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.

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.

***

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

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."

---

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."

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."

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

[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."

Committee on Oversight and Government Reform
Witness Disclosure Requirement — "Truth in Testimony"

Pursuant to House Rule XI, clause 2(g)(5) and Committee Rule 16(a), non-governmental witnesses are required to provide the Committee with the information requested below in advance of testifying before the Committee. You may attach additional sheets if you need more space.

Name:

1. Please list any entity you are testifying on behalf of and briefly describe your relationship with these entities.

Name of Entity	Your relationship with the entity
None	Mr. Klepper is testifying in his capacity as a former member of the Defense Business Board
	The contract below was awarded to ReactiveCore LLC where Mr. Klepper currently serves as the Chairman and CEO, and was not personally awarded to Mr. Klepper.

2. Please list any federal grants or contracts (including subgrants or subcontracts) you or the entity or entities listed above have received since January 1, 2015, that are related to the subject of the hearing.

Recipient of the grant or contact (you or entity above)	Grant or Contract Name	Agency	Program	Source	Amount
ReactiveCore LLC	HQ003417C0023	Department of Defense	8 (A)	Washington Headquarters Services	1,845,000

2. Please list any payments or contracts (including subcontracts) you or the entity or entities listed above have received since January 1, 2015 from a foreign government, that are related to the subject of the hearing.

Recipient of the grant or contact (you or entity above)	Grant or Contract Name	Agency	Program	Source	Amount

I certify that the information above and attached is true and correct to the best of my knowledge.

Signature: KOKlepper

Date: 3/16/2017

Page 1 of 1

Kenny Klepper

Chairman and CEO
ReactiveCore LLC

BIOGRAPHY

Kenneth O. Klepper has practiced the tradecraft of enterprise business transformation in both the energy and healthcare industries for over 40 years. He specializes in large-scale organizational change and is a dynamic and results-oriented leader with proven success in fostering a corporate culture and mindset of reliability and innovation.

As a highly accomplished Senior Executive, he has broad-based experience in change management, business transformation, team building, operations, finance, mergers & acquisitions, technology development and integration, and continuous improvement.

Most recently in his position as President and Chief Operating Officer of Medco, Mr. Klepper oversaw the sales and account market groups, and all business operations, including the world's largest and most advanced automated pharmacies and information technology group which have been recognized for setting new standards for pharmacy dispensing quality. During his tenure, Medco was recognized by Fortune magazine as the third most innovative company in America behind Apple and Nike, and was the only company most consumers have never heard of it. He was also responsible for Accredo Health Group, Inc., which was acquired by Medco in 2005 and has since become the nation's largest specialty pharmacy. Accredo serves the needs of patients with complex conditions requiring sophisticated treatment.

Prior to joining Medco, Mr. Klepper served in leadership positions at WellChoice, Inc. (formerly Empire BlueCross BlueShield), Cigna Healthcare and Phillips 66. WellChoice was the second largest tenant in Tower One of the World Trade Center September 11, 2001. With 2000 employees in the building at the time of the disaster and the loss of 11 lives. The Kennedy Business School developed the attached summary of WellChoices remarkable resiliency and recovery after the tragedy. He served as a member of the Defense Business Board and the United States Navy Corporate Executive Panel (CEP), and is currently a member of the Diplomat Rx and US Naval Institute Board of Directors. Mr. Klepper is married with two children and two grandchildren.

Mr. Klepper has lead several successful business turnarounds including:

- Spearheading changes to grow New York's largest health insurer, Empire Blue Cross/Blue Shield, from $50+ million loss to $2+ billion IPO.
- Overseeing Medco's $7 billion spin-off from Merck and Co. as well as its $2.2 billion acquisition of Accredo Health Group.
- Architected the strategic combination of Medco and Express Scripts where he brought Medco public in 2003 at a $3.6 billion market cap and then subsequently sold the company 8 years later to Express Scripts for $29 billion.

Mr. Klepper currently serves as the Chairman and CEO of ReactiveCore LLC, a software company located in New York City.