approval of the state insurance department, the state attorney general, the state supreme court, the federal Securities and Exchange Commission and—late in the process—the state legislature.[15] Ahead lay years of negotiation and lobbying, and an uncertain outcome. In the meantime, whatever capital Empire had to spend would have to come from its premium revenues or its investments. This meant, notes Deborah Bohren, that the company had to "make hard decisions on where you're going to put your resources." The proposed technology upgrade was one such decision. "Some of the discussions got a little testy," recalls Tiano, "because the amounts of money that were being looked at were just mind-boggling."

Empire's financial watchdogs were most concerned with building up the company's surplus—i.e., the cushion on top of the minimum mandatory levels of reserves required by the state and the national Blue Cross and Blue Shield Association. The surplus, says Tiano, was "the money you can use to invest," but at the same time, she adds, the question remained: "how close do you want to get to your minimum reserves, knowing that anything can happen in this industry?" While there was widespread agreement that the consolidation and streamlining of Empire's core systems had been a good use of scarce resources, skeptics at Empire were less persuaded of the need for a comprehensive and costly infrastructure upgrade. "During the period of our recovery," Remshard notes, "we made do with what we had. We didn't have any capital that we could invest in modernizing our systems, ... but people did an incredibly good job of keeping the stuff running. ... If your system is good enough that you get the claims in ... and you pay the right amount and the member never hears from the doctor again about the bill, that's fine. And that's what we were doing. We were doing it very well."

To Klepper, however, the expense of the upgrade would be more than offset by the improvements in service it would bring—and, by extension, the new customers it would attract. He viewed himself as "very much a change agent," who came to Empire as a "process champion for customer service, because in the beginning, customer service was an issue," and he argued that a focus on good service made sound business sense. "The cash you invest in these systems," he

14 Conning, pp. 27-29.

15 Freudenheim, September 26, 1996.

maintains, "has to yield return. ... [But] economic value is not always, 'it's cheaper.' Sometimes it helps you sell; it helps create revenue." In the end, the company decided to fund the infrastructure modernization. The proceeds from the sale were enough to allow Empire to put aside some money for its surplus, and spend some on the upgrade. "Financially," says Klepper, "it was a home run."

Empire signed its lease with the World Trade Center in December 1997. The ten floors it would occupy were just "cement slabs," in Klepper's words. "We built the whole thing out."[16] The infrastructure modernization was laid out in a three-year plan drawn up by Mike Galvin, vice president and chief infrastructure officer at Empire. The plan encompassed all aspects of Empire's technology systems, from the "wide area network," which provided connections to both internal and external users, to the "server environment," to individual workstations. When the work was done and employees "walked into the World Trade Center," Klepper says, "everything was state-of-the-art. All the machines were standard; standard software; high performance network; brand new phone system. ... It was just like they went to a different universe."

Settling In. By 1999, Empire was well established in its new quarters, where its corporate offices and a few "dedicated" call centers, among other things, were housed.[17] The World Trade Center was, however, only one of eleven sites occupied by the company. Its Albany offices, which it had acquired as part of a 1985 merger, were home to Empire's main customer service center and its claims processing center, as well as its medical management operations.[18] National accounts were handled in its Middletown site, north of New York City. A new facility in Melville, Long Island, housed a nurse call center as well as a customer service center. A number of other Empire offices scattered around the state, and in Connecticut, handled specialized pieces of Empire's business, such as Medicare.[19] In addition, the company's mainframe computer was located in a secure, undisclosed site.

The "decentralization" of Empire had been going on since the 1985 merger, but had accelerated in recent years. Some considerations of "disaster recovery" entered into the company's decision to maintain multiple sites—i.e., if some catastrophe or major malfunction should hit one location, its functions could be transferred to another. But for the most part, economics had been the driving force behind decentralization. "We have been moving more and more jobs out of New York City, probably for the last five or six years," says McCarthy, to take advantage of lower rents

16 Empire leased the following floors at the World Trade Center: 17, 19, 20, 23, 24, and 27-31. It also leased two "sub-floors," one in each of the two towers.

17 One of the call centers served New York City employees; two others served two separate labor union accounts.

18 The Medical Management Division was responsible for "oversight of utilization activities," according to Angelo Dascoli, vice president for medical management at Empire. Essentially, this meant approving, or denying, medical services and monitoring patient care. Empire employed a staff of physicians and nurses, and operated a 24-hour nurse call center for members.

19 After the World Trade Center, which housed 1,900 employees, Albany was the largest site, with about 1,800. The rest ranged in size from several hundred to as few as ten employees.

and lower prevailing wages outside the metropolitan area. But, she adds, in light of events to come, that would prove to be "the best decision we ever made."

Meanwhile, Empire's financial health continued to improve so that, in 1999, Standard and Poor moved its credit rating a notch higher—to BB, or "marginal." It was still in the "vulnerable range," but now within shooting distance of S&P's "secure range." Things had stabilized enough to prompt the company to declare in a 1999 strategic plan that the time had come to "shift our focus from recovery to leadership."

Choosing Operational Excellence

In April 1999, David Snow joined Empire as its president and chief operating officer. Snow, who had most recently spent five years at Oxford Health Plans, a commercial insurer, had worked with Stocker in the 1980s at US Healthcare, another for-profit firm that had since merged with Aetna; Stocker, says Snow, knew that "part of what ... I brought to the table was a strategic kind of change mentality" that would be "compatible with [his] own views." When he arrived at Empire, the company had "just finished executing on a strategy to stabilize [it]"; it had done "a lot of gut-wrenching downsizing," and had its first break-even year. "It was time to develop a new strategic vision,'" Snow continues, "... so the timing couldn't have been better for me to come in."

Despite the strides made over the last few years, Snow saw considerable room for improvement in Empire's operations. "My harshest criticism when I came to Empire," he recalls, "was that we were not a customer-facing company. We tended to focus inward, so that attorneys wrote the customer-facing documents, and they were unintelligible." The company's many different insurance products and physician networks led to confusion among members and doctors alike, and created "huge inbound phone volume, and total dissatisfaction"—not to mention high error rates. Empire's 40 call centers were "segmented"—specializing in specific accounts and therefore unable to "support each other because they had [only] their unique knowledge." Customer service representatives leafed through voluminous manuals—what Stocker calls "praying hands books"—to answer questions on products and benefits. Although Empire's enrollment had stopped declining, it "hadn't had net new growth in years," Snow says. "It enrolled people, and it lost people out the back door. ... I knew to get forward growth we had to work on retention. We had to work on our pricing. We had to work on customer satisfaction to drive top-line growth."

With these concerns in mind, Snow asked Empire's senior managers to consider three different "value disciplines," or models, and adopt one to be the company's "primary focus": "operational excellence," which had as its goal "executing business flawlessly"; "product leadership," which emphasized new and cutting-edge product designs; and "customer intimacy," which specialized in knowing and meeting the particular needs of customers.[20] By all accounts, there was little argument about which discipline was right for Empire at that point. "We couldn't survive," Stocker observes, "by being intimate with the customer, having boutique design plans, because we couldn't even implement a simple plan. And we were never going to be product innovators, because we could hardly do the ones we had." In short, Snow says, "it was pretty slam-dunk. It wasn't a heavy debate." Operational excellence was, in Stocker's words, "really our only option."

Becoming Operationally Excellent. As articulated in Empire's strategic plan, the quest for operational excellence meant being able to "deliver our products better, faster, and cheaper than our competitors" — or, as Snow puts it, "let's [make] it simple; let's make it error-free." In part, this involved streamlining the company's products and processes. Over the years, Empire had accumulated a large and unwieldy inventory of health insurance offerings. "We provided every kind of health insurance product in the market," says Stocker. "... We had piled product on product on product ... and never got rid of the old products." Led by Snow, the company began "winnowing out the bad products," in Stocker's words, "and simplifying." In place of "hundreds of variations and special arrangements," as one annual plan put it, Empire would offer a smaller number of standardized products with "well-defined options"; some types of coverage were dropped altogether. The winnowing process was not without cost, especially for the company's sales force, who had to break the news of canceled products to unhappy customers. "It's painful in the short term," says Bryan Birch, senior vice president and chief sales officer at Empire, "to dissatisfy customers to the point where they leave the company." In all, Stocker estimates, "we lost about 25 percent of the business," though the losses were generally balanced by gains elsewhere. But, he adds, "when we got done, we could manage [the products]. The phones stopped ringing. When people did call, the customer service [representatives] knew how to answer their question." In addition, Empire boiled down some eleven different provider networks to two, and simplified its confusing ID card system, which, says Snow, had comprised "185 different cards with different [product] names."

The operational excellence initiative also launched a new round of process redesign. All of Empire's "major processes," says Snow, "claims, customer service, enrollment, sales, billing" were "re-engineered" to meet the "better, faster, cheaper" imperative. One of the most highly touted of these was the "first pass" rate for claims — i.e., the percentage of claims that could be paid automatically, without the intervention of a claims examiner. At the beginning of Empire's odyssey in operational excellence, the company's first pass rate was, according to Gloria McCarthy, a dismal 35-40 percent. McCarthy's staff sat down with information technology (IT) employees to review claims processing at Empire, searching for situations that caused claims to "suspend" and

20 Quotations are drawn from Empire's 1999 strategic plan. The models themselves were taken from *The Discipline of Market Leaders*, by Michael Treacy and Fred Wiersema. In preparation for their discussion, Empire's senior managers were asked to read the book.

for ways to program the system to handle them automatically. As a result, by 2001, the first pass rate had shot up to about 89 percent.

For the most part, streamlining and re-engineering efforts like these, while challenging, were uncontroversial within Empire. This was not the case with the other major initiative associated with operational excellence: an ambitious plan to become a "world class" company through "the rapid adoption of technology."[21]

Becoming "Technology-centric." For Snow and for Kenny Klepper, his chief ally in promoting a "zero-defect mentality" at Empire, technology was a means both to improve the company's performance to and build its "brand equity" in a marketplace dominated by commercial insurers whose products were often less expensive. Operational excellence, says Klepper, was a "customer-facing approach that says if I'm providing a service, that service should be reliable, it should be 24 by 7, it should always be available." The implications of this "operating philosophy" were profound for the organization. It meant, for one thing, building "a lot of redundancy" into its systems. Redundancy—essentially, back-up capacity—and its correlate, "fail-over," ensured that, in the event of an outage, a system would continue to operate "seamlessly."[22] "We kind of built this religion: operational excellence, redundancy, fail-over, reliability," says Snow. But, while prudent, redundancy and fail-over were expensive precautions, requiring duplicates of major system components, such as servers and telecommunications equipment.

Snow and Klepper defined reliability to mean more than undisrupted service, however. The term also embraced the notion of continuous accessibility. To achieve this, they looked chiefly to a relatively untried approach: "e-business." Using "web-facing technology," Empire could be available to its customers—brokers, physicians, members, and employers—24 hours a day with an array of "self-service" options on its website.[23] Anything that could be done "over the phone or by fax," the premise was, customers "should be able to do through an e-business portal."[24] Snow was eager to see Empire stake out an early claim in the new world of e-business. Empire had "missed the managed care curve" a decade earlier, Bohren observes. "Dave came in ... and said, 'The next industry curve is e-business, and we need to get on that curve. ... We need to get out in front.'" The combination of e-business capabilities, sophisticated new telecommunications systems, and other cutting-edge technologies would, Klepper and Snow believed, catapult Empire into a leadership position in the local health insurance community. "We think," Klepper says, "that obsessive-compulsive demand for high performance, reliability, being there when the customer comes to you is a differentiator in the marketplace."

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21 Empire strategic plan, 2000-2002.

22 If, for example, one machine were to shut down, its functions would be automatically picked up by its back-up—i.e., it would "fail over" to another machine.

23 Brokers function as intermediaries between insurers and employers, particularly small ones. [Bock, p. 4.]

24 Bock, p. 6.

But the proposal to take Empire to the leading edges of technology—particularly the e-business initiative—sparked renewed debate over the right use of the company's limited resources. If approved, the project would be expensive. The web technology needed to power the e-business end of it would cost over $60 million; other parts of the project—primarily telecommunications technology—would run to $20-$30 million. For any health insurer, let alone Empire, an outlay of that magnitude would give pause to some. "Very few companies have tried to do all of that all at the same time," Tiano points out. "Even ones with far more capital than we have haven't really tried to go that far. It was a lot to bite off."

The opposition from some quarters was strong. Listening to Snow's presentation of his three-year plan for installing new technologies at Empire, CFO John Remshard recalls, "I just said, 'I don't get it. How are you going to pay for that? ... We don't have the capital. We can't build this into our rates. And how do you know we can even do that? This is a company that just came out of its grave.'" The possibility that a company could get in over its head technologically was not a remote one. Skeptics could point to the recent example of Oxford Health Plans which had developed a massive new computer system in the late 1990s, only to have it crash during the "cut-over" from the old system. Oxford "developed all new systems," says Remshard, "and boom! They blew up on them. They lost control of the business. ... All the technology that Oxford did just sank the company."[25]

Remshard was preoccupied with nursing Empire's finances back to health and readying the company for an initial public offering when, and if, it received the go-head to convert to for-profit status. "I have a very clean balance sheet," he says. "I'm aiming to have the simplest and the cleanest financial set-up available. And I wasn't going to mortgage the company's future for a systems project that, at the end of the day, may or may not work. You never know about these things. No matter how careful you are, sometimes they may not work; or they may work, but the market changes." While Empire's fiscal condition had steadily improved since 1994, it was still in a "turnaround" stage, with little margin for error. "We kept our expenses lean," Remshard observes, "and that's what I like. You watch your profit margins; you ... keep your rates competitive. And the first thing I worry about is how our management group is controlling administrative costs. You don't spend it unless you have to."

For their part, Klepper and Snow argued that the new technologies, along with process redesign, would ultimately reduce administrative costs by improving productivity, as measured by the number of members served by each employee. While acknowledging that "we are more technology-centric than probably a lot [of other companies]," Klepper maintained that the system being proposed would "yield value in the marketplace." It was, he concedes, the duty of the company's fiscal watchdogs "to be frugal and not just buy gadgets," but at the same time, their insistence on an adequate "return on investment" (ROI) could stifle innovation. "Yes, it has to show

25 According to a March 2, 1998 *New York Times* editorial, Oxford's losses in the last months of 1997 "exceeded the total of all its previous profits."

some ROI," Klepper says, "but how much accounting do you have to do? Because you can grind yourself into dust in some of those ROI analyses. ... In some way, you have to believe this is what you have to do, because ... management is not purely an accounting exercise."

Presiding over the debate in the summer of 1999, Mike Stocker was acutely aware that if he chose to go with the leading-edge technology, he'd be taking his company down a path whose end he would not see for years to come. "The strategies that you devise and carry out," he reflects, "really take you down three or four-year courses; and you'd better have the right strategy, because if it's the wrong [one] and you go in the wrong direction, it's very hard to change. It takes a long time to change." Nonetheless, he gave the project the go-ahead. "The e-business investment," Stocker acknowledges, was "frankly, really a bet," but he was willing to put money on it, essentially for two reasons. "Part of it stems from what we think the market is going to look like," he explains, "and part of it ... was a way I could keep good people." With "e-business just exploding" in the late 1990s, he points out, "I could see my good IT people saying, 'What am I doing working on a claims system?'" Lacking other means to reward valued employees—such as stock options or "huge bonuses"—the technology projects were a way, Stocker concludes, "to keep people here, because I could keep them intellectually interested."

Going to the "Leading-Edge"

The massive, multi-stage technology project was implemented through Empire's by now well-oiled strategic management and implementation process. "We would never have been able to make the volume of change from 1999 to [late 2001] that we made," Snow observes, "without the SMI process." The centerpiece of the project was the e-business initiative, which got underway in October 1999 as a collaboration between outside vendors and Empire's own "advanced technology engineering center," a team of about 100 IT specialists. They would essentially be starting from scratch, according to Shevin Conway, who, as chief technology officer, was responsible for the development of web-based technologies at Empire. "All [the company had in place] was a content-based website," he says, "... that basically just showed brochure wear. ... It was static information. No transaction-based processing going on at all."

It was the opportunity to start from a "white board with no markings on it," in Conway's words, that fired up the staff of the advanced technology center. "Our passion," says Klepper of the group, "is innovation. That's what keeps my team really motivated." They envisioned a huge technological leap forward: a website with "a very large set of features," Conway explains. "It wasn't like, are we going to go out with these five or six [features], and let's see how it goes from a marketing perspective, and then we'll add on the rest. ... It was, here are the 30 things that we need to do, and let's get them out there."

Over roughly the next two years, they launched four web portals: for brokers, for members, for physicians, and for "mid-tier" employers—i.e., those with up to 250 employees. Each portal was designed, says Conway, with the "self-service paradigm" foremost in mind. A wide range of critical transactions could be conducted online: physicians, for example, could submit claims which would be "auto-adjudicated" on the spot; brokers could select health insurance products to offer clients, and enroll members; employers could handle registrations and changes in benefits; members could record changes of address and other similar data, or check on the status of claims.[26] "What was unique about what we did," Klepper notes, "was we provided some technology that allowed you as a non-technical consumer to sit at home on a PC with no software to load, just with a browser, and to literally look into our mainframe [computer] and see your claims." In addition, customers on any portal could make use of a "click to talk" feature that would connect them by phone to a customer service representative, who could provide assistance with online transactions, by "co-navigating" the screen with the customer.[27] Empire's competition had nothing like this to offer. "We have," Klepper proudly declares, "a very industry-leading set of e-services."

Call Center Technology. The introduction of web technology also helped transform Empire's management of its inbound calls, through the use of an "intelligent contact management" (ICM) system. It began with "web calls"—i.e., phone calls originating from customers using the "click to talk" option on the company's website. Based on a caller's web log-in number, the ICM would direct the call to the appropriate customer service representative. The ICM, moreover, was "constantly talking to the voice switches out there," as Mike Galvin puts it, so that it could route the call to the next available agent at any location—whether, for example, in Empire's offices in Albany or those in Melville. The system also provided agents with what Klepper calls a "screen pop," which filled them in on the customer's identity and benefits package, as well as notes from recent contacts. "They know who it is," Klepper says, "before they ever pick up the phone."

Impressed by the "suite of tools" offered by ICM, Empire's technology staff decided to widen its application. "After we saw what we could do with the ICM when it came to web calls," Galvin explains, "we said, why not leverage this thing for our voice calls." Empire already had in place an IVR—or interactive voice response—system for inbound calls; customers could punch in their ID number and then select from a menu of choices, which included an automated self-service option. Empire linked its IVR (voice) system with its call management technology by building an IVR "server farm," which the ICM could "talk to"; as with web calls, the ICM could "load-balance" phone calls "across the whole enterprise," Klepper says, "versus just in a single call center."

The advent of web technology fundamentally altered the way phone inquiries were handled at Empire. Previously, customer service representatives essentially specialized in a single account. "Each contract has its own little nuance and complexity," Gloria McCarthy explains, "and prior to 2001, people had to be trained and commit that either to memory or to paper documents."

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26 Bock, pp. 8-10.

