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COMPENSATION REFORM: HOW SHOULD THE FEDERAL GOVERNMENT PAY ITS EMPLOYEES?

HEARING

BEFORE THE

SUBCOMMITTEE ON CIVIL SERVICE
AND AGENCY ORGANIZATION

OF THE

COMMITTEE ON
GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

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CONTENTS

Page

Hearing held on April 1, 2003 1

Statement of:

Blair, Dan G., Deputy Director, Office of Personnel Management; and Hannah S. Sistare, executive director, National Commission on the Public Service 16

Kelley, Colleen M., national president, National Treasury Employees Union; Jacqueline Simon, public policy director, American Federation of Government Employees, AFL–CIO; Bill Bransford, counsel, Senior Executives Association; and Karen Heiser, Federal Managers Association 105

Mihm, Christopher J., Director, Strategic Issues, U.S. General Accounting Office; Max Stier, president and CEO, Partnership for Public Service; and George Nesterczuk, president, Nesterczuk and Associates and consultant, Heritage Foundation 50

Ruppersberger, Hon. C.A. Dutch, a Representative in Congress from the State of Maryland 6

Letters, statements, etc., submitted for the record by:

Blair, Dan G., Deputy Director, Office of Personnel Management:

Information concerning group incentive program 46

Prepared statement of 19

Davis, Hon. Jo Ann, a Representative in Congress from the State of Virginia, prepared statement of 3

Heiser, Karen, Federal Managers Association, prepared statement of 175

Kelley, Colleen M., national president, National Treasury Employees Union, prepared statement of 108

Mihm, Christopher J., Director, Strategic Issues, U.S. General Accounting Office, prepared statement of 53

Nesterczuk, George, president, Nesterczuk and Associates and consultant, Heritage Foundation, prepared statement of 93

Ruppersberger, Hon. C.A. Dutch, a Representative in Congress from the State of Maryland, prepared statement of 10

Shaw, Jerry, general counsel, Senior Executives Association, prepared statement of 138

Simon, Jacqueline, public policy director, American Federation of Government Employees, AFL–CIO, prepared statement of 122

Sistare, Hannah S., executive director, National Commission on the Public Service, prepared statement of 28

Stier, Max, president and CEO, Partnership for Public Service, prepared statement of 72

COMPENSATION REFORM: HOW SHOULD THE FEDERAL GOVERNMENT PAY ITS EMPLOYEES?

TUESDAY, APRIL 1, 2003

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON CIVIL SERVICE AND AGENCY ORGANIZATION,
COMMITTEE ON GOVERNMENT REFORM,
Washington, DC.

The subcommittee met, pursuant to notice, at 1:08 p.m., in room 2247, Rayburn House Office Building, Hon. Jo Ann Davis (chairman of the subcommittee) presiding.

Present: Representatives Jo Ann Davis of Virginia, Murphy, Blackburn, Danny Davis of Illinois, Norton, and Van Hollen.

Staff present: Ronald L. Martinson, staff director; B. Chad Bungard, deputy staff director and senior counsel; John Landers, professional staff member; Heea Vazirani-Fales and Vaughn Murphy, legislative counsels; Robert White, director of communications; Christopher J. Barkley, clerk; Tania Shand, minority professional staff member; Jean Gosa, minority assistant clerk; and Cecelia Morton, minority office manager.

Mrs. DAVIS OF VIRGINIA. The subcommittee will come to order.

This is the first hearing of the Government Reform Subcommittee on Civil Service and Agency Organization in the 108th Congress, and the topic is both important and timely. The subject of compensation reform gets right at the heart of many of the challenges facing the Civil Service, from recruitment and retention to improving the efficiency and performance of the government itself.

Before I begin my own remarks, I would like to express my thanks to the witnesses who have agreed to join us today. We have brought together a broad and knowledgeable array of voices as we begin our exploration of this issue, and look forward to hearing all of your perspectives. I want you to know that I begin this hearing with an open mind. I see this session as a learning opportunity for the subcommittee.

Just over 2 months ago, the National Commission on Public Service, known as the Volcker Commission, issued its report on how to revitalize the Federal Government. At about the same time, the President issued his fiscal 2004 budget proposal. Both documents contain bold recommendations to reshape the Civil Service: The Volcker Commission, for example, suggests abolishing the General Schedule and allowing managers to base employees' salaries on "competence and performance." The White House's budget pro-

posal includes a $500 million Human Capital Performance fund to reward top performing employees, as well as a proposed shift of the entire Senior Executive Service to a pay-banding system.

More and more often, Federal agencies are seeking permission to develop a compensation system outside the General Schedule. More than 20 percent of non-postal civil servants now work under alternate personnel systems according to the Volcker report, including those developed at the Federal Aviation Administration, the Internal Revenue Service and the General Accounting Office. In all of those examples, change in the compensation system was designed not merely as an end to itself but as a way to improve agency performance.

The GAO is here today and I am looking forward to hearing how the various pay for performance systems are working so far, including GAO's own.

We are also fortunate in holding this hearing just 1 week after the Office of Personnel Management released its Federal Human Capital Survey. The results contain lots of good news. Ninety-one percent of employees believe they are doing important work and the overall percentages of Federal workers who are satisfied with their job is 68 percent or who believe the work they produce is high quality at 81 percent. It is consistent with findings in the private sector. Moreover, more than 60 percent of employees are satisfied with the basic pay and benefits.

Not all the news was good, however. Fewer than half of the employees are satisfied with the recognition they get for doing a good job. Just 30 percent said the rewards program gives them an incentive to do their best. Only 27 percent of employees believe that steps are taken to deal with poor performers. On the surface, it appears that those results point to a work force that is generally satisfied with their pay, their benefits and their jobs but would like to see a work culture that better rewards performance and does not reward substandard work.

I would like to hear the witnesses' perspective on this picture and what the Federal Government should be doing in the area of compensation reform. I thank you and I look forward to a lively and informative discussion.

[The prepared statement of Hon. Jo Ann Davis follows:]

From the Office of
Congresswoman
Jo Ann Davis

Opening Statement
April 1, 2003
Hearing of the Subcommittee on Civil Service and Agency Organization
"Compensation Reform: How Should the Federal Government Pay Its Employees?"

This is the first hearing of the Government Reform Subcommittee on Civil Service and Agency Organization in the 108th Congress, and the topic is both important and timely. The subject of compensation reform gets right at the heart of many of the challenges facing the civil service, from recruitment and retention to improving the efficiency and performance of the government itself.