27 Ibid.

But in 2001, all of the benefits for Empire's different accounts were put online, which meant, says Carl Tesoro, vice president for customer service, that Empire could "not only bring up the individual's record, but very easily bring up the benefit profile [as well]." It was "a major breakthrough," says McCarthy, "for us to put [benefits] online." Customer service representatives began to be trained to "handle eight or ten different contracts," Tesoro notes, "whereas before they would have typically handled one." While some dedicated service centers remained, due to contractual arrangements—including those for New York City employees and labor unions at the World Trade Center—most of the 40 call centers at Empire were consolidated into five "virtual call centers," able to handle most accounts.

By this time, most of Empire's operations had been transformed by advanced technology. In addition to the web-based systems, the company had introduced new imaging techniques—known as optical and intelligent character recognition (OCR/ICR)—which scanned paper claims directly into digital form. What was once a paper-driven operation had become almost entirely electronic. In the mid-1990s, McCarthy observes, someone who went "on a tour of a claim shop would see paper, lots of paper. You go there today, you see no paper. Everything is online."

Reliability. But, as McCarthy notes, an increased reliance on digital and web technologies meant an increased vulnerability to system failures. In an effort to minimize disruption, Klepper introduced a policy of "aggressive self-reporting" on failures and outages. The centerpiece of these were "reliability meetings," held three times a week, in which Empire's IT staff—and later, at Klepper's suggestion, members of the operations staff—discussed, via videoconference connecting all of the company's sites, any system glitches and problems that had arisen. Even "very minor" problems got "senior level attention," Klepper says, "because reliability is not finding out what the problems are and [then] you fix them; it is all about how you prevent them from happening again."[28] The staff brought "intensity," as Klepper puts it, to its quest for reliability. It was "almost like it's unacceptable to have an outage anymore," says Galvin. "You had to have that mindset."

Reliability also meant closer monitoring of Empire's operations, with the aid of new technology. For example, through a "corporate event monitor" on Empire's intranet, managers could track the performance of all the company's call centers, in terms of "speed to answer" and other measures, in real time—i.e., with only a 5-10 minute delay. This turned out to be a strong selling point with corporate customers. "When a major account comes in," explains Birch, "and says, 'Customer service—how good are you? I want performance guarantees on these things,' we show them [the call center monitoring system], and we say, 'Here's your guarantee.' ... It's not measuring performance every quarter—it's literally right there in front of you on a real-time basis. When a customer sees that, plus all the other technology that is tangible, they are wowed by it."

28 To chart its progress in preventing outages, the company established a new measure: "mean time between failures."

Finally, reliability meant building in redundancy and fail-over in the new technologies at Empire. Redundancy and fail-over features had been included in the systems upgrade that the company had undertaken when it moved into the World Trade Center. "We had redundancy all the way down to the [wall] jack," says Galvin. The same philosophy was followed as new systems and capabilities were introduced. So, for example, two separate ICM machines were installed, one in Albany and one in the secure site where the mainframe computer was located; one IVR server farm was housed in the World Trade Center, with a back-up in the company's secure site. In addition, the data from every server—as well as from the mainframe computer—was regularly backed up on tape and stored at a secure location. And, in the event that one facility suffered an outage, various routing technologies, such as the ICM, would redirect traffic to other Empire sites. "We engineer[ed] for failure," says Galvin. "We engineer[ed] for the worst thing that could possibly happen."

This was not to say that Empire did not have formal "disaster recovery" plans in hand. At about the same time the company moved into the World Trade Center, it hired a consultant to help put together plans that would keep it operating in the event of what David Snow calls "a big-bang disaster." All of Empire's divisions were required to formulate their own recovery plans, which were folded into a larger company-wide document. The plans were "operationally focused," Tiano explains. Typically, they included provisions for setting up command centers and appointing employees to staff them; but beyond that, Tiano says, they were short on specifics. They were "high-level documents," Galvin notes. "Didn't have detail, exact detail [that said] push this button and do this and that." The reliability initiative, by contrast, was designed to deal with smaller crises, according to Snow, such as system crashes or power outages. "It just so happened," he notes, "that reliability had been taken so far" that it would prove to be "a massive disaster recovery tool beyond our wildest dreams."

Upswing. By the end of August 2001, most of Empire's new web services were in place. The broker portal was the first to be launched, in October 2000, followed by the member portal in December 2000 and the physician portal in August 2001; the employer portal would be completed a few months later, in December 2001.[29] The broker portal was an instant success. After a little less than a year in operation, almost 1,800 brokers—out of some 4,000 in Empire's database—had registered to use the portal.[30] Use of the other portals, however, lagged behind. By November 2001, 74,000 of Empire's 4.3 million members would have registered to use the member portal, and 8,500 of 70,000 doctors, the physician portal. Klepper expected the numbers to rise over time. "It takes awhile to get people up the curve," he says, "and [for] people to get used to [using the website]."

29 Bock, p. 6.

30 All figures on portal registration are drawn from Bock, pp. 9-10.

Meanwhile, other key performance indicators rose significantly between 1999-2001. Enrollment figures, notably for Empire's managed care plans, grew steadily over this period, netting the company its largest new membership increase in over 20 years, according to Snow. Productivity, as measured by the average number of members served by each employee, had grown as well. In 2000, the number served increased by over ten percent, from 579 to 643; in 2001, the company reported a 9.8 percent productivity gain—Empire served 320,000 more members with nearly 200 fewer employees.[31] At the same time, the company was consistently operating in the black; the years 1999-2001 were, says Snow, among the "three most profitable years in the company's history." Its surplus skyrocketed from a low of $35 million in the mid-1990s to a healthy $839 million in 2001. It was such figures that prompted Standard and Poor to raise Empire's credit rating from BB ("marginal") to BBB ("good") in 2000, and to BBB+ in May 2001. Empire had gone, says Remshard, from being "a company that was technically bankrupt to [one] that's considered investment grade."

There were signs of qualitative improvement as well. In August 2001, the BlueCard Performance Index—a measure of each Blue's level of service in the national BlueCard program—gave Empire a score of 100 percent.[32] It was, Snow notes, "the first time in the company's history" that it had received the highest possible score. In addition the National Committee for Quality Assurance, an accrediting body, gave Empire's HMO plan—once a dismal performer—a rating of excellent, the highest rating it awarded. No longer pilloried in the press for poor management, Empire had won the editorial support of the *New York Times* in its bid to become a for-profit insurer. It was little wonder that the company's strategic and annual plans had largely dropped the language of recovery and turnaround, and instead looked optimistically to the future and achieving its ambitious goal of "bridging the gap to world class."

September 11, 8:48 a.m.

When American Airlines flight 11 slammed into the North Tower of the World Trade Center, Empire employees in the building felt the powerful jolt. "The building swayed so much," recalls Grace Messina, "that my desk drawers opened up, and when it swayed back, my desk drawers [closed]." While some initially thought that an earthquake might have struck, most soon concluded that a plane had hit the building. But, says Angelo Dascoli, vice president for medical management at Empire, "we thought it was a small plane that had hit the building, because lots of smaller planes would fly at about the 100th floor level, down the Hudson." At the time, Dascoli had just finished a meeting with Dr. Alan Sokolow, head of Empire's Health Services Department, at Sokolow's office on the 28th floor, and had been about to take the elevator down to his office on the 23rd floor; instead, however, he decided to stop by the office of one of the company's lawyers. This

31 Empire Blue Cross and Blue Shield Annual Plans, 2001 and 2002.

32 The BlueCard program allowed members access to any Blue Cross and Blue Shield provider nationwide. The resulting network, Birch points out, was twice the size, in number of physicians, of Empire's nearest competitor.

turned out to be a lucky move: when the American jetliner crashed into the tower, it sent flames shooting down the elevator shaft and into the lobby, which was then engulfed in flames. Anyone who was in the elevator or the lobby at the moment of impact suffered severe injury or death. Mike Galvin, too, would normally have been in the lobby or on the elevator up to his office at about that time, after his regular Tuesday morning workout; but his gym partner had called to say he would be unable to join him, so Galvin skipped the gym and was instead in his office on the 30th floor. "I thank God," Galvin says, "that he called me."

Looking out the window after the impact, Galvin saw debris falling from the plane, and immediately began shepherding Empire employees out to the emergency exits, where they joined a stream of people making their way down the stairwells. By all accounts the descent was orderly, though there were increasingly ominous signs of a major disaster: the smell of jet fuel saturating the air, gray smoke filling the corridors, water from the emergency sprinkler system pouring over the stairs. Later, many recalled meeting firefighters coming up the stairs. "That's something that will be etched in my mind forever and ever," says McCarthy. "I really felt for the firemen," Dascoli recalls. "By the 20th floor, they were exhausted. They all had packs on; the [oxygen] tanks looked like they weighed about 40 pounds. ... The thought ran across my mind that these guys have to go another 50 flights more."

Once out of the stairwells and into the lobby area, evacuees confronted a terrifying scene of pandemonium. The lobby, once paneled in marble, was unrecognizable—both McCarthy and Dascoli remember thinking that they had come out into an unfinished basement area. From there, people were directed out of the tower by emergency personnel. For some, this turned out to be the most harrowing part of the ordeal. "What exit you got out of the building," says Messina, "really determined what you were going to see, what you were going to experience, and where you were going to go." Dascoli was "led out a kinder way," he notes, a route that took him through an underground mall and then up a stairwell that brought him some distance from the World Trade Center when he resurfaced. Galvin was less fortunate. While descending to the lobby from the mezzanine, he "came around to the windows where the plaza was, where I first realized how serious this was," he recalls. "All the carnage was out in the plaza. [There were] burning bodies; a body had fallen right next to me." Galvin was "a little bit in shock," he says, "but I also couldn't help but think about all the guys I was seeing going up the stairs, and the people around us, helping us. We saw the firemen and the policemen, the Port Authority guys helping everyone."

Out on the plaza level, the situation grew increasingly chaotic. A second jet, United Airlines flight 175, struck the South Tower at 9:03 a.m., showering debris on people still fleeing the North Tower. "There was glass flying," Deborah Bohren remembers. "I put my briefcase over my head. ... Plane pieces were falling." Emergency personnel were hurrying people away from the towers. "As we got out through the [Marriott Hotel] bar," Bohren says, "the policeman at the door kept saying, 'Run, get away from the building. Don't look back. Just run.'"

Not knowing what was happening, evacuees imagined the worst. "I didn't know if we were at war, or what," Bohren recalls. "... I didn't know if planes were hitting every place." When the South Tower collapsed at 9:59 a.m., "people started screaming, 'They're shooting again.' We thought planes were buzzing us." Bohren had "an out-of-body experience," as she raced away from the World Trade Center. "I can see myself with my purple Patagonia bag, serpentining, not knowing, am I safer in a building or out of the building?" As Dascoli, who was by then several blocks away, watched people running by, ahead of the huge cloud of smoke and debris billowing out from the destroyed South Tower, he believed there might have been another attack. "I thought," he says, "there were troops on the ground shooting."

Not everyone who was in Empire's World Trade Center offices that day made it out safely. One of the most poignant stories to emerge from the September 11 attack concerned two Empire employees, Ed Beyea and Abe Zelmanowitz. When Beyea, a quadriplegic, could not be evacuated without the assistance of firefighters, Zelmanowitz insisted on staying with him until help arrived—despite "desperate phone calls," the *New York Times* later reported, "from his brother begging him to leave."[33] They died together when the North Tower collapsed at 10:28 a.m. "Nobody," says Bohren sadly, "expected the building to fall." There were other acts of heroism by Empire employees. "One of our security guards," Bohren says, "... went back into the building to help. He [was the father of] a five-year-old son." In all, nine Empire employees died in the attack, along with two long-term consultants. Three others were hospitalized with severe burns.

Those fortunate enough to escape unhurt still faced a perilous journey to safety. In the scramble to get out of range of falling debris, people began to trip and fall over each other. "That was the first time I felt panic," Galvin says, "because I had people lying on top of me, and there was a big pile of them." Galvin managed to extricate himself, and help an injured woman to safety, and then continue running up West Street away from the crumbling towers. He was unable to make calls out on his cell phone—a problem many ran into as intensely heavy cell phone use throughout the city jammed the airwaves—but a friend managed to get through to him. Galvin asked him to "please call my family first," and then to call his brother and instruct him to contact a colleague at Empire's Albany offices "and tell her to invoke disaster recovery"—i.e., begin implementing the company's disaster recovery plans. Eventually, Galvin made his way to his parents' house. "I had dinner with them," he says. "I was just very grateful to spend time with them. But I went from there to Albany that night. Because I had to get this company back."

Out of Harm's Way. Many of Empire's senior managers were far from the scene when the World Trade Center was attacked. Mike Stocker and Linda Tiano were on a train to Washington, DC to attend a Blue Cross and Blue Shield Association meeting. Tiano remembers that she and Stocker had both tried calling their offices from the train, just to check in. "We started calling and

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33 Mark Lander, "A nation challenged: survivors; sharing grief to find understanding," *New York Times*, January 17, 2002, p. 1A. Later, President George W. Bush made mention of the two men in a speech at the National Cathedral in Washington.

calling, and we couldn't get a line. And then I'm getting through, and nobody's picking up the phone. I'm going, 'What are these people doing?' And I'm leaving nasty messages for people." The mystery was cleared up when Tiano's daughter called her cell phone with news of the attack, which she had watched on television. Helpless, Stocker and Tiano sat on the train en route to Washington, unable to find out the fate of their colleagues at the World Trade Center and fearing the worst. "It was hours," says Tiano, "before we were able to really conclude that probably not everybody was dead."

When they finally pulled into Union Station, which was shortly afterward evacuated, Stocker and Tiano managed, with the help of a colleague, to hire a car and a driver to take them back to New York. During the long drive back, they were still unable to get hold of co-workers at Empire to find out "who was alive," Stocker recalls. In frustration, he called his real estate broker. "It was clear that we needed [office] space," he explains, to replace what had been lost at the World Trade Center, and there would soon be a "huge rush on space." He instructed his broker to start looking into office availability in Manhattan. "It was," he says, "the only useful thing I could think to do."

Dave Snow, along with Bryan Birch, was in a Florida resort, The Breakers, attending an awards event for top-performing sales staff. He was on the golf course with them when "cell phones on the golf carts all around us started ringing." Snow raced to the pro shop where, on its large-screen TV, he saw "our building on fire," and watched as the second plane hit the South Tower. With the help of the staff at The Breakers, Snow was able to set up "kind of a disaster recovery center" equipped with phones in one of the hotel conference rooms. By chance, he had with him a list of all of Empire's senior managers, with their home and office phone numbers, as well as their cell phone numbers. "Immediately," he says, "I started making outbound calls."

By this time, Empire employees had begun to scatter as they made their tortuous way out of danger. Grace Messina and some colleagues boarded the Staten Island ferry; Deborah Bohren was walking north to the Bronx on her way home to Westchester County. Gloria McCarthy was "stumbling up the West Side Highway," as Snow puts it, when he was able to make contact with her.[34] McCarthy had taken nothing with her when she fled the North Tower. "I didn't have a pocketbook," she says. "I didn't have a phone. I had nothing." When she finally managed to call home and speak to her children, her daughter told her that "Dave Snow had called from Florida, and that it was important that I get onto a conference call." That afternoon, using Snow's calling card number—she had no cash or credit cards—McCarthy stood at a pay phone on the West Side Highway and joined in a conference call with other senior managers whom Snow had succeeded in tracking down.

34 Snow also reached Mike Galvin on his cell phone as he was running up West Street.

Farthest away from the scene was Kenny Klepper who, with Shevin Conway and senior IT staff, was in Bangalore, India, working with IBM to evaluate its Global Services India operation for offshore development. There was "a knock on the door," he recalls, "and [someone] said, 'Turn on the TV.'" Using Conway's worldwide cell phone—which had been restored to working order only a few hours earlier—Klepper was able to get through to Empire before the towers fell. "The first outbound call," he says, was to his wife, who worked on the 19th floor of the North Tower. The next one was to Albany, where he was soon linked up with Dave Snow in Florida.

First Steps. Later, both Snow and Klepper would talk of the guilt and frustration they felt at not being with their colleagues in New York when the towers collapsed, but they also came to believe that their distance from the scene had been a help as the company tried to regroup. "We kind of agreed," Klepper says of his group in Bangalore, "that we were there because that's where God wanted us—to not be in the middle of the conflagration, so we were able to fairly objectively start taking some actions … and begin to move ahead with the planning."

The "first priority," says Klepper, "was to locate and identify our employees." Using an employee database, they "swung around" the Albany customer service call center and began making outbound calls to trace the whereabouts of employees who worked at the World Trade Center. They also set up an 800-number, publicizing it on television, for employees and their families to call in, either to let the company know where they were or to get information on family members and colleagues. Staff members in the Albany office, says Stocker, "stayed up all night for several nights taking calls," or making them, "trying to figure out where [World Trade Center employees] are, if they're okay." Some of what they learned was painful. There was especially grim news for Klepper—eight of the nine employees who died had worked for him. Still, by the end of the second day, the list of missing people, once in the hundreds, had shrunk enough so that, Stocker recalls, there was a growing sense of relief that "we were going to make it, … that we were going to basically be okay."

The second priority, says Klepper, "was to assess business damage and move into business recovery." Clearly, the physical damage was massive. "I had ten full floors in Tower One," Klepper points out, "which was just under half a million square feet. All those assets went down." This included, according to Empire's inventory, 263 servers and 2,255 desktop computers along with "all the data in those machines." Faced with the loss of a huge "hunk of infrastructure," the question on everyone's mind was, as Klepper puts it, "what's still running?" The short answer was, just about everything.

Open for Business

In the confused hours immediately following the attack on the World Trade Center, perhaps the greatest worry for Empire's senior managers—apart from the welfare of employees—was whether customers would be able to contact the company. "The first concern," says Birch, "was telephonic capability." McCarthy agrees. "I [was] thinking," she recalls, "we have to be able to answer the telephones. We have to serve the customers." Like others at Empire, she "was afraid that people would think we were destroyed as a company, and then we would not be able to recover because people would begin to leave us." Second on the list of concerns, according to Birch, was "[would] there be any claims disruption"—a matter of paramount importance to Empire's members and providers. As information filtered in from Empire's various sites, fears that key services would be affected were quickly allayed. "We didn't lose the call centers," says Klepper. "We didn't lose the claim systems. We didn't even lose our website." The delivery of services was, in Bohren's words, "seamless to our customers." Amid the sadness of loss and destruction, the company's resilience became a source of deep pride shared by all. The reasons offered for its recovery, however, revealed a variety of perspectives.

There was widespread agreement at Empire that the continuity of its operations in the wake of the attack was *not* largely attributable to its disaster recovery plans. "The discipline of that," Bohren maintains, "did not prepare us for what happened" at the World Trade Center. To Klepper and Snow, Empire's recovery was the direct result of the company's quest for operational excellence and reliability. "Most of the systems that were available," says Klepper, "that made the loss of the World Trade Center fairly invisible to the customer, were not disaster recovery per se—it was high reliability design." In particular, he cited the key role played by fail-over provisions. Once the World Trade Center "literally left the grid," he notes, the traffic normally routed to it was automatically redirected to other facilities.[35] When, for example, the ICM began getting no response from the IVR server farm at the World Trade Center, it began rerouting calls elsewhere. "The ICM—which was talking to the IVR farm," Galvin explains, "saying, 'Are you there, are you there, are you taking a call?'—says, 'My God, there's no IVRs out there; send all the calls to the other IVR farm.'" Customers, he notes, "never even saw a blip on that." Meanwhile, the 263 servers that contained corporate intranet and e-business applications, as well as the company's Lotus Notes environment, failed over to back-up servers in Albany.[36] The installation of the back-up server farm in Albany, Klepper points out, had been completed just weeks before September 11. "That really saved our cookies," he says.