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More and more often, federal agencies are seeking permission to develop a compensation system outside the General Schedule. More than 20 percent of non-postal civil servants now work under alternate personnel systems, according to the Volcker report, including those developed at the Federal Aviation Administration, the Internal Revenue Service and the General Accounting Office. In all of those examples, the change in compensation system was designed not merely as an end to itself, but as a way to improve agency performance. The GAO is here today, and we're looking forward to hearing how the various pay-for-performance systems are working so far, including GAO's own.

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Not all the news was good, however. Fewer than half of the employees are satisfied with the recognition they get for doing a good job, and just 30 percent said the awards program gives them an incentive to do their best. Only 27 percent of employees believe that steps are taken to deal with poor performers.

On the surface, it appears that those results point to a workforce that is generally satisfied with their pay, their benefits, and their jobs, but would like to see a work culture that better rewards performance and does not reward sub-standard work. I would like to hear the witnesses' perspectives on this picture and what the federal government should be doing in the area of compensation reform.

Thank you. I look forward to a lively, informative discussion.

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Mrs. DAVIS OF VIRGINIA. I would now like to recognize our ranking member, Mr. Danny Davis, and see if he has an opening statement.

Mr. DAVIS OF ILLINOIS. Thank you very much, Madam Chairwoman. I do indeed, and it is a pleasure, as it always is, to be here with you. I want to commend you for holding this hearing as we begin to explore in a very serious way some of the real issues and concerns with which we are going to be confronted, not only now but for years to come.

There is a steady drumbeat to reform of the current Federal pay system. This hearing provides a forum for the members of the subcommittee and other stakeholders to discuss the pros and cons of various pay reform proposals and the process for implementing such reform. The current pay system has been described as being designed for the heavily clerical and low-graded work force of the 1950's rather than today's knowledge-based government and that it should be redesigned to be more performance oriented, flexible and market sensitive.

Others have argued that the Civil Service Reform Act of 1978 and the Federal Employees Pay Comparability Act of 1990 were enacted to do just that. If the current system is not working, then the question becomes why not. If we do not understand why the current system is not working and address those concerns, how can we ensure that a new system will not be fraught with the same problems? Furthermore, if the current system is to be reformed to give managers more flexibility, how can we ensure that a new system will be fair and equitable and free from political influence?

Efforts to reform the Civil Service based on the need for more flexibility may indeed be valid, but often more flexibility without accountability is simply something we cannot afford to do. This subcommittee should not consider any reform legislation unless it addresses this very important issue of holding decisionmakers in the Government accountable for their actions and the decisions they make.

David Walker, the Comptroller General, has been a strong advocate for pay reform. Yet, in a letter dated March 26 to the Government Executive Committee, Mr. Walker wrote, "As with all pay-for-performance efforts, appropriate safeguards and accountability procedures would need to be in place to ensure fairness, prevent politicization and prevent abuse." The bottom line is that in order to receive any additional performance-based flexibility, agencies should have to demonstrate they have the modern, effective, credible and validated performance management systems in place that are capable of supporting such decisions. Unfortunately, most Federal agencies are a long way from meeting this task.

I agree with Mr. Walker and hope the witnesses before us today can address these concerns about accountability that he has raised.

I thank you, Madam Chairwoman, and yield the balance of my time.

Mrs. DAVIS OF VIRGINIA. Thank you, Mr. Davis.

Are there any other Members who would like to be recognized for an opening statement? Ms. Norton.

Ms. NORTON. Thank you, Madam Chair.

You have called a hearing on a most important subject. I would agree that we are at rather much of a watershed moment when it comes to Federal compensation but that is, in my judgment, because of structural changes in the way people approach Federal work today. They don't come to the Federal sector the way they used to and that is why your concern about hard to fill positions is well placed.

I was chair of the subcommittee when locality pay was first put in place. That was a reform that was decades in the making and seems to have disappeared from the radar screen and from the pocketbooks of Federal workers. I would hate to see us engage in compensation reform on a piecemeal basis or have to repeat the history of reform. I couldn't agree more that there is not a lot to make an engineer or a nurse or a pharmacist come to work for the Federal Government and remain with the Federal Government. I am equally concerned with the 2-percent increase for Federal employees if we want to keep hard to retain and attract employees, what are we going to do about the fact that those we already have are piling out of this place, many of them trained with investment from the Federal Government because very frankly, by retiring early or on time, they can market their skills for better pay and better health care than they get in the Federal Government. So it is very hard for me to look at the ones we can't get anyway without looking at those we have when you consider that half the work force could retire within the next 3 years. That is a true example of a crisis. It makes the crisis we face in hard to attract and retain employees look like a small crisis. That is a crisis writ large.

I hope in looking at compensation reform, we will bear in mind that we face a structural crisis with employees in the Federal Government and have our work cut out for us as we try to find a comprehensive approach in the need for reform.

Thank you very much, Madam Chair.

Mrs. DAVIS OF VIRGINIA. Thank you.

I ask unanimous consent that all Members have 5 legislative days to submit written statements and questions for the hearing record and that any answers to written questions provided by the witnesses also be included in the record. Without objection, so ordered.

I also ask unanimous consent that all exhibits, documents and other materials referred to by Members and the witnesses may be included in the hearing record and that all Members be permitted to revise and extend their remarks. Without objection, so ordered.

Our first witness today is our colleague, Congressman Dutch Ruppersberger. I am delighted that you were able to accept our invitation to testify at the first hearing of the Subcommittee on Civil Service and Agency Organization. By tradition, we do not administer an oath to Members of Congress, so you are recognized for 5 minutes, Congressman.

STATEMENT OF HON. C.A. DUTCH RUPPERSBERGER, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MARYLAND

Mr. RUPPERSBERGER. Thank you, Madam Chairman, and it is a pleasure to be here.

I have two people here who are not going to testify, Attorney Sharborough, director of human resources for Baltimore County, and Melissa Boone, who is gainsharing program manager.

I am here really based on the previous 8 years when I was Baltimore County executive and we implemented a gainsharing program which is really an employee group-incentive based on performance.

First, what is gainsharing? Gainsharing is a group incentive program. Gainsharing rewards employees for making improvements that reduce costs without compromising quality and objectives. The concept is based on team work where participating employees improve performance and get to share in the savings. For example, if savings are generated, the group of employees receives half of the savings while the other half goes into the General Fund of the treasury of that government.

Let me start by saying gainsharing is a program that works. It saves money but more importantly, it boosts morale and it makes government service more responsive and cost-effective. That is a very important element of gainsharing, the morale and making employees feel as if they are shareholders in the government.

Programs like gainsharing will only succeed if everyone who is affected by the process is brought to the table. For example, in Baltimore County, we could not have done this without the cooperation of our employee unions. What we are talking about here today is using the Volcker Commission recommendations and changing the culture of government management and workers.

Baltimore County has approximately 761,000 citizens which makes the county more populous than four States and larger in land than two States. There are 19,000 employees and it has an operating budget of $2 billion. Baltimore County is the only one of two counties in the country that has no municipalities which means the county provides all the services. Baltimore County has a strong executive rule. The county executive has the power to establish the budget. The county council approves the budget but they can only cut the budget. The county council cannot increase the budget or move funds from one area to another and the county's budget must be balanced each year. It is a challenging county with a diversity of incomes, a diversity of people, a diversity of education levels, a diversity of work force, and a diversity of geographic location which wraps around Baltimore City and is urban, suburban and two-thirds rural. Providing services to all these distinct and unique populations and areas is very challenging.

When I took office as Baltimore County executive in January 1995, county employees had not received pay raises in 4 of the previous 5 years. Layoffs in several departments had further damaged morale while demand for services had increased. By 1996, Baltimore County was experiencing a narrow revenue stream and aging infrastructure. In the 4-years before 1996, the county work force had declined by 17 percent, there had been a job freeze, the first employee layoffs in county history and there were two early retirement programs enacted. There had only been one cost-of-living-adjustment in the 6-years before. Needless to say, county employees' morale was at an all time low.

While serving on the Baltimore County council prior to becoming Baltimore County executive, I observed that the gradual decline in employee morale was affecting service quality to our citizens. As county executive, I wanted quality and productive improvements. I believe government is basically a service industry and we need to be more responsive to our constituents.

The question was, how do we make working for the county rewarding and exciting? How do we get our employees to be vested in their government and how do we make them want to perform for the benefit of everyone? After researching the issue, I concluded that a gainsharing program would meet all those criteria with no added cost to the taxpayers. One of my first acts was to bring aboard a human resources consulting firm, a local consultant from the Regional Economic Studies Institute at Towson State University in Baltimore County. Development of the gainsharing program began in November 1995 with a survey of employees across all departments to determine the readiness to participate. While initially hesitant about the program, the union leaders believed that the gainsharing program demonstrated that people in the field, the frontline employees, do know their job the best. The process enabled Baltimore County workers to prove they could deliver better service at lower costs with virtually no complaints.

Baltimore County's gainsharing program brings together many old ideas in a new package. It uses total quality management principles and teambuilding strategies to transform frontline workers. The team goal is to improve performance and save money by bringing the insights and experience of frontline workers to bear on the problems. The program's emphasis on getting frontline employees to develop solutions empowers them to become shareholders in the government, much like in the private sector. The bottom line is Baltimore County's gainsharing program generates cost savings and increases employee morale while also improving the quality of service at the local government level.

We have to remember that this program worked because we brought everyone into the tent. We talked to and gained the support of our employees, we brought together both mid-level and top level management and facilitated cooperation between them and our frontline employees and we retained outside consultants to get their insight to work on these solutions. The result was a highly motivated, effective and cost-efficient work force that delivers quality service to our constituents.

Baltimore County's gainsharing program won a national award from Harvard University and the Ford Foundation for innovations in government. Since the program was implemented it has saved over $4.1 million. With the help of the gainsharing program, Baltimore County was 1 of only 20 counties out of 3,000 that were able to obtain an AAA bond ratings from the rating houses in New York. As a result of that, the governing magazine rated Baltimore County as one of the top four managed counties in the country.

As a result of increased employee morale, increased government efficiency and a well managed county, our administration and as Baltimore County Executive, was able to attract over 40,000 new jobs which eclipsed the previous administration job creation of 800, going from 800 jobs to 40,000 new jobs over the 7-year period. One

of the reasons is employees and business want to be involved and went to a county they feel is well managed and where there are good services for their employees.

Baltimore County is only one of a handful of governments that have implemented a gainsharing program. Because of that, Baltimore County is receiving inquiries from local, State and Federal Government from around the country. I am pleased to say the gainsharing program has gone international. Last year, the State Department made inquiries into the success of Baltimore County's gainsharing program. After a review of our successful program, the State Department asked for funding from Congress to implement a gainsharing program. Most recently, U.S. workers have looked to implement the gainsharing program abroad. Members of Baltimore County's gainsharing program have traveled to Belgium to train the State Department employees in that country.

If we are looking to revitalize and change the culture of the Federal Government, we have to make sure that our frontline workers are vested in what is happening. We should encourage all Federal employees and managers to find ways to improve performance. Gainsharing is not just about employees getting additional money for performance. It is about the employees becoming shareholders in the government and as a result, we will have improved morale which leads to improved government performance.

[The prepared statement of Hon. C.A. Dutch Ruppersberger follows:]

Statement of Congressman C.A. Dutch Ruppersberger
Testimony on Gainsharing
Before the Civil Service Subcommittee on Government Reform
April 1, 2003

What is Gainsharing? Gainsharing rewards employees for making improvements that reduce costs without compromising quality and service objectives. The concept is based on teamwork, where participating employees improve performance and get to share in the savings.

Let me start by saying Gainsharing is a program that works. It saves money, but more importantly it boasts morale and more importantly it makes government service more responsive and cost effective.

But, programs like Gainsharing will only succeed if everyone who is affected by the process is brought to the table. For example, in Baltimore County we could not have done this without the cooperation of our employee's unions.

What we are talking about here today is using the Volcker Commission recommendations and changing the culture of government managers and workers.

Baltimore County Overview

Baltimore County has approximately 761,148 citizens which makes the County more populous than four states and larger in land area than 2 states.

There are 19,000 employees and it has an operating budget of $2 billion dollars.

Baltimore County is only one of two counties in the country that have no municipalities, which means the county provides all of the services.

Baltimore County has a "Strong Executive" rule. Where the County Executive has the power to establish the budget, while the County Council authorizes the budget they can only cut the budget. The County council cannot increase the budget or move funds from one area to another, and the County's budget must be balanced each year.

It is a challenging county with a diversity of incomes, a diversity of people, a diversity of education levels, and a diversity of geographic location which wraps around the city and is urban, suburban, and two-thirds rural. Providing services to all these distinct and unique populations and areas was very challenging.