To some, the decentralization of Empire's operations played a crucial role in getting the company back on its feet quickly. Many of its most critical operations—claims processing, customer service, medical management—were located either in Albany or Melville. Moreover, Conway notes, "all of our key [computer] systems"—such as claims processing—"were maintained outside the World Trade Center," in the company's mainframe computer. Had the site of Empire's mainframe been hit, Bohren observes, the consequences would have been "much more serious." As it was, despite the destruction of huge amounts of equipment and data, Empire's most critical

35 The exception was the dedicated call centers in the World Trade Center, which had to be manually reprogrammed to direct calls to other sites. According to Carl Tesoro, it took about a day to reroute those calls.

36 "The insurance plan that came to the rescue," *PC Magazine*, January 29, 2002.

functions could be carried on with little or no disruption. "We were paying claims the same day that [the towers] went down," says Snow. "We could pay all our claims."

Other technological or organizational improvements also helped keep the work on track. Paper claims coming into the World Trade Center were routinely imaged and the data stored elsewhere, which meant, says Carl Tesoro, that "even though the paperwork was gone, we could bring up the images in Albany and Melville, and keep processing." Only about two days' worth of claims, which had not yet been imaged, were lost.[37] The effort to streamline Empire's product offerings, and to replace unwieldy benefits manuals with web technology also paid off. When calls that would normally be routed to the World Trade Center were directed to Albany or Melville, customer service representatives "could service the business," Stocker says, "because we'd simplified the products. That was huge." Moreover, service representatives had easy access to information on these accounts via the intranet.

For some, the habits ingrained through years of SMI and reliability meetings carried employees through in the face of unimaginable destruction. Empire's recovery was "really about the people and the technology," says Galvin. As an example, he points to the quick thinking and independent action of "a lead server guy in Albany" right after the North Tower was struck. "He promoted all the profiles"—information about individual employees which enabled them to log on to Empire's computer systems—from the World Trade Center servers to the back-up servers in Albany before the towers collapsed, thereby saving the company "a lot of manual effort. We would have had to rebuild all those profiles manually." People "knew what they had to do," Galvin says. "That was not something that was in a plan. That's something he just did." To Galvin, it was "the discipline and the structure and the process and accountability that saved the company." That discipline, Grace Messina notes, continued to sustain employees in the days following the devastating attack. "Here's the beauty of who we became," she says. As she and her staff struggled to keep the company's systems running smoothly, "our mantra [was]: you do not break the process because of this crisis. ... Accelerate everything you're doing because of the crisis, but don't break the process."

Finally, the commitment of employees to the company was, to some, the key to its recovery. After surviving the terrors of September 11, Stocker points out, "a lot of people got home however they could, took a bath and packed their clothes and drove to Albany or Melville or Middletown and went to work." They built new servers to replace the destroyed ones, or hunted down new office space, or holed up for weeks in a hotel doing software development. "When the building went down," John Remshard observes, "everybody went off and started organizing themselves. ... Everyone had a mission. Everybody knew what they had to do." The role of

37 Imaging and other advanced technologies were, however, largely limited to Empire's "customer-facing" operations, such as claims processing. Most administrative areas, such as the legal department, kept paper files and, as a result, lost many of their documents. Among the "lessons learned" from September 11, says Birch, "are mainly [that there should be] document imaging across the board."

technology, while important, was in his view eclipsed by the contributions and resilience of Empire's employees. "All the systems [failed over]," he says. "That was all great, but the people pitching in, trying to overcome ... what had happened to us all" impressed him more. "While we were trying to figure out who made it out [of the World Trade Center], and who didn't, people were still talking to customers, people were still paying the bills." Remshard believed that employees' commitment grew out of their earlier experience of helping to bring the company back from the brink of insolvency and the taint of scandal. "People [were] real enthused about working for the company, real enthused about the turnaround," he says. "It was a heck of an accomplishment ... for everybody."

On October 12, 2001, Empire held a "remembrance service" at St. Ignatius Loyola Church for the employees who had died on September 11. The company's workforce was still scattered—some had set up temporary quarters in Melville or Albany, but about one-third were either working from home when they could or waiting for office space to be found. There had been several grief counseling sessions offered at different locations, but this would be the first time employees could gather in one place to commemorate their lost colleagues and reflect on the terrible events they had witnessed and survived. Ahead lay many challenges, and triumphs, for the company: leasing and building new space for all of its workers; convincing worried customers—and hungry competitors—that Empire was a going concern; preparing for conversion to for-profit status, which would finally receive the formal go-ahead from the state legislature in January 2002. But on this October day, Empire's employees paused to look back.

When the service was over, the 2,000 or so people in attendance spilled out onto the steps of the church and then into the street—Park Avenue—for an emotional reunion. "I happened to be at the top of the steps at that point," Bohren recalls, "and [there was] a sea of people," greeting each other with hugs and cries. There were employees who "had been working nonstop," and displaced employees "who wanted to come back, who needed to be around [their colleagues]." The crowd was reluctant to disperse. "People needed to see and touch each other," Bohren says. "...We stopped traffic for half an hour." This image, both sorrowful and celebratory, stayed with Bohren long after the commemorations were over and employees had returned to the business of Empire. "There was a strength that came from our workforce," she reflects. "I'm not sure where it came from, but it was amazing."

Chairman CHAFFETZ. Thank you.

Mr. Korb, you're now recognized for 5 minutes.

STATEMENT OF LAWRENCE J. KORB

Mr. KORB. Chairman Chaffetz, Ranking Member Cummings, thank you very much for inviting me here today.

I think this hearing comes at a very critical time. As Ranking Member Cummings mentioned, President Trump wants to add $54 billion to the fiscal year 2018 budget. It's also important to keep in mind that they're proposing to add $30 billion to the fiscal 2017 budget, and then the Congress last year added $23 billion in the National Defense Authorization Act. So we're talking about adding $100 billion to the defense budget compared to what we thought about a year ago.

It's also important to keep in mind, as has been very well documented and even people in the Pentagon admit, that the overseas contingency budget, or the warfighting budget, about half of it is used to fund items from the enduring items or from the base budget, and then the Pentagon has gotten relief for the last 5 years from the budget cap. So I want to put that into perspective.

Now, in terms of what the Defense Business Board recommended, let me give you some examples from my own career that I think buttress the points that they made. Basically, I've been working on these issues ever since I was in the service in the sixties; at AEI in the seventies, working with former Secretary of Defense Melvin Laird, who I think was probably the most effective Secretary we have ever had; the privilege I had of serving for 5 years in the Reagan administration administering about 70 percent of the defense budget; and then continuing to focus on these areas at Brookings, the Council on Foreign Relations, and now the Center for American Progress.

When I was Assistant Secretary of Defense, my title was Manpower, Installations, and Logistics. Right now, you do not have anybody in that position. They have taken the manpower or personnel part of it, elevated it to an Under Secretary, even though he or she does not have responsibility for installations and logistics.

During most of the Cold War, we had one Assistant Secretary serving in the policy area. It was called the Assistant Secretary for International Security Affairs. Now you have seven confirmable positions in the policy area. All of these men and women have their own staffs.

When I was working in government, the Congress took the lead in proposing the Goldwater-Nichols Reform Act, which was really very, very critical to get the Department to really be unified for the first time. All of my colleagues fought it because they felt that it was saying that they were not doing their job. I thought, having based on my own research and testifying on it, I supported it. What we did is we empowered the Chairmen of the Joint Chiefs of Staff and the Joint Staff, and so they increased their staffs. The service chiefs did not decrease their staffs, and so what you ended up with was an increase in the staff.

Similarly, when we set up new commands, like the Africa Command and the Central Command, you did not decrease the staffs of the commands that used to have responsibilities for those areas.

And then, finally, and this is very, very critical, and in the Bob Woodward article, they quote the former Secretary of the Navy Ray Mabus talking about the fact that he says 20 percent of the budget goes to overhead in agencies, and he mentioned the Defense Intelligence Agency and the Defense Logistics Agency. Well, the fact of the matter is, when those agencies were created, the idea was that the services would transfer those functions to a unified organization, and they would cut their own staffs. They didn't.

And I mention in my testimony when I did my dissertation and wrote my book on the Joint Chiefs of Staff, when I asked a former Chief of Naval Operations, you know, how did you handle this? He said: Oh, we never cut the size of our own logistics organizations or intelligence.

Let me conclude with this point. I can assure you that if you add the additional funds that have been proposed by President Trump, you will ensure that those reforms do not get made. The best way to ensure that it happens is don't give them any more money. Thank you.

[Prepared Statement of Mr. Korb follows:]

TESTIMONY OF LAWRENCE J. KORB

SENIOR FELLOW, CENTER FOR AMERICAN PROGRESS

BEFORE THE HOUSE COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

MARCH 21, 2017

Chairman Chaffetz, Ranking Member Cummings, and Members of the House Committee on Oversight and Government Reform, I appreciate the opportunity to appear before you today, and I commend you for attention to the Defense Business Board "Transforming DoD's Core Business Processes for Revolutionary Change" before the public so that the Congress and the new administration can have a full and fair debate about the subject of what may be $125 billion of administrative waste in the Department of Defense.

Discussing this report by the Defense Business Board, which was briefed to Defense leadership starting in early 2015, comes at a critical time for the Department of Defense and the nation. Despite the fact that the U.S. spends more on defense than the next seven nations in the world combined (five of whom are our allies) and that the U.S. defense budget is three times larger than that of China, and more than ten times that of Russia, and, according to experts like General David Petraeus, our military is "awesome." The new administration has already proposed to add $84 billion to the FY 2017 and FY 2018 top line. Moreover, the National Defense Authorization Act for 2017, which has been passed by the Congress and signed by former President Obama, has already added another $28 billion to the FY 2017 request. Finally, the Obama administration and the Congress have already given the Pentagon over $100 billion in relief from the caps imposed by the Budget Control Act of 2011, and the Pentagon, with the acquiescence of the Congress, has used the Overseas Contingency Operation (OCO) budget, or warfighting budget, to spend another $150 billion over the past five years on programs having nothing to do with the wars we are fighting, something the Pentagon comptroller has publicly admitted.

The statements by President Trump now and while a running for office that the U.S. military is a "disaster" are totally without basis. The military does face substantial challenges in terms of readiness and modernization, but these require a clear strategy supported by the administration and Congress before adding more money. When the report in question was commissioned, I believe the leadership in the Department understood that systemic inefficiencies pose a threat to the future of our national defense, not an inability to pay for what we need.

In looking at the report by the Defense Business Board, we need to ask at least three questions. Why did the Pentagon commission the report, what is the basis for this large back office staff, which now consists of over one million people to support an active duty force of only 1.3 million, and why did the Pentagon try to bury the report?

The Pentagon, under the leadership of then Secretary of Defense, Chuck Hagel, who in my view was the most qualified person ever to be selected for the Secretary of Defense position (a war veteran, political appointee in the Reagan administration, distinguished and long-serving Senator from Nebraska, and successful businessperson) recognized that the Department of Defense needed to improve its tooth to tail ratio especially after the B.C.A. stopped the massive growth in defense spending which saw the defense budget increase from less than $300 billion to nearly $700 billion between 2001 and 2010.

I base my analysis and recommendations before you today on decades on managing and analyzing the defense enterprise. Having served on active duty in the 1960s, I worked at the American Enterprise Institute in the 1970s with former Secretary of Defense Laird, a highly effective leader and excellent Secretary of defense. I served as Assistant Secretary of Defense in the Reagan administration in the 1980s. I have analyzed and written about defense issues at the Brookings Institution, the Council on Foreign Relations, and the Center for American Progress since then, and it has become clear to me that the overhead in the Department of Defense has grown too big, especially when compared to the size of our active force Secretary Hagel was correct to ask the Business Board to undertake this study, especially since the Pentagon has to date never been able to pass an audit.

Let me give four examples of this bureaucratic bloat which I have personally observed. First, the proliferation of senior positions with fewer responsibilities over the past 40 years has done more harm than good. When I had the privilege of serving in the Reagan administration, my office at the Assistant Secretary level had responsibility for manpower, installations and logistics. Today that job has been elevated to the undersecretary level, even though the occupant is responsible only for manpower and has no responsibility for installations, or logistics.

Similarly, during much of the Cold War, the Pentagon had only one Assistant Secretary handling policy issues (the Assistant Secretary of Defense for International Security Affairs). Today you have an undersecretary with a principal deputy, and five assistant secretaries all with their own staffs and all serving in confirmable positions.

Second, when Congress, over the opposition of the Pentagon, enacted the Goldwater-Nichols Reform, (which I supported in testimony before the Congress), it increased the power and responsibilities of the Chairman and Joint Staff. Consequently, the size of the Joint Staff which supported the Chairman increased. However, this increase was not met with a reduction in the size of the staffs of the individual service chiefs. This created bloat across back office organizations throughout the uniformed services.

Third, when the Pentagon established new unified commands, like the African Command or Central Command, which took over some of the responsibilities of the existing commands, like the European Command, the existing commands did not reduce their staffs proportionately. Indeed, Combatant Command staffs have grown and massively increased the use of contractors.

Fourth, when Secretary of Defense Robert McNamara consolidated functions, like intelligence and logistics by establishing organizations like the Defense Logistics Agency (DLA) and the Defense Intelligence Agency (DIA) the services did not reduce the size of their own logistics and intelligence organizations. In fact, when I was working on my dissertation and subsequent book on the Joint Chiefs of Staff, I interviewed several service chiefs about the impact on the services of Secretary McNamara transferring functions from the services to the office of Secretary of Defense. One told me it had no impact because he kept his intelligence and logistics organization intact. And during my five years in office, this point was brought home to me when I constantly had to battle the individual services to transfer logistics from them to the Defense Logistics Agency.

In June, 2015, then Navy Secretary Ray Mabus, made this point in a speech at AEI. Mabus, who served as Secretary of the Navy for all eight years of the Obama Administration, complained that 20% of the defense budget or about $120 billion went to the so-called "Fourth Estate," that is, defense agencies like DLA that provide support to the armed services. He called this pure overhead. What he did not say was the fact that the Navy and the other services maintain parallel organizations is part of the problem.

Finally, according to the New York Times, the Pentagon effectively buried the report because they were afraid that the Congress would use this report as a rationale for not adding additional funds to the defense budget. I urge the Congress to employ this rationale and not add the additional defense funding that is being sought by the administration. Analysis of Pentagon spending, to include a review and plans for implementation of this report, should come before any major increases in defense spending. Indeed, if the President wants to bring best business practices to government, he should spend this year analyzing current defense spending and instituting an audit of the Pentagon as well. This is something that the new administration should embrace given the President's statement about eliminating wasteful military spending.

This is also what our warfighters need and deserve: every dollar of waste is a dollar that does nothing to help the men and women we send into harm's way and ask to make the ultimate sacrifice. Adding funds before doing rigorous analysis of studies like this almost ensures that reforms will not be made.

Thanks again for the invitation to appear before you. I look forward to your questions as you deal with this critical issue.

Chairman CHAFFETZ. Thank you all for your testimony.

I'll now recognize myself for 5 minutes.

Mr. Tillotson, let's go back to the study. You originally awarded the study to—name the company again.

Mr. TILLOTSON. Ryan Consulting.

Chairman CHAFFETZ. Do you happen to know R. Keith Harding, the president, I believe.

Mr. TILLOTSON. I do not know.

Chairman CHAFFETZ. If I have the right website.

Mr. TILLOTSON. You may, but I'll be honest with you. No. I do not know.

Chairman CHAFFETZ. And how much money was paid to Ryan Consulting?

Mr. TILLOTSON. For the two elements of the contract that were executed during the DBB study, about $2.9 million. There was a third deliverable that was not incorporated in the DBB study, and that was another, I think it was, $3 million; so overall about $6.

Chairman CHAFFETZ. Six million?

Mr. TILLOTSON. Yes, sir.

Chairman CHAFFETZ. And how much of the work did they actually do?

Mr. TILLOTSON. I can't tell you. I do know that the McKinsey team lead, the lead for the study was from McKinsey, and I don't know what the actual work split is.

Chairman CHAFFETZ. Mr. Rutherford, how much were you paid to do this study?

Mr. RUTHERFORD. $8 million.

Chairman CHAFFETZ. So you got $8 million, but you let out this contract for $6 million. How does that work?

Mr. TILLOTSON. I don't know. That's not how the numbers——

Chairman CHAFFETZ. Where did the other $2 million come from?

Mr. RUTHERFORD. I was just referring back to what—looked at our contracts for the totality of the full contract. I thought it was $8 million.

Mr. TILLOTSON. Excuse me. Let me correct myself. I think it was closer to $9, is what we actually wound up with. Sorry. It was an additional 6. That's why I'm remembering a $6.

Chairman CHAFFETZ. Oh, an additional $6?

Mr. TILLOTSON. Yes, sir, $6 plus $2.9. So it's about $9. That sounds about right.

Chairman CHAFFETZ. So $8.9- or $9 million, and McKinsey gets $2 million—or $6 million.

Mr. TILLOTSON. Right.

Chairman CHAFFETZ. Or $8 million, and we don't know what percentage of the work Ryan did.

Mr. TILLOTSON. I do not know percentage of the work Ryan did.

Chairman CHAFFETZ. Is that something you can figure out and get back to this committee?

Mr. TILLOTSON. I can certainly go ask. I'll have to go ask Ryan.

Chairman CHAFFETZ. Yeah. How in the world did you select Ryan Consulting? With all due respect—I'm sure they're nice people—if I have the right website, they got three senior people. Their head of human resources has a grand total of 6 years, and I'm sure that Tiffany Hollis, again, if I have the right website, is a very nice person.

Mr. TILLOTSON. I will get back to you with the answer.

Chairman CHAFFETZ. But how do they get such a contract? I mean, the Pentagon, we're talking about $600 billion or something in annual expenditures, and I'm rounding by big numbers here.

Mr. TILLOTSON. Yes.

Chairman CHAFFETZ. McKinsey & Company is a huge, massive company with a great reputation. I really am curious because I think we're starting to see where a lot of waste starts to go, right? What did we get for the $900,000 or million dollars that Ryan kept if the math you gave me already was working?

Mr. TILLOTSON. Sure.

Chairman CHAFFETZ. You give them 9. They give McKinsey 8. What did we get for that other million dollars?

Mr. TILLOTSON. I will get back to you and let you know how much work they put in.

Chairman CHAFFETZ. That's what I worry about. Even just doing a study, we can't figure out what we cost and what it didn't cost and who got paid and who did the work. And then we give a contract to somebody, with all due respect—and I'd love to look at their background, and we will—but how in the world did they even get the contract to start with, because you're going to need the expertise and the depth and the knowledge of a McKinsey to actually get it done? So if you could let us know.

Mr. TILLOTSON. Sure.