Evolution of Gainsharing

When I took office, As Baltimore County Executive, in January 1995, county employees had not received pay raises in four of the previous five years. Layoffs in several departments had further damaged morale, while demand for services had increased.

By 1996, Baltimore County was experiencing a narrowing revenue stream and aging infrastructure. In the four years before 1996 the county work force had declined by 17 percent. There had been a job freeze, the first employee layoffs in the county history, there were two early retirement programs enacted, and there had only been one cost of living adjustments in the six years before. Needless to say County employee morale was very low.

While serving for nine years on the Baltimore County Council I had observed that the gradual decline in employee morale was affecting service quality.

As County Executive, I wanted quality and productivity improvements, I believe government is basically a service industry and we needed to be more responsive to our constituents.

The question was how do we make working for the County rewarding and exciting. How do we get our employees to be vested in their government and how do we make them want to perform for the benefit of everyone.

After researching the issue, I concluded that a Gainsharing program would meet all those criteria at no added cost to taxpayers. One of my first acts was to bring aboard a human resources consulting firm and a local consultant from the Regional Economic Studies Institute at Towson State University in Baltimore.

Development of the Gainsharing program began in November 1995, with a survey of employees across all departments to determine their readiness to participate.

While initially hesitant about this program, Union leaders believe that the Gainsharing program demonstrated that people in the field, the front-line employees, know their job best.

The process enabled Baltimore County workers to prove that they could deliver better service, at a lower cost, with virtually no complaints.

Gainsharing Program Overview

Baltimore County's Gainsharing program brings together many old ideas in a new package. It uses Total Quality Management principles and team building strategies to transform frontline workers. The team goal is to improve performance and save money by bringing the insights and experience of front line workers to bear on problems.

In such a service environment as government, the motivation and capabilities of the employee's is what will ultimately improve performance. Gainsharing is a guaranteed way to improve workforce productivity, because it is designed to use the knowledge of front line workers to improve and enhance performance goals.

The program's emphasis on getting front-line employers to develop solutions empowers them to become shareholders in the government, much like in the private sector.

The bottom line is, Baltimore County's Gainsharing program generates costs savings and increases employee morale, while also improving the quality of service at the local government level.

Lessons Learned about Gainsharing

We have to remember that this program worked because we brought everyone into the tent. We talked to and gained the support of our employees, we brought together both mid-level and top level management and facilitated cooperation between them and our front line employees, and we retained outside consultants to get their insight to work on these solutions.

The result was a highly motivated, effective and cost efficient work force that delivers quality service to our constituents.

Where Gainsharing is now

Baltimore County's Gainsharing program won a National award from Harvard University and the Ford Foundation for innovations in Government.

Since the program has been implemented it has saved $3.4 million dollars.

With the help of the Gainsharing program Baltimore County was one of the twenty counties out of three thousand that were able to attain three triple-A bond ratings from the rating houses in New York. As a result *Governing* magazine rated Baltimore County as one of the top four managed counties in the country.

I am pleased to say that the Gainsharing program has gone internationally. Last year, the State Department made inquiries into the success of Baltimore County's Gainsharing program. After their review of our successful program the State Department asked for funding from Congress to implement Gainsharing. And most recently, U.S. workers have looked to implement a Gainsharing program abroad. Members of Baltimore County's Gainsharing program have traveled to Belgium to help train and implement U.S. workers in that country.

If we are looking to revitalize and change the culture of the federal government we have to make sure that our front line workers are vested in what is happening. We should encourage all federal employees and managers to find ways to improve performance.

Gainsharing is not just about employees gaining additional money for performance. It is about the employees becoming shareholders in the government. As a result we will have improved morale which leads to improved government performance.

Mrs. DAVIS OF VIRGINIA. Dutch, thank you so much for being willing to come and share that success story. I think you hit on some critical points there that you can't make changes without bringing all parties to the table. That includes the managers, the employees, the unions who are there for the workers and I appreciate your coming and testifying.

Historically on the Hill, we don't question the Members when they come.

Mr. RUPPERSBERGER. If you would like to question me, you can.

Mrs. DAVIS OF VIRGINIA. I think my ranking member would like to ask a question but I will tell you, we normally don't do it. We are not setting a precedent either.

Mr. DAVIS OF ILLINOIS. I would just ask in terms of participation, was this done by divisions, departments or just areas of work and how did that get organized?

Mr. RUPPERSBERGER. What happened is we realized we had to get outside consultants to implement a program because there are always programs and new administrations are finding ways to do this. I studied this gainsharing for years when I was on the county council and read about it, how utility companies had been able to use it, so I realized we needed to get experts in the area and we hired national consultants. They came in and analyzed our government. They picked pilot programs to start the gainsharing program for Baltimore County.

As an example, one area was food service in our detention center where individuals were making maybe $23,000-$24,000 a year. They came together as a group. They were frontline employees who said we can do this better if management would listen. They came together with management, had facilitators there to help them, made the changes and each and every employee, after the changes were made and the money was saved, took home about a $5,000 bonus that year. All of a sudden, the labor unions that were all upset about this new program said we want a piece of this action.

Another example was in our grass cutting in Rec and Parks, as county executive I was getting ready to privatize it because they just weren't producing. We went to the frontline and worked with them. They said, if you give us the resources and the equipment, we could beat any private sector. They had facilitators, came as a group, discussed how they could cut the grass the best way, and they ended up improving performance. The whole concept is as performance is improved, costs go down. Then all of a sudden everyone wanted to be involved.

It is a program that you just don't show up with a good idea. If you have an idea as a frontline employee, you come together, go to the facilitator, the facilitator will bring the group together as the frontline, almost like a group therapy session and talk about the program. Then they will put the program in writing and the program will go to the department head and eventually would come to me. If the program worked, all of a sudden frontline employees would just go punch the clock and say we are a part of this operation, we feel good about this, we are shareholders in this operation. Then it kept going from department to department.

To give an example of how gainsharing works, you can't give police officers a bonus for the arrests they make. You have one vehi-

cle used by three shifts and the same people drive the same car. If one group doesn't put their foot on the brakes and they don't have to change tires in 6 months where another group had to change it every 2 months, that would be a savings, a group incentive to improve performance which cuts costs. Part of that savings goes back to them.

Let me say this because sometimes we get these programs confused. The main issue of gainsharing is not really the bonus or the extra money that goes back to employees because performance is improved, the main issue is the morale that in good times and bad times, the employees feel they have the ability on the frontline. How many times do we see in any government or bureaucracy that midlevel managers were good employees or they were not good managers, were never trained and interfere with frontline. All of a sudden this relationship between management and frontline improved and like teambuilding, you had morale. When morale changes, a lot of things change. So far this program has continued to work. We are still in a recession now. When I say "we" I mean Baltimore County, my previous job, and we still have employees who feel good about going to work.

Mr. DAVIS OF ILLINOIS. Thank you very much. For many years, I have been an advocate of what I call the shared approach to management, so I see why you got elected to Congress.

Mrs. DAVIS OF VIRGINIA. Ms. Blackburn, do you have a question?

Ms. BLACKBURN. Yes, I do have one. This sounds absolutely fascinating and I thank you for your comments.

Going back to the compensation, could your individual managers decide if they wanted to give an increase in salary or if it was going to be given as a bonus or a promotion or your incentivization program, what you would do to incentivize your employees, who made that decision?

Mr. RUPPERSBERGER. The incentive has to be the entire team, that is the team concept. We had other incentive programs that were in the county but basically this is a team concept, so the entire team will be compensated. What is really good about it is if you have people on the team that aren't working or carrying their weight, management doesn't even have to get involved in that. The team comes together and the team will say, look, you are hurting us, we have this program to improve performance. Because you are lazy or you are not doing the job, you are hurting us. So it is strictly a team concept, has nothing to do with our merit or compensation system, entirely different, a team concept.

This is a program that you have to develop the program with a facilitator and it has to be approved but it comes from the frontline.

Ms. BLACKBURN. You mentioned $4.1 million in savings. Overall, what percentage of your budget per year would you say you see as a savings?

Mr. RUPPERSBERGER. I don't know what that would be—less than 2 percent.

Ms. BLACKBURN. Less than 2 percent, that is great.

Mr. RUPPERSBERGER. Remember, every department doesn't have a gainsharing program. It starts with the employees and the facilitators.

Mrs. BLACKBURN. Were you able to reduce your overall budget because of the success of the program?

Mr. RUPPERSBERGER. Well, basically I would say that is why I talked about our AAA bond rating and how Governing Magazine rated Baltimore County. They write about counties and cities and evaluate them. So I think from a management perspective, yes, we were able to improve performance. As performance goes up, costs go down. Yes, clearly in the areas in which we were working, costs were going down in that regard and the performance was going up. The difference is the savings was going half to the group, the employees, and half back to our general fund.

Ms. BLACKBURN. To the general fund. Thank you.

Mrs. DAVIS OF VIRGINIA. We have started a trend here but we are not going to continue it next hearing.

Ms. Norton, do you have any questions?

Ms. NORTON. No, but thank you for your graciousness.

Mrs. DAVIS OF VIRGINIA. Mr. Van Hollen.

Mr. VAN HOLLEN. No, thank you.

Mrs. DAVIS OF VIRGINIA. We have been joined by Mr. Murphy. I don't want to catch you off guard but would you happen to have any questions for Congressman Ruppersberger?

Mr. MURPHY. No. It is good to have him here.

Mrs. DAVIS OF VIRGINIA. Dutch, I thank you so much for coming and appreciate your taking the time. I know how busy a Member's schedule is. It was very enlightening. Thank you.

Mr. RUPPERSBERGER. Thank you.

Mrs. DAVIS OF VIRGINIA. If the second panel would come forward and remain standing, we do ask that each witness be administered an oath.

[Witnesses sworn.]

Mrs. DAVIS OF VIRGINIA. The witnesses will now be recognized for opening statements. We ask that you summarize your testimony in 5 minutes. We have your written testimony and I would hope all Members have had an opportunity to read it. Your written testimony will be made a part of the record.

I would like to welcome OPM Deputy Director, Dan Blair and the Executive Director of the National Commission on the Public Service, Hannah Sistare. I thank you both for being with us today. Mr. Blair, we will start with you and recognize you for 5 minutes.

STATEMENTS OF DAN G. BLAIR, DEPUTY DIRECTOR, OFFICE OF PERSONNEL MANAGEMENT; AND HANNAH S. SISTARE, EXECUTIVE DIRECTOR, NATIONAL COMMISSION ON THE PUBLIC SERVICE

Mr. BLAIR. Thank you very much, Madam Chair. It is indeed an honor and privilege to be here today to represent Director James. I appreciate this opportunity to appear before the subcommittee, particularly on this panel with Hannah Sistare. Hannah and I are longtime colleagues. She was a true mentor and friend. I am particularly pleased to be on this panel with her.

I would also like to acknowledge the good work of OPM's Deputy Associate Director for Pay and Performance Policy, Don Winstead who is sitting in back of me.

I ask that my entire written statement be adopted for the record.

Mrs. DAVIS OF VIRGINIA. So ordered.

Mr. BLAIR. On behalf of Director James, I am pleased to appear here today. I would like to talk about what we have been doing in terms of compensation reform for Federal employees.

Following Director James' appointment as Director of OPM, she asked the staff to take an in-depth look at white collar Federal pay. The result was a White Paper entitled, "A Fresh Start for Federal Pay: The Case for Modernization." The intent of the White Paper was not to lay out specific reform proposals or solutions. Rather, it was to expose the current problems with the Government's white collar pay system.

The paper concluded the following points. The current General Schedule is an antiquated system best suited for the 1950's work force but not for today's knowledgable work force. It has minimal ability to encourage and reward achievement and results. It does not adequately reflect market pay and it precludes agency's from tailoring pay programs to their specific mission and labor markets.

Since the paper was released, the conversation about pay modernization has continued on a number of fronts. Last year, Congress enacted legislation creating the new Department of Homeland Security. It was significant that Congress recognized that the new department needed flexibility for a modernized approach for compensation by authorizing the Director of OPM and the Secretary for DHS to jointly develop and establish a new human resources system. We are in the initial stages of working with DHS managers and employees to identify those options for consideration.

We also recognize the thought provoking work contained in the recent report of the National Commission on Public Service. The Commission concluded that the Federal Government must be reshaped and that the systems that support it must be rooted in a new personnel management system which has principles and ensure a much higher level as a government performance. Indeed, the President's budget for fiscal year 2004 includes two proposals intended to help create a pay for performance culture in the Federal Government.

First, the administration proposes establishment of a Human Capital Performance Fund. Second, the administration proposes to raise the pay cap for the Senior Executive Service and implement an open pay range for senior executives.