Chairman CHAFFETZ. I also want to know specifically from the time you decided to do this study to the time you actually let out the contract and actually McKinsey started working on it, because that's part of the problem: whether you're buying an F–35 or whether you're buying a study, again this is the problem in the bureaucracy of the Pentagon.

Let me go to you, Mr. Stein. I only have a minute left here. What's your biggest takeaway from all of this? You've got a lot of expertise. What's your biggest takeaway and maybe add to that what your biggest frustration is?

Mr. STEIN. The biggest takeaway is that the focus has to be on the warfighter, and the process has got to be a partnership between Congress and DOD. And I think we're all in this together, and there's a lot of work that needs to be done. And this is critical. The $20 trillion that one of the retired Chairman of the Joint Chiefs says is we got a $20 trillion——

Chairman CHAFFETZ. Yeah, but specific to this study. Come on. We've spent all this money. You've looked at this. You were the chairman. Now you're former chairman. What's working, and what's not working?

Mr. STEIN. Well, the key thing that works is you got to have heart surgeons, as I said, to help the DOD. There are only certain people that can do this type of work. And you need their help, and I will say that McKinsey did a great job, and I will say that there's a lot of work around—both uniformed and non-uniformed people in the DOD that did great work. But you need people like Kenny Klepper. If not Kenny Klepper, you need people that understand this process to make change. And once you figure out what those changes are, you got to coordinate between Congress and DOD, and you've got to change culture, and culture is tough to change.

Chairman CHAFFETZ. Thank you.

I now recognize the ranking member, Mr. Cummings.

Mr. CUMMINGS. Thank you very much.

Mr. CONNOLLY. Would the ranking member just yield for 1 second before he starts?

Mr. CUMMINGS. Of course.

Mr. CONNOLLY. I thank my friend and not to count against his time. I want to welcome a lot of my constituents from Herndon, Virginia, who are here watching a hearing, and we are delighted to have them here today.

Chairman CHAFFETZ. We welcome you all for being here, and you're very sharply dressed. Let the record reflect how sharply dressed, well, at least row four is. Thank you. We appreciate your attendance.

I now recognize the ranking member, Mr. Cummings.

Mr. CUMMINGS. Thank you very much.

Mr. Stein, you all volunteer for this, right?

Mr. STEIN. Yes.

Mr. CUMMINGS. That's what I thought. And how confident are you about the potential savings? You know, you were the chairman of the Defense Business Board when the study was conducted. Is that right?

Mr. STEIN. Yes, sir.

Mr. CUMMINGS. And I know how dedicated you are to these kinds of causes. But, you know, it just seems like we talk about this all the time, but it seems like we never get a hold of it. In other words, we talk about it, savings. We talk about overspending, but it seems that we can never—you know, we get a lot of good recommendations, but we never get there. Do you follow me? So, first of all, I guess, you feel pretty comfortable that the potential savings are there?

Mr. STEIN. I absolutely feel that the savings are there, number one. Number two, when we looked at this, our focus was, how do we do this without firing people? You know, you have almost 30 percent of the workforce retiring in the next 5 years, which, you know, this was 2 years back. You have 1 percent of the contracts is 65 percent of the—is a spend. You got 1,500 data centers in today's world of the cloud. And the big thing, Congressman, is everybody says that, you know, we are—the number is too low or the number is too high, but nobody sat in the room with us and with Kenny. And this is a process that I hope comes out of this, is people sit in the room and sit down with Kenny and go through the numbers, and we have to update the numbers.

But the numbers don't lie. And what we have got to do is adults sitting around—because this is for our kids and grandkids to get this right. There are not many times that we will have to get this thing right. And what I was saying is we do have $20 trillion of debt, and if interest rates go up 3 points, that wipes out the defense budget. What I'm saying is what I would love to come out of this is we have got very bright people in Congress, in DOD, and Kenny spent a year talking about—this was an unpaid job—he spent a year on this. And I think if we can work toward what he has done, his process, and seeing how we take advantage of that process, I think this country will be better off.

Mr. CUMMINGS. And I got that. Well, let me go back. You know, we have had all of these—I'm going to come to you in one second, Mr. Klepper, and you may want to answer this too. We have had all these instances—I haven't heard about any recently—where we are paying like $500 for a trash can. I mean, is that kind of waste and fraud—I see you laughing, Mr. Korb—I mean, are we still doing that?

Mr. KORB. When I was in government I had to handle the $500 toilet seat. I had to deal with that before Congress.

Mr. CUMMINGS. Must have been a hell of a toilet seat; $500 you said?

Mr. KORB. Yes, that was a big issue, and Senator Grassley and I were able to work together to stop that type of stuff.

Mr. CUMMINGS. Is that a large part of the problem, Mr. Klepper, do you think? In other words, you got a system that's just, it's almost on automatic—let me finish—then you got some old boys in there, too, hello, and they've been used to getting these contracts. And nobody, everybody wants folks to make a profit, but we don't want to be ripped off either. So I'm trying to figure out, do you see a lot of waste? What are you seeing? Anybody else on the panel that might be able to answer that?

Mr. KLEPPER. So we focused on, in the study, as far as the analysis, trying to find the areas where we thought there was the biggest opportunity to get savings quicker. You don't see big IT reengineering kind of things or multiyear projects. There's lots of savings through automation that you could have there. So we focused really on two areas: contract optimization and restructuring and an early retirement opportunity to avoid having to fire people. Big numbers on both sides.

Two key areas that we saw in the contracting piece, and it is there—the data is there. It's inescapable. One, and I think you heard some conversation, is there's a lot of tiered contracts. So somebody has a contract, and the only way you can get on the contract is you have to be a sub and maybe a sub of a sub and a sub. So what happens is, in the subs, it's like a credit card transaction fee. So, when you get down to the bottom, what did you actually pay for the service by the time it went through this bureaucracy, forgetting even the cost of the bureaucracy and all the people that worked all of those contracts——

Mr. CUMMINGS. That's what the chairman, that's what you were alluding to, right?

Chairman CHAFFETZ. Yes.

Mr. KLEPPER. So it's rampant, and it's massive. And so, when we looked at that, we went in specifically looking at those things because you can get at that, not necessarily even reducing contractors' services, looking at what you end up paying and going out and rebidding large-scale bids for like-type services and getting a much, much bigger rate, better rate at the same kind of services. So that was one of the key deliverables in the contract optimization component.

Mr. CUMMINGS. I see my time is up. Thank you.

Chairman CHAFFETZ. I thank the gentleman.

I now recognize the gentleman from Ohio, Mr. Jordan, for 5 minutes.

Mr. JORDAN. Thank you, Mr. Chairman.

Mr. Stein, you were chairman of the DBB when the Department of Defense commissioned you guys to do the study. Is that accurate?

Mr. STEIN. Yes.

Mr. JORDAN. And the goal was to look at how to make back-office operations more efficient, save money? That was the objective of the study?

Mr. STEIN. Yes, sir.

Mr. JORDAN. I just want to walk through the basics here, and as I understand it, you felt like you needed some help on a study of this size, so you worked with McKinsey. They did a lot of the work to come up with the findings. Is that right?

Mr. STEIN. No. The way it worked is I asked Kenny to lead this effort.

Mr. JORDAN. Okay. So the DBB led the effort.

Mr. STEIN. The DBB led the effort.

Mr. JORDAN. McKinsey helped.

Mr. STEIN. McKinsey helped.

Mr. JORDAN. Okay. And the conclusions were that you could save $125 billion in taxpayer dollars over 5 years at the Department of Defense. Is that accurate?

Mr. STEIN. Yes, sir.

Mr. JORDAN. And that savings meant that you could save money in back-office operations. That money could then go to upgraded weapons systems and to our troops in the field.

Mr. STEIN. Yes.

Mr. JORDAN. Great objective. I think that's exactly what we all want to have happen.

Now, so you get this study that says you can save $125 billion over 5 years and put the money in troops and better weapons systems. All sounds good. My guess is this wasn't the first study that the DBB had authorized the commission to do. You probably do studies all the time and have reports. Is that accurate? This wasn't your first study?

Mr. STEIN. This was not our first study.

Mr. JORDAN. So you do this all the time, right?

Mr. STEIN. Yes.

Mr. JORDAN. So all these other studies—you commission a study. You work with some outside group, maybe or maybe not. You get back the report. What typically happens with the report and all those other studies? What do you do with the report?

Mr. STEIN. They're put on the website, and they're distributed, bound and——

Mr. JORDAN. The DOD website, right?

Mr. STEIN. Yes.

Mr. JORDAN. Are they typically printed out, lots of copies published, wide dissemination? Does that all happen?

Mr. STEIN. Yes, sir.

Mr. JORDAN. Every other time you've done a study and got the conclusions, that's the normal course of business?

Mr. STEIN. Yes, sir.

Mr. JORDAN. Okay. Well, that sort of raises the obvious question: Did that happen with this report?

Mr. STEIN. I think it was taken off the website.

Mr. JORDAN. So all the other times, you use taxpayer dollars, you do a study, find out something important for taxpayers and potentially savings, there's a normal, normal way that information is presented to the public. DOD puts it on their website. They take that report; they print it. They make several copies; i.e., it's published. And it gets wide dissemination so we can learn the valuable information that we spent a lot of taxpayer dollars to get?

Mr. STEIN. Yes, sir.

Mr. JORDAN. In this case, was the report put on the website?

Mr. STEIN. It was put on the website and taken down.

Mr. JORDAN. Oh, so it didn't stay on the website?

Mr. STEIN. After I left the DBB.

Mr. JORDAN. And that's not the normal course of business, right?

Mr. STEIN. No, sir.

Mr. JORDAN. Okay. Was it printed?

Mr. STEIN. I think their people were told not to print the report.

Mr. JORDAN. So it wasn't printed. Mr. Tillotson looks like he's disagreeing based on his hand motion over there.

Mr. TILLOTSON. There's your printed report.

Mr. JORDAN. Okay. Was it widely disseminated, Mr. Stein?

Mr. STEIN. Kenny, you can talk——

Mr. JORDAN. Mr. Klepper?

Mr. KLEPPER. I don't know if it was widely disseminated. I know, after I left the board, I called back in and asked if I could get a printed copy, and they told me they were told not to print it. That's the first printed copy I've ever seen.

Mr. JORDAN. Mr. Tillotson, is that the only printed copy, or were there lots of copies?

Mr. TILLOTSON. There were lots of copies.

Mr. JORDAN. Really?

Mr. TILLOTSON. Yes, and they were distributed at the time and were available——

Mr. JORDAN. Why does the guy who chaired the DBB at the time the report was commissioned and at the time that the report was actually completed say that it wasn't widely disseminated, it wasn't printed, and was taken off the website?

Mr. TILLOTSON. So I have no idea why he wasn't given a copy of the printed report.

Mr. JORDAN. Why did The Washington Post report what Mr. Stein seems to be and Mr. Klepper seem to be saying here today and not what you're saying?

Mr. TILLOTSON. Because they also believe, as Mr. Stein believes, that it was taken off of the website. It was not. To be accurate, it was moved from one location to another location. It was never taken off the website.

Mr. JORDAN. Was it moved from a high-profile location to a somewhat less high-profile location?

Mr. TILLOTSON. It was moved to the meeting minutes location, which is publicly available. It's been downloaded 2,800 times since January of 2015.

Mr. JORDAN. Mr. Stein, is that consistent with how things are normally done with the other reports, the many other reports you've commissioned?

Mr. STEIN. This is to the best of my knowledge. I've not checked. Kenny, do you have any comment there?

Mr. JORDAN. Well, let's just assume you guys are—assume that what you are saying is exactly right, because I've got just a few seconds here. Tell me why; why the difference? Why was this report treated different?

Mr. Stein, why would it be treated different?

Mr. STEIN. I don't understand it.

Mr. JORDAN. Maybe it was the magnitude of the findings. Could that be? Seems logical to me.

Mr. Chairman, if I could just read one, we have an email from Deputy Secretary of Defense, Mr. Work, that he sent to the Secretary of the Navy, Mr. Mabus, and he says this. He criticizes a speech that Mr. Mabus made where he referred to the very report we're talking about right here. And he said: "There were problems with your speech." And let me just quote: "Senator McCain believes we can take a 30-percent reduction in management headquarters." He says to Mr. Mabus: "Your comments could easily be used by him and his staff as justification for the size of the cuts referenced in the report."

So maybe the reason it was treated different is because some folks at DOD didn't actually want this out there, this $8 million study that shows $125 billion in savings over 5 years? Could that be a logical explanation why it was treated different, Mr. Stein?

Mr. STEIN. I have no idea. I really don't. I left the DBB, and after I left DBB, I had no responsibility on what happened to the report. All I know is, if I was still chairman of the DBB, that report would have been——

Mr. JORDAN. Treated like it normally—like all the reports are treated, right?

Mr. STEIN. Yes, sir.

Mr. JORDAN. Thank you, Mr. Stein.

Thank you, Mr. Chairman.

Chairman CHAFFETZ. I thank the gentleman.

I now recognize the gentleman from Virginia, Mr. Connolly, for 5 minutes.

Mr. CONNOLLY. Thank you, Mr. Chairman.

And welcome to the panel.

Mr. Tillotson, it's your contention in response to Mr. Jordan's questioning that there was no attempt to downplay or hide or suppress the results of this study. Is that correct?

Mr. TILLOTSON. That's correct, Congressman.

Mr. CONNOLLY. How many copies of the report were, in fact, printed?

Mr. TILLOTSON. I can't tell you, but I will find out and let you know. I don't know I've been dropping them off every place I've gone since The Washington Post article came out because people have been asking. So we have a stack of them. They've been available throughout the period.

Mr. CONNOLLY. So have copies been made available to the current members of the DBB?

Mr. TILLOTSON. Yes.

Mr. CONNOLLY. You have one, Chairman Bayer.

Mr. BAYER. Yes, sir, I do.

Mr. CONNOLLY. So were copies made available to former members and the former chairmen of the DBB, such as Mr. Stein.

Mr. TILLOTSON. This is the first I've heard that anybody had not been given a copy when it was requested. So I can't answer.

Mr. CONNOLLY. So maybe we can accomplish something here today. Would you promise under oath, Mr. Tillotson, to make sure Mr. Stein and company have copies of the report?

Mr. TILLOTSON. Yes, Mr. Congressman.

Mr. CONNOLLY. I thank you so much.

Mr. Tillotson, in your testimony, you identify potentially $1.9 billion in savings under the IT rubric.

Mr. Rutherford, I believe the comparable number in your report, McKinsey's report, is actually $5 to $9 billion. Is that correct?

Mr. RUTHERFORD. I believe so, sir.

Mr. CONNOLLY. So, Mr. Tillotson, why the discrepancy? Why are you so low and McKinsey so high? And as you may know, this committee is pretty interested in the IT management and procurement issue, and DOD is the one agency that's been, from our point of view, a reluctant partner in compliance with FITARA, also known as Issa-Connolly.

Mr. TILLOTSON. The answer to your question, Mr. Congressman is I don't disagree with the numbers from McKinsey. I also don't disagree with the DBB report that suggests there are many more billions to find. What we have provided in the response to date is what we have actually put in place to date as opposed to other activities that we need to do.

Mr. CONNOLLY. Okay.

Mr. TILLOTSON. So we put $1.9 billion worth of initial work in the 2017 budget. In the 2018 budget, we added another 250 million, which I would acknowledge, by the way, to this committee is not anywhere close to what's possible. But there was a deliberate decision made as we constructed our discussions in 2018 to allow headroom for new administration to walk in and make decisions.

Mr. CONNOLLY. All right. Fair enough.

Mr. TILLOTSON. I think there is ample more dollars to be saved in the IT space alone that would even actually come up close to the total number McKinsey is suggesting we could achieve. I think we can achieve those numbers, which are kind of more in line with the DBB numbers.

Mr. CONNOLLY. Well, let me ask this, I would ask that you submit to the committee that potential plan. We would be very interested to see a little fleshed-out plan in terms of what are the savings we think we could strive for, not for the purpose of making you face the inquisition, but from the point of view, we want to get better compliance for FITARA across the entire Federal Government; you're the biggest.

Mr. TILLOTSON. I understand, Mr. Congressman. We agree with you.

Mr. CONNOLLY. Terrific.

Mr. Korb, I mentioned to you before the hearing, but for the average citizen, looking at a relatively indisputable number of $125 billion over 5 years, maybe at least, but all right, that is wasted in Pentagon spending or grossly inefficient. Why in the world would we want to add $54 billion to the Pentagon's budget this year when we haven't addressed the critical issue of efficiency? Why would we want to throw more good money after bad? If this were a civilian agency, I know my friends on the other side of the aisle would be all over it.

Mr. KORB. I agree with you, Congressman. In fact, my feeling is, if you give them the extra money, and as I mentioned in my testimony, it's not just the 54; they want to add $30 to the 2017 budget in addition to the $28 that the Congress has added in the 2017 NDAA. They won't do it. If you really want them to do this and make a full-faith effort to implement these recommendations, you cannot give them more money, because if you do, there will be no incentive to do it. And I think that's really the key issue.

I mentioned in my testimony about my work with former Secretary Laird. If you go back and you take a look at the Nixon administration when the defense budget was cut substantially, in today's dollars, it was like $350 billion. Look at the reforms they made under the leadership of David Packard. That's the point I'm trying to make, and I couldn't agree with you more.

Mr. CONNOLLY. And I would just add, because my time is up, but I mean, there is a huge opportunity cost too. So, in addition to throwing good money after bad potentially—I'm talking about by leaving waste unaddressed, this waste—we're also taking away from civilian domestic investments that are all so critical. So it's a double cost when we do this if we don't address this issue.

Mr. Chairman, I thank you for having the hearing today. I think it's a very important one. And I appreciate very much all of our witnesses being here.

Chairman CHAFFETZ. I thank the gentleman.

I will now recognize the gentleman from Florida, the chairman of our Subcommittee on National Security, Mr. DeSantis of Florida, for 5 minutes.

Mr. DESANTIS. Thank you, Mr. Chairman.

Thank you to the witnesses.

Mr. Tillotson, when the results of the study indicating these potential savings were revealed, what was your reaction?

Mr. TILLOTSON. My reaction was that the potential for the savings was certainly there, but the timetable was not going to be executable in a Federal Government setting. And I had long conversations with Kenny, with Mr. Klepper, at the time. Recognizing that the basis of his recommendation was largely a corporate model, he agreed. And part of that issue is because we have an interaction in the process that occurs both within the executive side of the Federal Government and then a subsequent interaction that occurs with Congress in decisions of significant magnitude that involve changing organizations and structures.

Mr. DESANTIS. I understand that. But at bottom, though, you do welcome—you did welcome the opportunity to try to save money and make the operations better?

Mr. TILLOTSON. Unequivocally. I think the study was well done. I think the work done by McKinsey was significant. In fact, we followed on from the McKinsey work to try and put better cost repetition in place so that we can get a better handle on these issues. So everything that was done in the study has actually now allowed us to form the basis of how we approach the problem going forward.

Mr. DESANTIS. To your recollection, who briefed the Deputy Secretary on the results of the study?

Mr. TILLOTSON. It was Mr. Klepper and Mr. Stein.

Mr. DESANTIS. Were you there when he was there?

Mr. TILLOTSON. Yes.

Mr. DESANTIS. What was his reaction?

Mr. TILLOTSON. His reaction was also positive.

Mr. DESANTIS. It was positive?

Mr. TILLOTSON. Yes.

Mr. DESANTIS. Then why did he ultimately dismiss the findings?

Mr. TILLOTSON. He did not. In fact, when the reference that was made to the email exchange in which he allegedly referenced or dismissed the findings, he was—he, Secretary Work, was actually addressing the fact that Secretary Mabus was raising the issue in public rather than bringing it forward as an internal conversation. And in the same email, I quote, from Secretary Work to Secretary Mabus: "There is absolutely nothing wrong with your call for the Department to get more efficient. It is timely and on point. I'd simply request that you continue to push internally to get the Department more efficient and focus your public comments on the Department of the Navy."

Mr. DESANTIS. And I did see that, and I appreciate that. So let me ask this: The Washington Post article claims that Deputy Secretary Work suppressed the DBB study from wider dissemination and tried to keep—now you have disputed that Washington Post story. Is it your testimony that this report received the fullest possible dissemination within the Department?

Mr. TILLOTSON. The report was discussed within the Department at the highest levels. It was discussed with all the senior leaders of the Department at the time. I will tell you I think there were——

Mr. DESANTIS. You said say it was widely disseminated.

Mr. TILLOTSON. Yes, sir.

Mr. DESANTIS. Is that your testimony?

Mr. TILLOTSON. Yes, sir.

Mr. DESANTIS. Was this study shown to the Secretary of Defense?

Mr. TILLOTSON. Yes, I believe it was at the DEXCOM meeting; it was discussed at the DEXCOM with Secretary of Defense at the time.

Mr. DESANTIS. Okay. And what was the reaction from the SecDef?

Mr. TILLOTSON. I think he was positive at the time.

Mr. DESANTIS. Okay.

Let me ask, Mr. Bayer, have you read the study?

Mr. BAYER. What I have read are the slides. I have not read the—it was never formalized into a completed study report.

Mr. DESANTIS. That was there—since you've become chairman, has there been discussion about limiting the distribution within

DOD? Have you been privy to—obviously, you read The Washington Post article, I am sure, when that came out.

Mr. BAYER. Yes. Absolutely not. It's never been limited. It's been available on the website from the moment it was briefed to the board and the public in January.

Mr. DESANTIS. You don't have a role? Your testimony would be you have no role in limiting it in any way? Is that correct?

Mr. BAYER. I didn't limit it in any way.

Mr. DESANTIS. Okay. And you didn't have any discussions with anybody at DOD about limiting the report, the dissemination.

Mr. BAYER. It was—having been on the Defense Business Board for a decade—perhaps a little context here is that we are—the board is tasked by terms of reference to do a particular piece of work: in this case, this effort, this effort. When that effort is completed, it is briefed to the public, and the chairman and the members of the committee then brief the other senior leadership in the Department, at which point, the board moves on to other work. From the time in which this board is—this effort was completed, the effort at hand, the board has done nine other pieces of work in the normal progression of things.

Mr. DESANTIS. So what is your response to the questions that were asked? You have some of these things that are publicly available, more prominent? This one is, I would say, a little bit harder to find location. Why is that?

Mr. BAYER. Well, very simply, there are three places on the Defense Business Board website where previous work is displayed. When you dial on to the website at the beginning, there is a banner of work that flies by. That's always the most current work. For a while, this effort was there, but it was——

Mr. DESANTIS. For how long? Do you know?

Mr. BAYER. I don't. I'd have to go back and look at——

Mr. DESANTIS. Was it still on when you took over?

Mr. BAYER. When I took over, it was on, but it was replaced by the next piece of work: "Fostering an Innovative Culture through Corporate Engagement and Partnership." It was always available on the minutes of that board meeting in January of 2015. It was erroneously listed as a report because, with the greatest respect, this is what a report looks like. It has all the context and the verbiage associated with the briefing and the deliberation of the board.

What was on the board's site at that time was this, which is now hardbound. That is a collection of slides. There is no narrative, no explanation, no discussion. And, further, every single page of this thing says on it: "The full DB report will later contain detailed text which will reflect the totality of the points discussed and modifications." Those were never delivered, and it was never put into final form. So that's why it stayed on the report section—on the minutes section of the meeting and not a report. It was never a report. It's a collection of slides.

Mr. DESANTIS. Well, my time is up. I think there will probably be some followup to that for some of our other members.

Chairman CHAFFETZ. Yeah. With the committee's indulgence here, Mr. Rutherford, was there ever a final report written?

Mr. RUTHERFORD. From the DBB's report?

Chairman CHAFFETZ. From the work you did, did you ever write a final report?

Mr. RUTHERFORD. Yes. So our deliverables from the final report we did in May were delivered to the DCMO; that was the work we did. The DBB report leveraged our baseline. We continued on after 2015.

Chairman CHAFFETZ. Those taxpayers paid you $8 million. Did you write a final report?

Mr. RUTHERFORD. We delivered a number of deliverables, both the baseline tools for them to leverage that going forward to actually measure the effectiveness. We gave them actually the breakdown of where the cost savings would be, where they should——

Chairman CHAFFETZ. I asked a pretty simple question: Is there a final report out there?

Mr. RUTHERFORD. There is a set of deliverables that we gave.

Mr. CUMMINGS. May I ask one question?

Chairman CHAFFETZ. Go ahead.

Mr. CUMMINGS. Did you complete the contract?

Mr. RUTHERFORD. Yes, sir, we did.

Mr. CUMMINGS. And how do you define completion of the contract? How is that defined?

Mr. RUTHERFORD. The contract asks for a number of deliverables. Number one was a baseline assessment of all of the six comprehensive support functions to the business board. So what we did is we provided a view of all of the numbers for the DCMO for them to measure on a go-forward basis where to spend across these six areas. In addition to that, we gave them a set of efficiency metrics they can use going forward to measure this baseline as they go forward.

Thirdly, we provided them a number of things when it came to where the cost savings may be.

Mr. TILLOTSON. If I may offer a point of clarity here, Mr. Rutherford is speaking accurately. The contract that was let was between the DCMO office and Ryan/McKinsey to deliver a series of information products, which includes a database, which included a number of documents. Those documents were there. They were not on contract—they were not on contract—to write a DBB report.

The DBB report, as Mr. Stein has indicated, is the responsibility of the Defense Business Board, and we delivered information from the government that we generated through McKinsey to the Defense Business Board for them to use as the basis of evaluation. So, when you ask if the—Mr. Chairman, respectfully, if you ask if they delivered a DBB report, the answer is no, they did not, but it was not their job to do so. Did they deliver the things we requested in the contract? Unequivocally yes. I have those documents. Those are separate documents.

Mr. CUMMINGS. I just have one more question.

Mr. Klepper, do you agree with this, this report slide thing? See, I'm confused——

Mr. KLEPPER. I can offer some clarity.

Mr. CUMMINGS. Yes, offer some clarity, because I'm used to a contract says you do certain things for a certain amount of money and you deliver them, period. So is this something that's open-ended, by the way?

Mr. TILLOTSON. No, sir. There were specific clean deliverables. We got those deliverables, and those were delivered.

Mr. CUMMINGS. And then——

Mr. KLEPPER. Some of this is new information to me. I can tell you about the report. The final report was being written. It was almost completed. I was waiting for it, and then I had made a decision to leave. And they were very close, because I was going to proofread, go ahead and do a proofread. So we were very close; they were working on it. So I called back, and I said—it was a few weeks later—I said: "Have you finished your report? Can I take it?" And the officer that was working it said they were told to stand down. So never got it.

Now this document that David's got, that's the first time I've seen it. I can't answer what happened after that.

Chairman CHAFFETZ. So I think it is safe to say that this thing you were waving around, Mr. Tillotson, this is not the report, is it?

Mr. TILLOTSON. That is all I have is a report.

Chairman CHAFFETZ. Yeah. It's not a report. It's a slide deck. In fact, it refers to a report that's forthcoming that never—didn't get produced. And we spent $9 million and never did get a report. Is that accurate?

Mr. TILLOTSON. No, that's not accurate.

Chairman CHAFFETZ. Where is the report? Where is the report?

Mr. TILLOTSON. So, with all due respect, Mr. Chairman, again, the contract wasn't to deliver a DBB report. There is no——

Chairman CHAFFETZ. You can keep going in circles. We paid $9 million of taxpayers' to get a report. You started flailing around saying, "Here it is; it's printed." This is a slide deck; it's not a report.

Mr. TILLOTSON. With all due respect, Mr. Chairman, the contract specified——

Chairman CHAFFETZ. No, don't give me—did you report—did they develop and produce and publish and put on the internet a report? Yes or no?

Mr. TILLOTSON. McKinsey did not put a report on the internet, nor were they——

Chairman CHAFFETZ. This is why we're having this hearing, and this is why you're overseeing a Department that is in chaos.

Mr. TILLOTSON. —nor were they contracted to do so, with all due respect, Mr. Chairman. They were not——

Chairman CHAFFETZ. I will now recognize Mrs. Watson Coleman of New Jersey.

Mrs. WATSON COLEMAN. Thank you, Mr. Chairman. I thank you for holding this hearing today.

The topic of waste within the Department of Defense is vitally important, and it deserves our utmost consideration, especially considering that President Trump's budget proposal is stripping other parts of the Federal budget to fund the Defense Department by an additional $52 billion.

Dr. Korb, during your January appearance before the Senate Armed Services Committee, you began your written remarks by noting that, in the defense budget, and I quote, "dollars are policy." Shifting $52 billion from other Federal programs speaks loudly about policy priorities, does it not?

Mr. KORB. Yes, it does.

Mrs. WATSON COLEMAN. Thank you. This committee has a duty to ensure that we are effective stewards of the taxpayer dollars, and that also includes ensuring the effectiveness of the programs that Congress funds.

Mr. Klepper, it sounds like one of the findings of your study was that the Defense Department has significant inefficiency and waste in its business processes. Is that correct?

Mr. KLEPPER. Yes, ma'am.

Mrs. WATSON COLEMAN. Dr. Korb, do you agree that Defense Department could implement changes that would result in billions of dollars of efficiency savings?

Mr. KORB. Yes. It is. And I testified before that, before the Senate Armed Services Committee, and one of my colleagues here, Mr. Tillotson, mentioned a report that I just did last week on this.

Mrs. WATSON COLEMAN. Thank you.

Instead of looking for efficiency savings at the Defense Department, President Trump's so-called skinny budget released last week slashes critical domestic programs to provide more than $50 billion in additional funding to the Defense Department. Despite the President's claim that this budget "puts America first"—and I put that in quotes—based on recent reporting, the budget would actually hurt some vulnerable communities, such as low-income and elderly Americans. For instance, the budget would eliminate funding for the Appalachian Regional Commission, a program in 13 States that has, since 1965, provided funding used to promote economic growth. Most recently, it has helped to retrain coal miners who have lost their jobs.

Dr. Korb, would you agree that it is important for the Federal Government to spend its dollars wisely?

Mr. KORB. I certainly would.

Mrs. WATSON COLEMAN. And one way to do that is to measure a program's effectiveness. Is that not correct?

Mr. KORB. That's correct.

Mrs. WATSON COLEMAN. The Appalachian Regional Commission cites a dramatic decline in poverty rates in Appalachia from 30 percent to under 17 percent between 1960 and 2017, a substantial reduction in the number of high-poverty counties from 295 to 84 during that same period.

Dr. Korb, assuming those numbers are correct, that sounds like the program has been working for America, does it not?

Mr. KORB. It certainly does.

Mrs. WATSON COLEMAN. The President's proposed budget would also eliminate funding for the Low-Income Home Energy Assistance Program, which helps low-income people pay for heat in the winter. It would also cut funding for the 21st Century Community Learning Centers, which helps fund afterschool programs serving more than 1.6 million children nationwide, and reducing Meals on Wheels, where millions of meals have been delivered to the vulnerable and the elderly.

Mr. Chairman, while I agree that we should provide the warfighter with everything that he or she needs, I do not believe that should come at the expense of critical domestic programs that serve our Nation's most vulnerable.

I agree that the dollars are indeed policy. So some of these dollars should go to the neediest of Americans.

And, with that, I yield back.

Thank you, Mr. Chairman.

Chairman CHAFFETZ. I thank the gentlewoman.

I will now recognize Mr. Issa of California for 5 minutes.

Mr. ISSA. Thank you.

I'm going to pick up a little bit where the chairman left off, no surprise. Yes, sir, it's you. You said there was a contract for a report. Who determines when you put the word "report" onto a PowerPoint stack? I know that terms are loose, but this thing purports to be a report in hard printing, right?

Mr. TILLOTSON. Yes.

Mr. ISSA. But it's not a report?

Mr. TILLOTSON. It is the report to the extent that one exists for this study by the Defense Business Board. And the answer as to who owns that is the Defense Business Board owns that product, and we provide support, administrative support, to the board when they do that. The information from McKinsey was government information that we would provide to the Defense Business Board as we would to the Defense Science Board or anybody else.

Mr. ISSA. Okay.

Let me go to the chairman for a second. This is a new era, and I think we've got to ask some tough questions. And I support this money being used. If I calculate it roughly, right, as an old Army guy, those 50 brigades would be over 100,000 men that we would be able to add in end strength. That's basically a full rotation, a whole group of people that don't have to redeploy in a given year if we had that many more in the Army. So this is the difference between Army people finding themselves coming and going back and forth to combat when you look at 50 brigades. I didn't focus on the other two branches; I'm not as familiar with them.

So, Chairman, let me ask a couple of questions. One of them was it was stated that they lost focus. Mr. Tillotson, I think, said that. How do you lose interest in $125 billion once you identify that number?

Mr. BAYER. Which of us do you want to answer that question?

Mr. ISSA. I'm sorry, Chairman Bayer, I thought—two chairmen, but only one has a title underneath there. But I'll take both of you. How do you lose interest once you recognize, even if it's not in a report but a stack of PowerPoint, how is it you lose interest in saving $125 billion?

Chairman Bayer, I'd like you first.

Mr. BAYER. Well, Mr. Chairman—I'm sorry. Mr. Issa, we don't lose interest in saving money. The board was formed 15 years ago. It's done far more than 100 pieces of work, all of which the great sweep of that work is about how the Department can do things more efficiently.

Mr. ISSA. Let me go through a question then because, obviously, this is a little bit like—it is an economic 9/11, if you will. On 9/11, we didn't connect the dots; so the bad guys bombed our country with our own aircraft.

So let's talk about $125 billion. Did you connect the dots between you and the appropriators or any other Members of Congress so we would know there is $125 billion in savings in your report—in your nonreport—that we could have had?

Mr. BAYER. That would have been done under the previous chairman, who served for an additional 90 days after that effort was voted out of the——

Mr. ISSA. No. My question is did anyone, not—are you saying you don't know?

Mr. BAYER. Well, I prefer to defer that to Chairman Stein at that time.

Mr. ISSA. Chairman Stein, did you report to Members of Congress, who would have been able to reprogram 125 billion if they took advantage of these savings?

Mr. STEIN. Well, first of all, there's—and this is the first time I have heard this, the difference between slides and a report, but we fully approved a report, this—I left after 90 days, and we started to move out to make—talk to Congress, and then we were stopped.

Mr. ISSA. Okay. Who stopped you? Who stopped you from telling Congress there were 100,000 men that could be deployed with this money?

Mr. STEIN. The best I—and remember these numbers are compounding. So, if you save a billion this year, it will be $2 billion——

Mr. ISSA. You mean eventually a billion here, a billion there, it adds up to real money? It's still true——

Mr. STEIN. It adds up to real money. This is real money.

The thing I want to make sure of, first of all, I will say, and I want to make this clear, this was the first ever that a—the work that McKinsey did was important. It's the first time it was ever done. So I just want to make sure that that is said.

The second thing is we had full approval in a public hearing on this report and Ash Carter or you know, we were told that——

Mr. ISSA. But I asked you who stopped it.

Mr. STEIN. We don't know. I was asked——

Mr. ISSA. Let me ask more than a rhetorical question because I'm going to run out of time, Chairman. How do we on this side of the dais ensure that never again are there tens or hundreds of billions of dollars in savings that the American people are denied because some unknown person in the Department of the Defense puts a kibosh on it for whatever reason and Congress doesn't find out about it? How do we stop that from happening? What law do we have to pass to guarantee the transparency to that gentleman or to the appropriators or to whoever in Congress so that in fact the American people never get a raw deal after good money has been spent to study something that could save the American people or at least save American lives by plussing up our military?

Mr. STEIN. I will say two things: Look, when I left, Mr. Bayer took over as chairman, and he didn't want to continue this. Secretary Carter did not want to continue this. So let me say the second thing here is that we have—and you're a businessman, Congressman. You know, having a great plan is one thing; having people that can implement it is another. You have one of the great people here that spent a year working on this. And you have McKinsey who spent a year and the people Scott had involved were as good as you can get. What I'd like to do is get people in the same room with Kenny Klepper, whoever that might be—and that's the one thing that frustrated me is not the same people would sit in a room, and they disagree or agree, but we're talking about very important things and nobody will get in the same room. And I'm saying that Dave Tillotson is as good a person as you can find. Bob Work is as good a person as you can find, and the antibodies got us. And the antibodies is going to kill this country if we don't stop. We have got to change culture, and we have got to make things happen.

Mr. ISSA. Mr. Chairman, I only ask that you and the ranking member and all of us commit ourselves to make sure that we never again allow the absence of this body knowing that there is an opportunity on a study like this and never again allow it to be buried. Certainly this is an example where I wish an IG had brought it to you, Chairman and Ranking Member Cummings. But since they didn't, I look forward to working with you on mandating that in the future so it can't happen again.

Chairman CHAFFETZ. Thank you.

And, Mr. Stein, just to clarify with the questioning from Mr. Issa, was there a final report that you had approved that did not get published?

Mr. STEIN. The best I know—and this is process now, and I want to make sure—we approved in a public hearing this report. It was fully vetted, fully—right now, you know, these guys are saying something different. I'm not technicalities, but when somebody talks about $125 billion, you had a change of Secretaries and you had change of chairmen. This chairman didn't want to pursue it, and the Secretary didn't want to pursue it. I can follow that. What I'm saying is we spent a year. We met with almost 80 executives in and out of the Department. We worked well with Dave Tillotson, and I give him a lot of credit. I give Bob Work a lot of credit, and I give the McKinsey team a lot of credit, and I give the most credit to Kenny Klepper. These guys bled their life for this for a long time.

Chairman CHAFFETZ. Mr. Stein, I'm trying to get real clear here. This is a slide deck. Is this the final report, or was there a different report that was not published?

Mr. STEIN. I have not seen that. I have not seen that.

Chairman CHAFFETZ. We'll hand it to you.

Let's now go to Mrs. Demings of Florida is now recognized.

Mrs. DEMINGS. Thank you so much, Mr. Chairman.

Mr. Tillotson, in your testimony, you indicated that, after the recommendations from the study or report came out, that you did address some IT inefficiencies but that you did not go as far as the study recommended. What are some examples of some of the other recommendations that you chose not to implement?