First, let me talk about the Human Capital Performance Fund. Under this proposal, $500 million would be appropriated in fiscal year 2004 for allocation by OPM to agencies that submit a plan to use their share of the fund for performance-based increases in basic pay. The fund would represent an important tool for rewarding high performing employees and it points the way to a greater emphasis on employee performance and contributions to mission accomplishments by requiring robust performance management as a criterion for funding but also for providing incentive for agencies to improve their performance management systems and human capital strategies aligning them more closely with their mission and goals.

The proposal would leave intact for now the General Schedule Pay System. Individual employees would remain at their existing grade and step levels. Annual across the board adjustments would

continue as well as locality pay and within grade step increases, while leaving the General Schedule and job evaluation system basically intact, proposed as an important first step in our efforts to bring performance-based compensation to the Federal Government. With this proposal, we can begin distinguishing between high and low performers in a meaningful way.

The second proposal to increase performance sensitivity of Federal pay system focuses on how we pay our senior executives. The administration recognizes that pay compression within the SES could result in serious recruitment and retention problems. More importantly, the current structure under which more than 60 percent of all senior executives receive exactly the same salary despite varying degrees of responsibilities and duties fails to support the goal of developing a pay-for-performance culture.

If we cannot demonstrate the value of a performance oriented pay system for our senior executives, how can we expect to foster development of performance oriented pay systems for the rest of the Federal Government?

I believe the administration's Human Capital Performance Fund and SES pay reform proposals represent major steps toward the establishment of long-term goals and modernizing Federal pay systems. We are confident these proposals will keep the dialog moving in the right direction.

Also, let me acknowledge the important work that effective performance management will play in any compensation program. OPM's White Paper announced how credible, reliable performance measures that make appropriate performance distinctions are critical to successfully increasing the link between pay and performance.

Thank you very much for this opportunity. I would be pleased to answer any questions.

[The prepared statement of Mr. Blair follows:]

STATEMENT OF THE HONORABLE DAN G. BLAIR
DEPUTY DIRECTOR
OFFICE OF PERSONNEL MANAGEMENT

before the

SUBCOMMITTEE ON CIVIL SERVICE AND AGENCY ORGANIZATION
COMMITTEE ON GOVERNMENT REFORM
U.S. HOUSE OF REPRESENTATIVES

on

COMPENSATION REFORM FOR FEDERAL EMPLOYEES

APRIL 1, 2003

MADAM CHAIRMAN AND MEMBERS OF THE SUBCOMMITTEE:

GOOD AFTERNOON. ON BEHALF OF THE DIRECTOR OF THE OFFICE OF PERSONNEL MANAGEMENT (OPM), KAY COLES JAMES, I APPRECIATE THE OPPORTUNITY TO APPEAR BEFORE YOU TODAY TO DISCUSS COMPENSATION REFORM FOR FEDERAL EMPLOYEES.

SHORTLY AFTER HER APPOINTMENT AND CONFIRMATION AS THE DIRECTOR OF OPM, KAY COLES JAMES ASKED OPM STAFF TO TAKE AN IN-DEPTH LOOK AT THE WAY THE FEDERAL GOVERNMENT PAYS ITS WHITE-COLLAR EMPLOYEES. THE PRODUCT OF THAT REVIEW WAS A WHITE PAPER, ENTITLED "A FRESH START FOR FEDERAL PAY: THE CASE FOR MODERNIZATION." THE WHITE PAPER WAS DESIGNED TO "LET THE CONVERSATION BEGIN." ALTHOUGH IT PURPOSELY DID NOT LAY OUT SPECIFIC PROPOSALS FOR CHANGING THE WAY WHITE-COLLAR EMPLOYEES ARE PAID, THE WHITE PAPER DID LAY BARE A NUMBER OF

PROBLEMS WITH THE FEDERAL GOVERNMENT'S CURRENT WHITE-COLLAR PAY AND JOB EVALUATION SYSTEMS. THE WHITE PAPER CONCLUDED STRAIGHTFORWARDLY THAT THE GENERAL SCHEDULE PAY SYSTEM—

(1) IS ANTIQUATED AND SUITS THE WORKFORCE STRUCTURE OF 1950, NOT TODAY'S KNOWLEDGE WORKERS;

(2) HAS MINIMAL ABILITY TO ENCOURAGE AND REWARD ACHIEVEMENT AND RESULTS;

(3) DOES NOT ADEQUATELY REFLECT MARKET PAY LEVELS; AND

(4) PRECLUDES AGENCIES FROM TAILORING PAY PROGRAMS TO THEIR SPECIFIC MISSIONS AND LABOR MARKETS.

SINCE THE RELEASE OF THE WHITE PAPER A YEAR AGO, THE CONVERSATION ABOUT PAY MODERNIZATION HAS CONTINUED IN A NUMBER OF FORUMS. LAST YEAR, CONGRESS ENACTED LEGISLATION ESTABLISHING A NEW DEPARTMENT OF HOMELAND SECURITY (DHS). IN SO DOING, CONGRESS RECOGNIZED THE NEED OF THE NEW DEPARTMENT FOR A MODERNIZED APPROACH TO COMPENSATION BY AUTHORIZING THE DIRECTOR OF OPM AND THE SECRETARY OF HOMELAND SECURITY JOINTLY TO DEVELOP AND ESTABLISH NEW HUMAN RESOURCES SYSTEMS FOR DHS, INCLUDING NEW BASIC PAY SYSTEMS. WE ARE NOW IN THE INITIAL STAGES OF WORKING WITH DHS MANAGERS AND EMPLOYEES TO IDENTIFY OPTIONS FOR FURTHER CONSIDERATION LATER THIS YEAR.

EARLY THIS YEAR, THE NATIONAL COMMISSION ON THE PUBLIC SERVICE, CHAIRED BY PAUL VOLCKER, ISSUED ITS REPORT, ENTITLED "URGENT BUSINESS FOR AMERICA: REVITALIZING THE FEDERAL GOVERNMENT FOR THE 21ST CENTURY." AMONG THE MANY THOUGHT-PROVOKING CONCLUSIONS OF THIS REPORT WAS THAT "THE FEDERAL GOVERNMENT MUST BE RESHAPED, AND THE SYSTEMS THAT SUPPORT IT MUST BE ROOTED IN NEW PERSONNEL MANAGEMENT PRINCIPLES THAT ENSURE MUCH HIGHER LEVELS OF GOVERNMENT PERFORMANCE." THE REPORT RECOMMENDS THAT THE CURRENT GENERAL SCHEDULE SYSTEM BE ABOLISHED AND NOTES THAT, UNDER THE PRESSURE FOR BETTER PERFORMANCE, MOVEMENT AWAY FROM THE GENERAL SCHEDULE HAS ALREADY BEGUN. WE AGREE WITH THE VOLCKER COMMISSION THAT ANY NEW PAY SYSTEM FOR FEDERAL EMPLOYEES MUST BE DESIGNED SO THAT AGENCIES CAN BETTER RECOGNIZE AND VALUE THE COMPETENCIES AND CONTRIBUTIONS OF THEIR EMPLOYEES.