Mr. TILLOTSON. So, actually, it's not so much that we didn't choose to implement. There's a time interval to get the work done to do the implementation. So, in the report—slide deck, whatever version you'd like—in the report, there is actually work required to be done to go put the details into place. We started on some of the obvious things that actually Mr. Klepper and Mr. Stein have already mentioned, like data center consolidation. There is a broader set of activities that regard moving information into a cloud environment that we would need to pursue. We did look at contracts for enterprise license agreements. So we looked at some of those. So part of this is just time phase for implementation.

We did take on consolidation of some of the medical IT systems. We abandoned some of those. So there was reduced—cost savings in that activity, and there is more to be done in that. We are actually continuing to work that. So we viewed this much—by the way, the recommendation the DBB did, that this was going to take a period of time to do. Again, commercial time schedule one thing; government time schedule another. But the answer is it is not work that ends; it is work that goes on.

Mrs. DEMINGS. Mr. Klepper, you said: "The money is there, but can we get the agency out of the way to move forward?" What did you mean by that?

Mr. KLEPPER. You know, as I go in there and look at this enormous waste at a time where, no matter where you want to spend the money, we see this happening. And there is this sense of helplessness; we can't fix it. I just have to believe that if we could show the aggregate economic impact to the Nation, not just the Defense Department—but these budgets are fungible; as you know, they bleed over into other areas—that if we could identify the savings and with clarity show the roadmap to fixing things, to getting to the savings, and identify for Congress those things that we need Congress to help us with. A lot of this is unintended consequences of policies and laws to solve one problem that created big inefficiencies and bureaucracies; it just happened. Nobody has ever measured this. So nobody has ever seen the aggregate historical financial consequence of those things over many years. So my belief—maybe I'm an optimist—I just believe that there is so much money here, and we are so desperate in need for these funds, if we can make the case to Congress and to the leadership of the Defense Department of the things that we need help with, that people will help us. Now, are we going to go from the very little savings that we had in the 2 years since this study was published to 125? There's more than that. Or is there going to be somewhere—I think the answer to that range between Scott's 60 to 80 and where I think we have a real possibility is in, can we work together to move self-imposed barriers out of the way to let us do that? And I just believe we can. I'm not ready to give up.

Mrs. DEMINGS. Mr. Korb, as you know, last week, the Trump administration released the budget proposal that would increase defense spending by 54 billion. At the same time, the budget would cut the State Department and U.S. Agency for International Development's base budget by 28 percent, the largest cut of a department the size of the Environmental Protection Agency. As you know, our national security is paramount, but the Trump administration fails to recognize how these draconian cuts make America less safe.

Last month, 120 retired generals and admirals wrote a letter urging Congress not to slash the funding for diplomacy and international development. They stated, and I quote: "The State Department, USAID, Millennial Challenge Corporation, Peace Corps, and other developmental agencies are critical to preventing conflict and reducing the need to put our men and women in uniform in harm's way."

Mr. Korb, would you agree with that statement?

Mr. KORB. I certainly would agree, and I would also add the Environmental Protection Agency because our military leaders have said climate change is a threat to national security. And essentially the Defense Department is not the only agency that provides for national security. As you pointed out, all of these other agencies do contribute as military people know full well.

Mrs. DEMINGS. Thank you. When he was Commander of Central Command, Secretary James Mattis spoke to Members of Congress stating, and I quote: "I would start with the State Department's budget. Frankly, they need to be as fully funded as Congress believes appropriate because if you don't fund the State Department fully, then I need to buy more ammunition ultimately." Mr. Korb, would you agree with Secretary Mattis' assessment?

Mr. KORB. Absolutely. And I hope that he continues to make that case to the President now that he's a Cabinet officer.

Mrs. DEMINGS. Is it fair to say preventing military conflict through diplomacy would cost less than engaging in it?

Mr. KORB. Very definitely.

Mrs. DEMINGS. Foreign aid is a popular target for those who say they want to seriously cut down on waste. However, many Americans may not realize foreign assistance makes up less than 1 percent of Federal budget.

Mr. Korb, is that right?

Mr. KORB. That's correct.

Mrs. DEMINGS. Are there national security implications that result from slashing foreign aid for our allies or humanitarian efforts?

Mr. KORB. Very, very definitely.

Mrs. DEMINGS. The Trump administration says that these extreme budget cuts for diplomacy are about putting America first, but America has a lot to lose if we stop making smart investments for our own global security.

Thank you very much.

And I yield back, Mr. Chairman.

Mr. PALMER. [presiding.] I thank the gentlelady.

The chair now recognizes the gentleman from Oklahoma, Mr. Russell.

Mr. RUSSELL. Thank you, Mr. Chairman.

And thank all of you gentlemen for being here today.

Mr. Tillotson, in the course of evaluating savings and a lot of the other things, I want to try to get back to some of the evaluations that were examined. How many positions currently filled by contractors could be filled by uniformed Active-Duty personnel?

Mr. TILLOTSON. I can't give you a number. And I would also answer that I would not necessarily fill those positions with uniformed personnel. In some cases, if we were going to replace them, we would fill them with contractors—pardon me, with civilians.

I'll be honest with you, Mr. Chairman—or Mr. Congressman—the issue that we are faced with in the Department is to look at the appropriate labor mix, and I do think one of the things that I'm in complete agreement with Mr. Klepper and Mr. Stein on is an aggressive review of our contracts to just see whether we need them at all.

Mr. RUSSELL. Well, I think there's a whole array of issues: nondeployability, efficiency, base salary. I mean, there's a number of things that we can see for efficiencies. And I'm just surprised that you would not have any type of estimation of a number. I mean, since we're saving money by keeping contractors, which I would dispute, we ought to have some idea of what percentage or what numbers some of that might be.

We see a continued decline on our military personnel, and yet we see a continued increase in bloat of the bureaucracy. Do you not see that as a problem, Mr. Tillotson?

Mr. TILLOTSON. I do see that as a problem, Mr. Russell. And I agree with you that—what I don't agree with is I don't see that the contractors are necessarily a savings. I think if I hire a contractor for a very finite job and they are done, then that's cheaper than hiring a full-time employee of any kind.

Mr. RUSSELL. Unless they can't perform the mission.

Mr. TILLOTSON. Unless they can't perform the mission, in which case it is inappropriate; I agree.

Mr. RUSSELL. Mr. Rutherford, in your analysis with McKinsey, you looked at a wide array of things. Did your baseline show any savings by replacing contractors with uniformed personnel or what those mixes might be, or did you examine any of that? I know you did examine both military and contracting personnel. Did you see any savings there?

Mr. RUTHERFORD. When we did our comprehensive assessment on the actual savings and we looked at the different business processes, we looked at changing demand management, changing actually the contract, the contracts within themselves, and renegotiating those, where you could do automation like Mr. Klepper talked about. We did not look at whether or not you could replace contractors and military personnel. What we looked at is where the compressible spend was within those different areas and that there was opportunities for savings within the contract services.

Mr. RUSSELL. Secretary Korb, if you don't mind me using that title in deference to your long service to our country—and I actually remember when you were in that capacity as a young soldier—when you were serving in the Navy, was it possible for a seaman to do a contracting personnel job more efficiently with less expense?

Mr. KORB. I would say very definitely.

Mr. RUSSELL. I suspected you might say that. And I guess, Mr. Klepper, I'm just amazed at your background and how you've been able to rescue what should have been destroyed and yet is resurrected from, unfortunately, the ashes. As you evaluated the structural and management processes of this problem, did you determine that there would be any efficiency in savings by replacing contractor functions with military personnel as a way to get at net saving?

Mr. KLEPPER. No, sir. What we actually did was a little bit the opposite. We looked at productivity and savings, and we did not touch any uniformed positions. So, if you look at all the savings that we listed, they were all nonmilitary—non-uniformed——

Mr. RUSSELL. Was this assuming though a steady line of military units, or did it take constant folding of flags and mothballing of ships and parking of aircraft?

Mr. KLEPPER. I'm not sure I understand that.

Mr. RUSSELL. Well, okay. So, as you're studying this, and you are looking at maybe we want to keep this contract, but as you lose a unit, then—would you take that into account, or was it a steady state of end strength that you made these evaluations on?

Mr. KLEPPER. We made it on a steady state of end strength. So we took—if I may, just for a second—the math, was we took the prior year—which, by the way, an important point here was 2013 actual; so the study needs to be updated. But we took 2013 because I needed a full year's savings, and we extrapolated that over a 5-year period for productivity.

Mr. RUSSELL. I would argue, and having been in the military myself, from 2013 to 2017, we've diminished our Armed Forces a great deal, and we are putting our Republic at risk in its defense. I would be the first to say that we need to reform contracting; we need to find saving. But I also think that when you pay a specialist E–4 or a seaman E–4 something like that, a sailor, at $24- to $30,000 a year, they can probably do the personnel job cheaper than a contractor. Would you agree with that or not?

Mr. KLEPPER. I would. And just if I could build on that point, the other piece that is the really big lever here is automation and compute power, where you have a higher intellectual worker versus low-end people doing papers and things, and I think there the opportunity for military personnel to self-serve is sort of an aspirational state that you would design to. So they can configure the changes they need without filling out forms and sending it back to come back months and months later to put self help. If I were going to improve, increase the amount of service that uniform did, I'd do it through upping the intellectual level of value and providing the automation tools that they could interact with much, much more efficiently.

Mr. RUSSELL. Thank you.

And thank you for your indulgence, Mr. Chairman. I yield back.

Mr. PALMER. I thank the gentleman.

The chair now recognizes the gentleman from Maryland, Mr. Raskin, for 5 minutes.

Mr. RASKIN. Mr. Chairman, thank you very much.

Mr. Korb, let me start with you. Is there an inspector general at the Department of Defense? Is that a person that we would rightfully expect to be doing the kind of work that the volunteers with the Defense Business Board have been doing?

Mr. KORB. Well, they would do some of it, but when you bring in groups like the Defense Business Board, they are people who understand how big organizations run. I mean, the inspector general a lot of times deals with waste, fraud, and abuse or, you know, people are not behaving themselves. You could ask them, but I do think and these gentlemen all—and men and women serve on there are nonpaid, and they bring—my experience has been they bring great expertise to help us because, a lot of times, you need somebody from the outside to——

Mr. RASKIN. To take a look from the outside.

Mr. Tillotson, let me ask you, did we waste $8- or $9 million of the taxpayers' money on a report on identifying waste in the Pentagon? And if we didn't waste it, what have been the savings that have come out of this report?

Mr. TILLOTSON. I don't believe we wasted the money. I think the work that was done that was actually contracted has been high payoff, and we continue to build on it. My direct answer to your question is to date we have loaded in approximately $7.9 billion worth of savings over the next 5 years based on the results of that study alone and eliminating any other savings that we've been doing in prior years?

Mr. RASKIN. So it's a good start, you are saying, around 7- or 8 billion.

Mr. TILLOTSON. And I will continue to reiterate my position that this is not a one-and-done activity.

Mr. RASKIN. Okay. Forgive me for interrupting; we just have limited time. My concern is I represent the Eighth Congressional District in Maryland, which includes NIH, which is now slated for a $6 billion cut. These are the scientists who are trying to rescue the population from lung cancer and breast cancer and colon cancer and cystic fibrosis and asthma and these killer diseases. And just cavalierly we would just slash $6 billion from the NIH when we have a report 2 or 3 years old now saying we could save $125 billion just by reducing bureaucratic bloat and contractor fraud and waste and abuse and overruns. I looked into the history of that last night. This goes back to the 1960s, the cost overruns, and the 1980s, with the $2,500 coffee makers and $600 toilet seats, scandal after scandal after scandal.

I want to ask someone—maybe, Mr. Korb, let me come back to you, you have a long history in the military—you know, when you have that kind of systemic repeat dysfunction over the decades, you've got to believe it's not totally pathological; it's working for somebody. Who is this system of bloat, waste, fraud, and corruption working for?

Mr. KORB. Well, unfortunately, it works for the individual groups. The real problem you have obviously——

Mr. RASKIN. When you say "groups," you mean which groups?

Mr. KORB. You have organizations, and in the Department of Defense and the history, the services have not wanted to give up functions to the Office of the Secretary of Defense to the extent that they should. You have basically—you have people, as I pointed out in my testimony, you've got a Defense Logistics Agency, but the services won't give up a lot of their logistics function. I used to argue with them all of the time to let us manage that. I think you have—and I mentioned this, too, creating all these Under and Assistant Secretaries. My goodness, I mean, why do you need that many people up there in the Office of the Secretary of Defense, and we keep creating them.

And as I've looked at that, the real key to running it correctly and making the savings is when you have a strong Deputy Secretary of Defense. As I mentioned earlier, David Packard came in from Hewlett-Packard, and Google back and you look at the fact we didn't have the cost overruns. Our budget was half of what it is now. And I tell you who else was very effective; when Dick Cheney was Secretary of Defense and brought in Don Atwood from General Motors. It was very well done. But when you don't have that strong deputy in there, it becomes very, very difficult.

Mr. RASKIN. Okay.

Mr. Klepper, you talked about changing the culture at the Department of Defense. What are the concrete steps that can be taken legislatively by Congress to help shock the system and change the culture so the taxpayers are getting their money's worth and we are not wasting our money in this way?

Mr. KLEPPER. As the guy that's had a life as a change agent, that may be the biggest question I've heard today because, when you look at large cultures that have—often an organization as big as DOD is not one culture; it is a whole bunch of tribes out there that have their own cultures because the size of it—there are three key things I will always say to focus on, is that, if you want to change the behaviors, it starts with leadership, and it is what gets recognized, reinforced, and rewarded. And to the extent as we worked our study across the institution, there is almost no trace—there are no metrics of productivity or reliability. There are mastery skills in appropriations. So I would say the key would be start with the head, and it would be that there is accountability for real measures of productivity.

And as a leader in an organization, the most important people that you can influence are your direct reports because, as you look through the chain of command—and it is a long one in an organization the size and complexity of Defense—anywhere in the chain of command you fail to get the support, the recognizing, reinforcing, and rewarding of these kind of values, it creates a black hole in the organization. A black hole is where change goes to die. So I would put enormous emphasis at that part.

The mechanics, the operation, the skill sets: we can get that. There's lot of talented people that we can bring in to do that. But if it is not driven from the top, reinforced, recognized, and rewarded, its odds of sustaining fall really, really dramatically. That is certainly true in the commercial, and I think that's human nature.

Mr. RASKIN. Thank you.

And I yield back, Mr. Chairman.

Mr. PALMER. I thank the gentleman.

The chair now recognizes Mr. Blum from Iowa for 5 minutes.

Mr. BLUM. Thank you, Mr. Chairman.

Thank you to the panel for being here today. I'd like to read something to you; in fact, I'll read it twice. The Department of Defense remains the only Federal agency that can't get a clean audit opinion of its statement of budgetary resources. Once again, the Department of Defense remains the only Federal agency that can't get a clean audit opinion of its statement of budgetary resources.

I'm from the private sector. I am a businessman. I'm a CEO of a public company. I understand audits. I understand clean audits. Taxpayers have invested $6 billion of their money over the last decade trying to fix the audit problem at the Department of Defense. We did a little research, and I found out that the Department of Defense has the world's largest accounting and finance organization of any company, any organization, in the free world, the largest. It doesn't seem to me to be a lack of resources. Will somebody, anybody—maybe we'll go one by one—please tell me, please tell the taxpayers, please tell my constituents in the State of Iowa why we can't have a Department of Defense that has a clean audit? Mr. Tillotson, let's start with you. And I'm very interested in these answers.

Mr. TILLOTSON. No problem, Mr. Congressman. And the direct answer to your question is I find the situation to be unacceptable as well. I have been working very steadily since I was moved up to OSD to try and put a lot more stick and rudder into getting the audit position cleaned up. I agree with you: it is an unacceptable position.

Mr. BLUM. Who do you report to?

Mr. TILLOTSON. I report to the Deputy Secretary of Defense.

Mr. BLUM. Do they agree it is unacceptable?

Mr. TILLOTSON. Yes.

Mr. BLUM. To your knowledge. Who do they report to?

Mr. TILLOTSON. The Secretary of Defense.

Mr. BLUM. Do they agree it is unacceptable?

Mr. TILLOTSON. The current Secretary agrees it is unacceptable. And so the answer to your question is the very size of that organization—this will go to the point that I'm sure Mr. Klepper will build on—when we look at the business practices of the Department within financial management, when we did that research with the McKinsey folks, it is the very size and kind of age of that process and the skill set of the people who are doing it that actually stand in our way, coupled with, candidly, our failure—and I'm going to say it this way—to enforce sound business practices in the nonfinancial community. We have very good rules, and sometimes we don't follow them. So I'm not going to sit here and make an excuse for you. The answer is we are working to fix that, and I agree with——

Mr. BLUM. Thank you for not making an excuse. I appreciate your candor.

Mr. Rutherford?

Mr. RUTHERFORD. Thank you, sir. We are not an accounting firm, and the focus of our effort was really on the cost savings potential. But with that said, when we came in, one of the big deliverables that we did—with any cost savings effort—is having an authoritative data set, to having real numbers that everyone can agree to that this is the baseline. We spent an inordinate amount of time making sure we developed that so we could leverage it on a go-forward——

Mr. BLUM. Does the Department of Defense pay their bills with checks, or do they pay their bills with cash? They use checks I assume, right? How can we not know where the money goes? How does that happen?

Mr. RUTHERFORD. We had to pull from 20 different data sets, one view on this, and on that view, it had over 5 million lines.

Mr. BLUM. Does that go back to the tribes we were talking about 5 minutes ago?

Mr. RUTHERFORD. And also to this, where the IT and where the data sits—it is a part of what Mr. Klepper was talking about as well—is just, how do you actually have a view of what the true spend is, and how do you actually take metrics on a go-forward basis to measure that over time to see if you're making——

Mr. BLUM. If we started cutting people's pay at the top, not the enlisted man, would this problem get solved? Maybe that's what we need to do.

Mr. Bayer?

Mr. BAYER. Mr. Blum, I had a substantial career on being on boards of directors of publicly and privately traded companies. So my diagnosis of the situation is that it is appalling, and it's all a direct result of leadership. If you—I would encourage you to take a look at the transition report that we offered the incoming administrations. We offered it to the team of Hillary Clinton. We offered it to the team of Donald Trump. We said that the challenge in the Department is getting a hold of its fiscal destiny, and the way you do that is put people who have business training expertise in these jobs.

Mr. BLUM. How many years have you been saying this?

Mr. BAYER. A long time.

Mr. BLUM. Is anybody listening? Is Congress listening?

Mr. BAYER. Trying to find some light in the darkness, the current Secretary, Jim Mattis, was at the time, when I chaired the Business Board the last time, was the chairman of Joint Forces Command. The Business Board felt very strongly that the Department had an excessive command infrastructure, one of which was Joint Forces Command. And we recommended to the Secretary of Defense at that time, Bob Gates, that he shut down Joint Forces Command. The Commander was General Jim Mattis. He embraced it and thought it was a spectacular idea and led the reformation.

What I find now is that he has picked an individual, if press is accurate, that he has picked an individual to be the deputy who has had a lifetime of being a chief operating officer and, frankly, a very tough customer about wringing out costs and achieving accountability in a very large defense aerospace company. I haven't met this guy; wouldn't know him if he came in the room. But what I have read about him on the internet leads me to believe that, perhaps, General Mattis is in, fact, embodying the recommendations that we made, picking really tough people to run these positions. The deputy is critical in that—who is Mr. Tillotson's boss. So I think it's all about leadership. It's all about toughness, and it's all about making it important. If it's not important, it's not going to get done, and you know that.

Mr. BLUM. I'm happy to hear that. Maybe there is light at the end of the tunnel.

Mr. Chairman, can I have—would you indulge just to have the rest of them answer, very briefly?

Mr. PALMER. The witnesses may answer.

Mr. BLUM. Try to keep it brief.

Mr. STEIN. I'll go quickly and answer your specific question. It's responsibility, and it's: Be determined to get this done. If it is determined to get it done, it will get done.

Mr. KLEPPER. I would repeat the leadership emphasis. I would also say that one of the things that we see that is a confounding issue is a culture where almost anyone can say no and very few people can say yes to the changes that you need to connect a lot of those dots. So that's part of it, but that still goes back to leadership——

Mr. BLUM. Culture.

Mr. Korb.

Mr. KORB. I think it requires a strong deputy. The Secretary, he or she is very busy running around the world and doing things. But you need someone like a David Packard; or Charles Duncan, who came in from Coca-Cola; Don Atwood, who came in from General Motors. When I have looked at this, that's when the Department has been run well because they are the chief management, and they also have the gravitas to make things happen that you suggest.

Mr. BLUM. Thank you, gentlemen.

And thank you for your indulgence, Mr. Chairman. I yield back.

Mr. PALMER. The gentleman yields.

The chair recognizes the gentlelady from the District of Columbia, Ms. Holmes Norton, for 5 minutes.

Ms. NORTON. My thanks to the chair.

We've looked at the Trump budget, which purports to achieve huge savings that it says can be done by looking at inefficiency and waste. Now the largest budget in the domestic budget is, of course, the defense budget. So let's begin, as I think anybody would, by looking at the largest first. I might ask this to any of you, to all of you; let me begin with Mr. Korb: If you were making a serious effort to target inefficiency and waste in the Federal Government, could you possibly exclude the Defense Department budget?

Mr. KORB. Absolutely not, and I made that point: If you give them money, they will have no incentive—if you give them more money—to make the reductions that they should.

Ms. NORTON. Do any of you believe that you would exclude the Defense Department, set it aside, if you were looking at your entire domestic budget and not look at the Defense Department? Do any of you believe that that's how you would proceed?

Hearing none, as they say.

Well, if we look at the budget of the administration, far from looking for inefficiency and waste there, what we see is an unheard of increase, a $50 billion increase, in that budget, taken of course out of the flesh of the rest of the domestic budget.

So let's look at the State Department budget, for starters. You look at the State Department and the Agency for International Development; it's a 28-percent cut. Some might say: You cut that much, you starve the agency to death. Mr. Korb, you believe there would be any agency left standing if you took 20 percent out of a combination of USAID and the State Department?

Mr. KORB. I think if you do that, you will jeopardize national security. And as has been already pointed out by your colleagues, most military people have objected to that, including the current Secretary of Defense.

Ms. NORTON. Do you think you would get a more efficient State Department, for example, and USAID by cutting them 28 percent?

Mr. KORB. I don't think so. For example, you have more people in military bands than you do in the Foreign Service. So the idea that somehow or another you can cut back really just doesn't make a great deal of sense.

Ms. NORTON. So I ask you to look at this combination because I was interested in how all this adds up. You take—the USAID and the State Department has a 28-percent cut. Then you look at the rest of the domestic budget. Look at the EPA; that's a 31-percent cut. Or the Labor Department, that's a 21-percent cut. Perhaps it's a coincidence, but you get a total there of $58 billion, which is about the same as the increase proposed in the Defense Department budget. So let's assume you could get such a huge amount pouring into one budget so quickly. Is that the way—could you get that amount used efficiently so as to justify lobbing in such a huge amount at one time on one agency?

Mr. Korb.

Mr. KORB. I don't think so. Particularly, as I mentioned earlier, the new administration is adding $30 billion to their 2017 budget. So they are going to put that in, and the fiscal year ends 1 October. So we're already a good way through it. And then adds another $54; I think we'll find it very tough to do it in an efficient—efficient way. That's why I commend the Business Board here because they talked about the savings over 5 years, not having them all right in the first year.

Ms. NORTON. Mr. Tillotson, this is an increase over 1 year. Can you cite me any precedent where such a huge amount got spent efficiently over a single year?

Mr. TILLOTSON. I can't cite a precedent, but I can cite the concern of the Secretary of Defense that we not ask for something that is not executable. And I can also cite the fact that the Secretary of Defense is internally on record with the tasking to the Department through the DepSecDef to look for additional efficiencies. And I can also state that the White House and the Office of Management and Budget is still holding the Defense Department accountable for offsetting part of the proposed increase in spending by continuing to find efficiencies within the Department. I don't think anybody is letting the Department off the hook in this conversation. And I will defer the rest of the prioritization of the budget to the White House. That is their decision, and I'm not privy to that conversation.

Ms. NORTON. Of course. And the way to do credible savings is to do across-the-board savings. Then maybe somebody will believe your budget.

Thank you, Mr. Chair.

Mr. PALMER. I thank the gentlelady.

I will now recognize myself for questions. Mr. Tillotson, The Washington Post article, investigative report actually, said that the Pentagon knew their back-office bureaucracy was overstaffed and overfunded. If you knew that, why didn't do you anything about it?

Mr. TILLOTSON. So, respectfully, we have been doing something about it. Since Secretary Gates, we have been continuing to draw down the headquarters' staffs at the Department of Defense. That was an initiative from Secretary Gates years ahead even of the DBB study. We continue on that trend, and we're meeting those goals. We have reviewed the defense agencies. I would take a bit of issue with the so-called back shop that we talk about in some cases because we talk about the defensewide account, includes the

Defense Logistics Agency, which does central purchasing and procurement——

Mr. PALMER. Sir, I want to continue on with some other stuff. And I appreciate the detail, but we have only got a few minutes. Or we can take as long as we need to, I guess. But you said you did something about it. I would assume that the fact that Chairman Bayer, Mr. Stein, Mr. Klepper, Mr. Rutherford are here, is that that was part of the actionable effort, this study. Would that be correct, Mr. Rutherford?

Mr. RUTHERFORD. Our study finished almost 2 years ago, and in that study, we laid out a path forward with the DCMO on how to measure this on a go-forward basis with line of sight into what is due the savings.

Mr. PALMER. Now how much of that has been implemented?

Mr. RUTHERFORD. You'd have to ask Mr. Tillotson.

Mr. PALMER. Mr. Tillotson, how much of that has been implemented? Can you give me a percentage amount?

Mr. TILLOTSON. Yes, sir. I will go and say that $7.9 billion worth of efficiencies have been laid in, which includes——

Mr. PALMER. Less than 8 percent.

Mr. TILLOTSON. Less than 8 percent. But as acknowledged in the DBB study itself, we needed to start; we needed to put some pieces in place; and then we needed to continue and sustain the effort. And that's our intent

Mr. PALMER. How much of your recommendations, Mr. Rutherford, do you think could be implemented?

Mr. RUTHERFORD. We think all the recommendations——

Mr. PALMER. That's a great answer. Thank you very much. Do you think that they could have quickly implemented 20 percent?

Mr. RUTHERFORD. The speed is the biggest issue. So what we have laid out with the DCMO is that the speed in which you would do this would actually have to be quite deliberate of year-over-year productivity, which is around, from our estimations, a 3-percent productivity gain every year, which would only be about 4- to $5 billion every year. To get something so quickly upfront would take something much more robust than we laid out.

Mr. PALMER. I want to ask you something else about—and I will stick with you, Mr. Rutherford. The investigative article also made this: the average administrative job at the Pentagon was costing taxpayers more than $200,000, including salary and benefits. Was that salary and benefits, or are there other costs in there? I mean, I find that shocking that that was the average cost.

Mr. RUTHERFORD. My understanding of the salary and benefits, but I should go back and get that for you.

Mr. PALMER. I would like for you to provide some answers to some questions to the committee because I'm not sure you'll be able to answer them right now. But I'd like to know how many people overall were in those administrative positions? How many were civilian versus military? And if you know the answer, I'd love to hear it. And I'd like to know how many of those earned over $200,000 because, if the average is $200,000, including salary and benefits, frankly, that's shocking to me. And how many are over $250,000? We're seeing this throughout the Federal Government. This is something I'd like to know. Could you provide those answers? How many total people are working administrative jobs, and how many are civilian versus military? How many of those earn over $200,000, and how many of those earn over $250,000?

Mr. RUTHERFORD. Since our work ended 2 years ago, I can go back and look at those numbers and pull together what our view was at that time.

Mr. PALMER. Mr. Tillotson, I would request the same information from you. You should be able to provide.

Mr. TILLOTSON. I was going to say, I think respectfully, Mr. Chairman, I'm the accountable agent for answering your question. And I understand the question. We'll be happy to take it on.

Mr. PALMER. Do you think we could get that next week?

Mr. TILLOTSON. I see no reason why not.

Mr. PALMER. Thank you. I've only got a few seconds here. Here's the thing that bothers me about this. You realize that the appearance—even the appearance of a coverup of a report like this undermines the Pentagon's credibility. It undermines your credibility, frankly. You hurt personnel that work at the Pentagon who show up for work every day and do their job. You hurt the taxpayers. You add to their burdens. You hurt the finances of the United States government. Every dollar that's wasted is another dollar, because we're doing deficit spending, that we're having to pay interest on. You know, the total amount of waste is more than 125 billion when you take that into account.

Finally, by wasting the resources committed to our national defense, I think you compromise the military's ability to carry out its mission. That's what is so troubling here. You look at the total financial picture of the United States Government and the path that we're on. I mean, we're at $20 trillion in debt. If we're having to pay interest on that entire debt, a 1-percent increase in interest on that, Mr. Stein, is $200 billion. So you begin to understand why everybody on this committee is so sensitive to this because you're adding to the burden of the American taxpayer.

I think it was the Joint Chiefs of Staff Chairman, Admiral Mullen, that said that the single greatest threat to our national security is our debt. So I appreciate the seriousness with which this hearing has been accorded by each one of you, and I appreciate it very much. But we have got to get a handle on this, not just at the Pentagon, but throughout the Federal Government, but particularly at the Pentagon because that's—constitutionally that's our first obligation, is our national security.

With that, I'll yield back and recognize—sorry. The chair recognizes Mr. DeSaulnier from California for 5 minutes.

Mr. DESAULNIER. Thank you, Mr. Chairman. I want to thank the chair and the ranking member for this hearing.

I'm reminded of many conversations I used to have with my father-in-law, who was a highly decorated Air Force general in World War II, who ended his career, near the end of his career, he was the auditor general of the Air Force, major general. He won a Distinguished Flying Cross, but he also won something, if memory serves me, called a Zuckert Award, which at its time was the highest achievement for management. He used to say that was harder to get than the Distinguished Flying Cross flying over Germany. But he also told me that too many people in the Department of Defense were more interested in keeping their jobs than doing their jobs well.

So, Mr. Korb, you mentioned the Packard Initiative. I often think back to Peter Grace and the Grace Commission. Why were those effective in having business people being able to make observations? This is not new: having business people come in and look at the public sector, acknowledge that they're different, and be able to get both Congress and the bureaucracy to change their culture and implement those. The frustrating thing, as you have said, is it doesn't seem sustainable. Although I do want to congratulate the Department of Defense in this instance for bringing Republicans and Democrats together in common cause. Mr. Korb?

Mr. KORB. I think it's because of the fact that they've managed large organizations, and they understand how to make them work; plus they have the gravitas to be able to stand up to generals, admirals, and other people. And I think that's the key thing. When I worked in government, we had—things got pretty bad, and it was mentioned earlier about the toilet seats and all of that. We had to bring David Packard back to help straighten things out. I think if you take, as I've looked at this all the time, when you have a deputy like that, and many times the Presidents will pick the deputy even before the Secretary. Before Dick Cheney took the job, Brent Scowcroft had picked up Don Atwood from General Motors. So I think that's the key because you have a lot of people, military people, like your father-in-law, done all these distinguished things. So you're going to need a big presence to be able to tell them, you know, what to do. And I think that's how it's worked best.

I mean, after all, David Packard, and everybody knew Hewlett Packard, and back in the seventies, because of how important that company was, when he said stuff, he made it happen. Just to give you an example, the services didn't want to have a single transportation command, okay. He was able to get that done.

Mr. DESAULNIER. So here's the struggle, and, Mr. Klepper, to you—and you've gone from different industries and been able to look at cultures, and as the McKinsey report says very clearly, that culture is a big thing, the willingness to accept criticism, to acknowledge that you need to accept that criticism in a manner that would be corrective, but it seems to be uniquely difficult in this environment. One quote from the McKinsey report, as acknowledged through The Washington Post investigation, said McKinsey noted that, while the Defense Department was, in quotes, "the world's largest corporate enterprise," end quotes, it had never, in quotes, "rigorously measured the cost effectiveness, speed and agility, or quality of its business corporation." It seems rather striking that that hasn't happened.

So, both on that comment and then on a comment you made in the same article where you're quoted as saying, "You're about to turn on the light in a very dark room"—and I won't read the rest of the quote. It's quite colorful. But it strikes me that that's really the essence of it, and there have been different periods of time where your kind of effort has worked in the Department of Defense or in large public agencies. But this keeps coming up, that the culture is the most resistant to changing. And oftentimes, as my father-in-law said, the rewards and promotion within that culture is more about just getting by than actually performing well.

Mr. KLEPPER. Well, I haven't been in a number of organizations where the task was a major disruption, a major change from the status quo and some of the business direction. A couple of things—look, this isn't a study; this is sort of what Kenny's learned, you know, along the way—is I talked about leadership as sort of the irreplaceable. Without that, you're sort of lost. But the other two things that I think are vitally important, and I do think they apply here, and we have heard different versions of it, is transparency and accountability, whether it's the audit system that we talked about, because you can't have an accountable organization without a transparent organization. I understand there's a lot of classified stuff, but the things that we're working on here, this is not classified stuff, and I do believe that sunshine is a good disinfectant.

One of the greatest things that we could do is to make the kind of inefficiency information more available to third parties and have ideas and have innovations to do that. But even then, if you don't deal with the tribal, cultural, who gets promoted in and for what—that's the recognized, reinforced, and rewarded—you got to go really, really hard on that. And at some place, efficiency and productivity have to become a more dominant marquee in that story. And I think if you start there from the top, and if we can successfully begin to bring transparency, we'll attract good practices, and there's an unbelievable amount of talent.

And the other thing I think where the article misrepresented somewhat the Pentagon, almost all the senior military people that we talked to were extremely supportive. I outbriefed General Odierno, and he was going up to testify during sequestration, and there was a whole roomful of people. It was like you're going in the coliseum. Is Kenny and Bobby going to get their head chopped off, or this is not—and we outbriefed to General Odierno. And he looked at us, and he said: "You know, I think you guys did a good job on this study, and I think the savings is there." And he paused and he said: "Your timing is not perfect." But he tasked people to move ahead, and then we weren't able to follow through.

So the talent is there. Transparency and leadership I think are the starting place, and I think it is something that we can do. This is an achievable goal, and there's lots of reward for us if we do it.

Mr. DESAULNIER. Thank you. Thank you, Mr. Chairman.

Mr. DUNCAN. [presiding.] Thank you. I'll recognize myself now. Let me just say a couple things.

First of all, the easiest thing in the world to do is to spend other people's money. Secondly, you can never satisfy any government agency's appetite for money or land. They always want more. And I have wondered for many years whether there are any fiscal conservatives at the Pentagon. I'll tell you a little story. I've been here a long time. This is my 29th year. When I first came here, I believed everything the Defense Department said. And I voted for the first Gulf war because I went to all the briefings and heard how great a threat Saddam Hussein was. And then I watched that war, and I saw his same so-called elite troops surrendering to CNN camera crews and empty tanks. So, by the time the second war rolled around, I had a lot more questions. And I got called to a meeting in a little room at the White House with Condoleezza Rice and George Tenet and John McLaughlin, the top two people at the CIA, and I asked them that day many questions. But I asked them: Lawrence Lindsey, the President's main economics adviser, had been on the front page of The Washington Post saying a war with Iraq would cost us $200 billion. I asked about that, and Condoleezza Rice said, oh, no, it wouldn't cost nearly that much; it would be 50- or 60 billion, and we would get some of that back from our allies. Now we're up in the trillions. That must have been the worst estimate in the history of the Federal Government.

And I can tell you that when I was one of the six Republicans who voted against going to war in Iraq, it was the most unpopular vote that I ever cast in my district because I'd seen a poll the night before saying 74 percent of the people in my district favored the war, and 9 percent were against, and the rest undecided. But slowly over the years, that most unpopular vote ended up becoming the most popular vote that I ever cast. As I sit here now, I hear all these people say that the Defense Department has been decimated or it's underfunded, and yet I look at the historical tables of the official budget, and it says that, in 2002, the defense budget was 348 billion. By 2010, it had gone to 693 billion. And it's just gone up every year. And this past year, in the budget, we spent 177.5 billion on new equipment. Well, we spend that much or close to it I guess just about every year. Well, that equipment doesn't wear out in 1 year's time. And the defense—the military construction budget is a separate budget. You can't go to any military base in this U.S. or in the world that there's not all kinds of new construction going on.

We somehow have got to bring this under control. We have got to get some more fiscal conservatives at the Pentagon, and I mean, I believe and I think most of us believe that national defense is the most important function or certainly one of the most important functions of our entire Federal Government, but it's getting kind of ridiculous when the Pentagon has done a masterful public relations job in convincing people all over this country that they're underfunded or been decimated, and I think it's almost gotten to the point that it's, in my opinion, it's pretty ridiculous. I am a very conservative Republican, but I think conservative Republicans should be the ones most horrified by the excessive overspending that's going on at the Pentagon.

And I commend the work that your board has done. I mentioned this 125 billion in the last newsletter a few months ago, a couple months ago, that I sent out to my constituents. We need more work that will go on like that.

And now I yield to Mr. Lynch for 5 minutes.

Mr. LYNCH. Thank you, Mr. Chairman.

And I associate myself with much of what you have just said. I don't think you need to be a conservative, but I do think your outlook needs to be fact-based, and I think that's where the differential comes in.

I just have one bone to pick, not necessarily with you, and I want to thank all the witnesses here. You've all been very, very helpful. I appreciate your report. I haven't gone through all of it yet, but I will.

President Trump came in, and one of the first things he did was to put a freeze on all Federal hiring. And, Mr. Tillotson, DOD is the biggest employer of returning veterans and veterans in this country. The Federal Government is collectively the largest employer of our veterans coming back from Iraq and Afghanistan and those who have served this country. First of all, the economics, we have had two other hiring freezes—one under Reagan, one under Jimmy Carter—and both of them, according to the GAO, increased spending in the Federal Government because we went to contracting, private contracting, and it boosted up the cost. And I think that's going to continue here. I don't think we're going to save any money.