THE PRESIDENT'S BUDGET FOR FISCAL YEAR 2004 INCLUDES TWO PROPOSALS THAT ARE DESIGNED TO HELP THE FEDERAL GOVERNMENT BEGIN TO CREATE A PAY-FOR-PERFORMANCE CULTURE. THE FIRST OF THESE PROPOSALS IS THE ESTABLISHMENT OF A NEW "HUMAN CAPITAL PERFORMANCE FUND." UNDER THE ADMINISTRATION'S PROPOSAL, $500 MILLION WOULD BE APPROPRIATED IN FY 2004 FOR ALLOCATION BY OPM TO AGENCIES THAT SUBMIT A PLAN TO USE THEIR SHARE OF THIS FUND FOR PERFORMANCE-BASED INCREASES IN BASIC PAY.

THE HUMAN CAPITAL PERFORMANCE FUND WOULD BE AN IMPORTANT NEW TOOL FOR USE BY FEDERAL AGENCIES IN REWARDING HIGH-PERFORMING EMPLOYEES. IT POINTS THE WAY TOWARD GREATER EMPHASIS ON EMPLOYEE PERFORMANCE AND CONTRIBUTIONS TO MISSION ACCOMPLISHMENT, RATHER THAN LONGEVITY. BY REQUIRING ROBUST PERFORMANCE MANAGEMENT AS A CRITERION FOR FUNDING, IT WOULD ALSO PROVIDE AN INCENTIVE FOR AGENCIES TO IMPROVE THEIR PERFORMANCE MANAGEMENT SYSTEMS AND HUMAN CAPITAL STRATEGIES AND ALIGN THEM MORE CLOSELY WITH THEIR MISSION AND GOALS.

THE PRESIDENT'S PROPOSAL TO ESTABLISH A NEW HUMAN CAPITAL PERFORMANCE FUND WOULD NOT AFFECT THE OPERATION OF THE GENERAL SCHEDULE PAY SYSTEM ITSELF. INDIVIDUAL EMPLOYEES WOULD REMAIN AT THEIR EXISTING GRADE AND STEP AND WOULD CONTINUE TO RECEIVE ANNUAL ACROSS-THE-BOARD PAY INCREASES, LOCALITY PAYMENTS, AND PERIODIC WITHIN-GRADE INCREASES. ANY PAYMENT FROM THE HUMAN CAPITAL PERFORMANCE FUND, HOWEVER, WOULD BE TREATED AS BASIC PAY FOR RETIREMENT AND BENEFITS PURPOSES AND WOULD STAY WITH THE EMPLOYEE IN FUTURE YEARS.

THIS PROPOSAL WOULD LEAVE THE GENERAL SCHEDULE PAY AND JOB EVALUATION SYSTEM BASICALLY INTACT. BUT IT IS AN IMPORTANT FIRST STEP IN OUR EFFORTS TO BRING PERFORMANCE-BASED COMPENSATION TO THE FEDERAL GOVERNMENT. WITH THIS PROPOSAL, WE CAN BEGIN

DISTINGUISHING BETWEEN HIGH AND LOW PERFORMERS IN A MEANINGFUL WAY.

THE SECOND BUDGET PROPOSAL TO INCREASE THE PERFORMANCE-SENSITIVITY OF FEDERAL PAY SYSTEMS FOCUSES ON THE GOVERNMENT'S SYSTEM FOR COMPENSATING SENIOR EXECUTIVES. THE ADMINISTRATION RECOGNIZES THAT "PAY COMPRESSION" WITHIN THE SENIOR EXECUTIVE SERVICE (SES) COULD RESULT IN SERIOUS RECRUITMENT AND RETENTION PROBLEMS. PERHAPS EVEN MORE IMPORTANTLY, THE CURRENT STRUCTURE OF THE SES PAY SYSTEM—UNDER WHICH MORE THAN 60 PERCENT OF ALL SENIOR EXECUTIVES RECEIVE EXACTLY THE SAME SALARY—FAILS TO SUPPORT THE OBJECTIVE OF DEVELOPING A PAY-FOR-PERFORMANCE CULTURE IN THE FEDERAL GOVERNMENT. IF WE CANNOT DEMONSTRATE THE VALUE OF A PERFORMANCE-ORIENTED PAY SYSTEM FOR OUR SENIOR EXECUTIVES, HOW CAN WE EXPECT TO FOSTER THE DEVELOPMENT OF PERFORMANCE-ORIENTED PAY SYSTEMS FOR THE REST OF THE FEDERAL WORKFORCE?

THE ADMINISTRATION'S SES PAY REFORM PROPOSAL WOULD ELIMINATE THE FIXED PAY LEVELS WITHIN THE CURRENT SES PAY SYSTEM IN FAVOR OF AN OPEN PAY RANGE WITH A HIGHER PAY CAP. BY ALLOWING FEDERAL AGENCIES TO ADJUST PAY FOR SES MEMBERS WITHIN A LARGER PAY RANGE, AGENCIES WOULD BE ABLE TO MAKE MEANINGFUL DISTINCTIONS IN PAY BASED ON EACH INDIVIDUAL EXECUTIVE'S PERFORMANCE AND CONTRIBUTION TO THE AGENCY'S MISSION AND GOALS. A "ONE SIZE FITS ALL" PAY SYSTEM DOESN'T

WORK FOR SENIOR EXECUTIVES ANY BETTER THAN IT WORKS FOR OTHER EMPLOYEES, AND WE ARE EAGER TO SHOW THAT A PERFORMANCE-ORIENTED PAY SYSTEM CAN WORK FOR SENIOR EXECUTIVES.

WE BELIEVE THE ADMINISTRATION'S "HUMAN CAPITAL PERFORMANCE FUND" AND SES PAY REFORM PROPOSALS REPRESENT MAJOR STEPS TOWARD THE LONGER-TERM GOAL OF MODERNIZING FEDERAL PAY SYSTEMS. WE ARE CONFIDENT THAT THESE PROPOSALS WILL KEEP THE CONVERSATION MOVING IN THE RIGHT DIRECTION. THESE TWO PROPOSALS TO INCREASE THE PERFORMANCE SENSITIVITY OF FEDERAL PAY SYSTEMS ARE GROUND-BREAKING.