The other thing is, because we are such, in the Federal Government, such a large employer of veterans, what this hiring—so 30 percent of our Federal employees are veterans, about 30 percent. So what this does now is it puts a freeze in. So, as these kids are coming back from Iraq and Afghanistan, the Federal Government, which normally would hire them, is saying no. And so we're already dealing with an elevated suicide rate. We have got substance abuse problems. We have got big, big problems with transition coming back in because of the multiple deployments that these kids have done. I was over at Camp Leatherneck there in Afghanistan, and I asked some of those kids how many tours. I got all the way up to seven tours. One of those young men was on his seventh tour. So that's got to cause some psychological problems. In the meantime, when they come home, we're telling them we can't hire them. And also it's costing us more money. So that's just a statement I got that is in opposition clearly to what the President is doing.

Now my background—here's where the question comes in—my background is in construction, steel erection. I used to build bridges. I was an ironworker for about 20 years. My degree is in construction management. So this stuff with DOD is infuriating to me. It really is. And from my own experience, transparency, Mr. Klepper, right on the money; that's what it's all about. In my business, my prior business, transparency and competitiveness in bidding, that whole process was really what gave the end user, the taxpayer, the biggest bang for their buck. When there was no workaround, our contractors would come in and sharpen their pencils, and, boy, that dollar would go a long, long way. And when there was a lot of work and people could just throw a number at you, things were much more expensive.

This process that we have with DOD, and we have got 36 major defense laboratories all around the country, including my own, where I can't figure out how to get a person who wants to bid on some of that work into the process. It's all smoke and mirrors. You need a secret handshake or something. I can't get people on the job who want to offer a lower price for those services. You know, it looks like to me—I have to say this—that a lot of retired generals have gone to work for these contractors and are in the system now, and it's like this good old boy network where the smaller companies can't get in there and offer lower prices. It's a problem. There are exceptions. I know Raytheon brings in all these subs, and they try to help with competition, and they'll educate the smaller subs so they can use them. They use the sub to the sub to the sub.

But is that at the heart of this problem? That's the question I have. Is that the heart of this problem? To make this—and I do agree with you, Mr. Klepper, some of this stuff is confidential; some of it is classified. But a lot of it is not, and we should throw it out there and make people bid openly, publicly, and competitively to make our government run more efficiently and at a lower cost to the taxpayer.

Mr. Klepper.

Mr. KLEPPER. Sir, the answer is yes. I think that's a significant part. If you look at contracting, I was just thinking as you were talking: You know the way that you get in is you find a sub of a sub of a sub, and you get on somewhere, which means you've got to know somebody that knows somebody generally to find them. Then there's a big, you know, by the time the government pays the tab, there's a lot of additional cost on it.

The other thing there's a practice here that's been around for a long time that drives all the worst possible behavior for spending. And it's a process—I don't know what the official. Maybe David could help—it's use-it-or-lose-it. If you don't spend all your money, then you get your budget cut. And one of the things we saw in the study, at the end of the year, there's a tsunami of contracts that completely overwhelm the contracting unit. There were anecdotal conversations with the McKinsey team where a single contract officer had to sign 60 contracts in one day because, if they don't get them signed, whoever the authoring contract, it's going to be heck to pay because now you've got my budget cut. So you have that practice, and that's a practice I just have to believe—I'm not smart enough to know how you guys could fix it. There has to be a way to fix it because that's driving an insane waste of money, use-it-or-lose-it. And I think the contracting structures are where there are some quick hits.

And I would add, lastly, the key to getting the numbers at the level that we are talking about is we need a large mobilization. To go at this study should take a mobilization of 4- or 500 people that we're putting in teams, and we're training them or deploying them, and they got targets and goals. Until we scale up how we even think about attacking this problem, we'll continue to just get dribs and drabs of savings.

Mr. DUNCAN. They tell me we have got to speed this up because we have got votes coming up, but I will tell you I have a bill in that gives an incentive award that lets the Department keep half the money that they save, and half goes back to the budget.

Mr. LYNCH. Mr. Chairman, if I could, I also have a bill that would allow veterans to be exempt from this hiring freeze so, at least when our kids come home from Iraq and Afghanistan, the government can hire them if they're qualified for those jobs, and the jobs are available.

Mr. DUNCAN. All right. Thank you very much.

Mr. Grothman.

Mr. GROTHMAN. Thank you. I have a question for either Mr. Stein or Mr. Klepper. What steps have the DBB team taken to ensure that benchmarks are applicable to the Department?

Mr. KLEPPER. I really can't answer that. We intentionally in our study try to avoid benchmarking because we were looking at such a high level. In benchmarking, you end up spending all your time arguing about apples-and-oranges comparisons. So benchmarking, I think, has an appropriate—I don't know, David, if you can answer that, but I can't speak for the Department there.

Mr. TILLOTSON. Mr. Congressman, one of the deliverables that we asked for from McKinsey was, in fact, benchmarking in some of these business areas compared to commercial sector. And it's what points us to some of the first areas to look at. So, specifically, financial, IT, and human resource management were identified as areas where the departments spend on certain activities, which has a good commercial analog, which is the first question we asked, which suggests we could find additional savings. So we are, in fact, using it.

Mr. GROTHMAN. How would you characterize your overall level of confidence in the cost and savings presented in the report? And I guess that's really more for Mr. Stein.

Mr. STEIN. Ask the question one more time.

Mr. GROTHMAN. Okay. How would you characterize your overall level of confidence in the cost and savings presented in the report?

Mr. STEIN. Until you have a full process of mobilization and a commitment to this process, one of the things that was talked about—I think this study by McKinsey was done 2 years ago—and I think you are going to have to update those numbers to see what actuals are, and I think you have a full commitment from the Secretary of Defense that this is what's going to happen.

Mr. GROTHMAN. Okay. There were a number of individuals interviewed as part of the report. Were those same individuals providing the preliminary findings from the report, and if so, what feedback did they provide on the data sources used as well as the magnitude of the savings identified?

Mr. KLEPPER. The primary feedback—and I could yield to Mr. Rutherford from McKinsey because I wasn't personally present during the actual data pool. But we knew that when we build the base case—I've done this type of work and know that the data always gets attacked. For anybody, if it makes something look bad, the first thing you do is say the data is not good, and that's often where you get stopped at. So we took extraordinary effort in the data pool to be sure that, when the data was pulled from the system and it was arrayed against the core processes, that there was a local signoff within the agency or the military department that said that the way that the data was stacked was reasonable, because we also wanted to be able to do, to rerun the models on an annual basis so you can track financial performance over time. So those are the two things that we put a lot of rigor in that. And when we got into the data pool, we found some of the same issues that may affect the audit systems, financial systems, et cetera.

But I have to say the McKinsey team, working with Dave Tillotson and the people he provided us—and there were over 100 people involved in this data pool; it is the biggest one that, I believe, has ever happened at DOD—that the foundational data is pretty solid. And we also offered a challenge process that, if somebody saw the data and said, "Hey, this is wildly wrong, your analysis is bad," that we could actually come in, audit the numbers, and if we found an error—look, if it was wrong, we want to know that the model is wrong—we could correct it. So the model came through, and today I don't think we have had any substantial challenges, at least that I've heard, that the base case model is wrong. The real debate, and maybe to your earlier question, is there's two parts of it: Is the savings there, the potential? And I would say it is absolutely there, and it's probably conservative. The big question is, can all of us together resolve, move the barriers, and get the implementation of the leadership? How much of it can we get and how fast? And I think that's sort of the wild card answer. And I believe we have a shot at the numbers that we published. I really do. But we certainly would need help from you and others like you to get some of the barriers out of the way.

Mr. GROTHMAN. I guess I have time for one more question. Mr. Tillotson, what level of independence was given to the McKinsey team?

Mr. TILLOTSON. The McKinsey team was basically on their own. Other than the assistance it took to get them into the databases, their analysis then was their own. And the DBB analysis, which was also done, was also independent. We did not influence either outcome.

Mr. GROTHMAN. Okay. Thank you.

Mr. DUNCAN. Thank you.

Ms. Kelly.

Ms. KELLY. Thank you, Mr. Chair, and thank you for holding the hearing today.

The topic of waste within the Defense Department is extremely important, and it deserves our attention, especially considering President Trump's budget proposes funding a $52 billion increase in the Defense Department by cutting other parts of the Federal budget. While I definitely agree that we should support the Nation's warfighters with everything they need, I am concerned that this budget proposal would hurt our national security in other ways.

Dr. Korb, our national security depends on more than just a properly resourced Defense Department, does it not?

Mr. KORB. Yes, it certainly does. As we have talked about here, several other agencies that are being cut to pay for this are actually going to undermine national security.

Ms. KELLY. Thank you. And we have talked about, I know, the State Department and the contributions it makes on national security.

I would like to ask about another cut. Under the President's proposal, Federal funding for the National Institutes of Health would fall by 5.8 billion, roughly a 20-percent cut. As chair of the Congressional Black Caucus Health Braintrust, this is very concerning to me. The President's proposed cuts would halt cancer research and other invaluable medical research among the more than 2,600 institutions that receive NIH funding. The cuts would also affect research of infectious diseases, which respects no national boundaries. According to The New York Times, over the last 50 years, 700,000 Americans have died from AIDS; 1.2 million died from the flu; and 2,000 died from the West Nile virus; and 1 died from Ebola.

During a television appearance on March 17, Republican Congressman Tom Cole stated: “I don't favor cutting NIH or Centers for Disease Control. You're much more likely to die in a pandemic than a terrorist attack, and so that's part of the defense of the country as well.” Congressman Cole called the President's proposed cuts very short-sighted. Do you agree that short-sighted cuts should be avoided?

Mr. KORB. I certainly do, and I'd like to quote my favorite President, Eisenhower, who said you can't be strong abroad if you're not strong at home. And if you don't deal with these diseases, you're going to have a difficult time getting enough people to volunteer for the military who meet all of the requirements that you need.

Ms. KELLY. Thank you. Anybody else care to comment?

No? Okay.

Mr. Chairman, while I fully support providing necessary resources again to our Nation's warfighters, we need to carefully consider whether we hurt our national security on other important fronts like global health.

And I yield back the balance of my time.

Mr. DUNCAN. Thank you.

Mr. Sarbanes.

Mr. SARBANES. Thank you, Mr. Chairman.

I thank the panel.

I want to commend you for the incredible amount of work that you've all put into this. You've bled for it. I commend you for not just sitting there and engaging in a primal scream for the last 2 or 3 hours. A couple things, and I know my colleagues have been reading from some of these quotes, but we have talked about how the President's budget is going to impose draconian cuts on a lot of domestic programs, things that we have all acknowledged are important, as well as foreign aid and so forth. NIH, I know my colleagues have spoken to those cuts.

This quote from OMB Director Mick Mulvaney, though, is just priceless, where he, in regards to the NIH cuts, said: “These were made because of the tremendous opportunity for savings at NIH and”—I'm sure someone else has read this quote, but I just want to repeat it—quote, “the President's businessperson view of government is focusing on efficiencies and focusing on doing what we do better.” I have to assume you all, when you saw that quote, just grabbed this report—we'll call it a report—and just ran as fast as you could up to the White House and handed it to President Trump because it's all about a businessperson's view of government and focusing on efficiencies and on doing what we do better.

Let's talk about the culture because that's the name of the game here: breaking the culture. And I've heard you speak, Mr. Klepper and Mr. Korb and Mr. Stein, about leadership being important, transparency and accountability being important. How high do you have to go to get the person who can actually make the change in the culture? Is it enough to go to an Assistant Secretary of Defense? You got to get at least to the Secretary of Defense to embrace the change in culture, or do you actually have to get to the President, who gets up every day and says, “The Pentagon has got lot of waste and inefficiency in it, and one of the priorities today and tomorrow and the next day is going to be for us to attack that and make it work more effectively"? How high do you have to go to find the person who you think can break the culture in a meaningful way?

You can just start with Mr. Korb there.

Mr. KORB. Well, I think it's really got to be your Deputy Secretary of Defense. The Secretary whoever he, and hopefully some day soon she, is basically is going to be traveling around the world and doing a lot of things. The deputy is the one who has to do it. And as I mentioned here, people like David Packard, Charlie Duncan from Coca-Cola, Don Atwood from General Motors, they've been able to do these things. And I think that's really where it has——

Mr. SARBANES. So, in terms of deploying the culture change, you need that level. But you would certainly agree, I guess, that if you don't have acquiescence in it or the buy-in or the approval of it from the levels above, all the way up to the President, then that person can't be effective presumably?

Mr. KORB. Well, that's true. If you take President Trump at his word, you would think this is what he wants to do, and if the Secretary, whoever he or she may be, should certainly buy into that and then get a strong deputy to make sure that it happens.

Mr. SARBANES. Other thoughts?

Mr. KLEPPER. You know, it's the sponsor model for change, and it starts with the President. He is mega sponsor ultimately because, even though the size of the Department of Defense from an efficiency standpoint has a bigger potential, it's an issue across all of government. It's an issue in all of industry. So this is—organization—high-performance organization needs to be reinforced all the way from the top.

Now, that's delegated, and I would say we had a case in the Department of Defense where the Deputy Secretary was all in. It was a change of leadership at the top, and we kind of went dark. So, in that situation, it really starts within the Department of Defense with the Secretary of Defense because if he's reinforcing and holding accountable to some tangible metric, organizational efficiency, the odds are that those direct reports are going to hold their staff accountable, and that's that cascading chain to where, at any point, somebody decides they're not interested in this and they're going to get evaluated differently, that's the black hole where change goes to die. So that's a really essential key——

Mr. SARBANES. I'm going to run out of time. So I just want to emphasize what you said. Culture change can't happen if it doesn't start at the top, all the way at the top. And this is the Federal Government. The person who's all the way at the top is the President of the United States. So leadership matters from there, but transparency and accountability, if those are going to be standards that can accomplish the kind of change you want to see and that you worked so hard to produce, to tee up for us, then that commitment to transparency and accountability has to begin at the very, very top.

And this committee has had the opportunity just in the last few weeks to demonstrate that we're not seeing that kind of accountability and transparency coming from the very top of this organization, which is the Federal Government and, in this case, the executive branch of the Federal Government. I hope we see more of it.

Mr. DUNCAN. I'm sorry. We have got to go to Mrs. Maloney. I apologize.

Mrs. MALONEY. Thank you. Thank you very much, and I thank you, Mr. Chairman.

And I thank all of you for your service. It's really, personally, I think it's a scandal. It's an incredible scandal. Of the 34 areas the GAO highlighted this year, seven for mismanagement or high risk, seven were in the Defense Department. And basically what your report showed, that if you had implemented the findings of this report that you all worked so hard on, you would have resulted in 125 billion in savings so that the losses that my colleagues are talking about for essential services for people wouldn't happen.

I think that this is an absolutely scandal, and it seems to me like if you can't, in reading some of the history of this, it's the Defense Department itself that stops the investigations, that stops the reforms, that says the data should be kept secret. It struck me, Mr. Rutherford, that you said you couldn't even get your hands on it, and especially what you said, you didn't know where it was. Do you have any sense of how much of the bureaucracy, of the many levels that they go through, is in the budget? Is it half of it? Is it a quarter of it? Is it a tenth of it? How much of it is in this permanent bureaucracy that has been created of the Defense Department spending, would you say?

Mr. RUTHERFORD. So what we looked at in our work was looking at the six core business functions, and within those business functions, we had to pull from 20 different data sets to pool all the information to actually give the transparency that Mr. Klepper is talking about so then Mr. Tillotson can move out against that to see what they can make adjustments against. As far as the percent of that that is bureaucracy, that's where we started to cut down; where can they actually find the savings? And that's when we came away with our 62- to $84 billion number over a 5-year period because it adjusted for a little bit more of a deeper dive into some of these sub-functions.

Mrs. MALONEY. That is amazing. Just to respond, I think if the culture can't seem to change, I think Congress should step in and help them change it, Mr. Chairman. Why don't we pass a bill that the data has to be transparent so that people can see it, so that people can report on it? If they're hiding their data, number one—number two, on their contract system that the sub of the sub of the sub of the sub gets to a small business, why don't we have competitive bidding to the best qualified? Forget—I read someplace you have like 155 contractors. For what? You write up the specs, you throw it out, and you see what comes in, instead of going through all these processes that end up giving it to the ex-general. So I would like to see competitive bidding for all of these processes and all of this new equipment. Why do you need all of this new equipment? I think you ought to bring in McKinsey and have them do a service to their Nation and run the State Department—I mean the Defense Department.

One thing struck me, that the contracting out of the Defense Department is more than about 10 agencies combined. I mean, it's huge. I want to ask, Mr. Rutherford, you had slightly different numbers than what the Defense Business Board came out with on what the final numbers were. Is that true?

Mr. RUTHERFORD. Yes, ma'am.

Mrs. MALONEY. Why was that, do you think?

Mr. RUTHERFORD. So they finished the report in January of 2015. We spent then 3, 4 months longer with the DCMO going deeper into the sub-functions, so we had the luxury of actually looking at some of the lower level data. We actually then brought in different types of benchmarks that we used in how you can actually achieve productivity gains, and that came up with a number that both in terms of the amount of spend came down, but it had more to do with the timing on how much you can achieve over a 5-year period.

Mrs. MALONEY. And your contract spend optimization, do you think that that would have potential savings, and how, much and what is contract spend optimization? What is that?

Mr. RUTHERFORD. The contract spend optimization is when you look at the contracts every year they come up. Are you actually, for rebidding purposes or renegotiation purposes, actually looking at, one, what does the Department of Defense really need from a requirements standpoint, and then, two, from a bottom-up standpoint, what should it cost the Department of Defense with more of a bottom-up view? And then you get a sense of where your negotiation power is to actually do optimization of those contracts over time. So, every year, you're getting better and better at the contracting process.

Mrs. MALONEY. Well, see, what I don't understand—we have the greatest military in the world, but they can't seem to manage anything. We're the best and the strongest. And how much savings did you attribute to aggregating and renegotiating contracts?

Mr. RUTHERFORD. I'd have to go back and look at the numbers, but what we looked for there on the contract spend—that was going to be from a year-over-year savings—we were looking at 4- to $5 billion every year for our 62 billion. Of that, it was going to be about 20 percent to 25 percent of that number would be in the contract optimization.

Mrs. MALONEY. These are huge savings. I have one report that they gave me, but it's from the business group. Could I see the original report that McKinsey did?

Mr. RUTHERFORD. I believe all of our deliverables that we gave to the DCMO were provided, but I can go back and check to make sure that that happened.

Mrs. MALONEY. But I mean, you know, I didn't—could I see your report? This is the report that we have. Was that yours?

Mr. RUTHERFORD. So there's the DBB report that they did, which was published on January 15. Our contract went beyond that, and our contract had a number of deliverables that were inputs into that report. But what we provided for the DCMO was a set of contract deliverables that looked not only at what the baseline was, but what metrics did they use for productivity gains, and then what was the estimated savings in each of those categories?

Mr. DUNCAN. I'm sorry. We have got votes going on on the floor now. So I want to thank all the witnesses for taking the time to appear before us today. You've been very patient. You've been here a very long time.

I ask unanimous consent that members have 5 legislative days to submit questions for the record.

Without objection, so ordered. If there is no further business, without objection, the committee stands adjourned.

[Whereupon, at 1:11 p.m., the committee was adjourned.]

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