SOME OF THE PROBLEMS DESCRIBED IN OPM'S WHITE PAPER WILL REQUIRE DIFFERENT SOLUTIONS. THIS IS PARTICULARLY TRUE FOR OUR BASIC JOB EVALUATION SYSTEM, WHICH REQUIRES MAKING DISTINCTIONS AMONG 15 SEPARATE GRADE LEVELS OF WHITE COLLAR WORK. MODERN KNOWLEDGE-BASED WORK IS SIMPLY NOT SUITED TO SUCH PIGEON-HOLING, AND OPM REMAINS COMMITTED TO PROPOSING MORE MODERN APPROACHES TO MEET THE MERIT SYSTEM PRINCIPLE OF PROVIDING EQUAL PAY FOR WORK OF EQUAL VALUE.

AS A FINAL POINT BEFORE CLOSING, I ALSO WANT TO ACKNOWLEDGE THE IMPORTANT PART THAT EFFECTIVE PERFORMANCE MANAGEMENT WILL PLAY IN ANY REFORM OF FEDERAL COMPENSATION. OPM'S WHITE PAPER NOTES HOW

CREDIBLE, RELIABLE PERFORMANCE MEASURES THAT MAKE APPROPRIATE PERFORMANCE DISTINCTIONS ARE CRITICAL TO SUCCESSFULLY INCREASING THE LINK BETWEEN PERFORMANCE AND PAY.

WE ARE MINDFUL THAT MANY AGENCIES HAVE WORK TO DO TO GET THEIR PERFORMANCE MANAGEMENT PROGRAMS AND PRACTICES INTO SHAPE TO SUPPORT PAY-FOR-PERFORMANCE. SUPERVISORS AND MANAGERS MUST BE TRAINED AND HELD ACCOUNTABLE FOR SETTING CLEAR EXPECTATIONS, PROVIDING ONGOING FEEDBACK, MAKING MEANINGFUL DISTINCTIONS AMONG LEVELS OF EMPLOYEE PERFORMANCE, AND ACTING ON THOSE DISTINCTIONS.

THIS CONCLUDES MY REMARKS. I WILL BE HAPPY TO ANSWER ANY QUESTIONS.

Mrs. DAVIS OF VIRGINIA. Thank you, Mr. Blair.

Ms. Sistare.

Ms. SISTARE. Chairwoman Davis, Congressman Davis and members of the subcommittee, on behalf of Paul Volcker and the members of the National Commission on the Public Service, I thank the subcommittee for asking the Commission to share its findings and recommendations on the issue of pay reform.

Paul Volcker took up the cause of the public service again because of many of the same concerns that motivated the first National Commission on the Public Service. The commissioners who agreed to join him in this task are from all political persuasions in both major political parties. Each of them has a wealth of public service experience. Collectively they have served every Presidential administration beginning with President Harry Truman. From start to finish, the Commission was aided, challenged and encouraged by many organizations and individuals concerning the state of the public service.

The Commission examined Federal pay in all three branches and at all levels. Three principles are suggested by the Commission in the report. First, government pay must reflect current market conditions if government is to attract and retain the work force it needs to perform its responsibilities.

Second, the relevant market for most of the Federal work force should be comparable jobs and capabilities in the general work force. The relevant market for government senior leadership should be positions demanding comparable responsibility and capabilities in the nonprofit work force.

Third, pay should be tied to performance. As noted, for the majority of the Federal work force, the private/non-profit sector was identified as the most appropriate market. The Commission recommended that Congress establish policies that permit agencies to determine the specific relevant market for their employees.

Currently, the Commission recommended that the existing classification system and the General Schedule be terminated. The Commission recommended a broad band system be adopted as the government's default system. In the alternative, agencies would adopt systems which best suited their own missions.

The Commission suggested a different compensation standard for senior government positions such as Federal judgeships, executives and Members of Congress. There they look to comparable positions in the private/nonprofit sector as a guide. We developed a comparison of executive pay for several categories of nongovernmental, nonprofit entities. In every case, the compensation of the nonprofit leadership was notably higher than that of the senior leadership of the Federal Government.

Another area of particular concern is the Senior Executive Service. This cadre of senior executives was established to provide the government with a skilled leadership without all the traditional Civil Service protections but with the ability to be rewarded for excellent performance. As a result of the pay cap, nearly 70 percent of the SES earns the same compensation. This clearly rules out rewarding excellence in performance.

The Commission recommends that Congress immediately increase the pay of capped senior government officials including Fed-

eral judges and Members of Congress themselves. Should Congress not wish to give itself this level of increase, the Commission asked it to decouple its own pay from that of Federal executives and judges.

I will repeat for the record a statement the Commission included in the report, "Few democracies in the world expect so much from their national legislators for so little in compensation."

Two additional areas addressed by the Commission bear on the issue of compensation flexibility. First is the importance of increased and careful oversight by Congress and responsible executive branch leadership to assure that the new system and personnel flexibility stay on track. Careful and ongoing oversight including statutory assurance of merit principles of government employment can ease concerns about abuse and prevent it from occurring.

Second and related is the importance of ongoing training. The Commission believed that adequate and consistently funded training for all Federal employees was of great importance.

The Commission focused to a greater extent in its report on pay of top governmental officials than it did on pay of the broad Federal work force first because of the clear challenge to effective governance when the leadership of government is significantly underpaid, and second, because the executive level pay caps are currently a barrier to pay reform, the entire work Federal work force.

Finally, an important barrier to utilizing existing performance incentives is the government performance rating process itself. Like the residents of Lake Woebegone, everyone working for the Federal Government performs above average. In fact, most of the Federal work force is in the superior category. Of 700 employees rated in 2001 using the pass/fail system, 93 percent passed and just 0.06 percent failed. Of the 800,000 who were rated that year using a 5 point system, 43 percent were outstanding, 28 were exceeds fully successful and 18 percent was fully successful.

The system is in need of reform. Agencies must adopt and apply credible measures of performance with appropriate training and oversight.

Thank you again.

[The prepared statement of Ms. Sistare follows:]

Subcommittee on Civil Service and Agency Organization
Committee on Government Reform
U.S. House of Representatives
April 1, 2003

Testimony Presented on behalf of the National Commission on the Public Service

Paul A. Volcker, Chairman

Commissioners

Charles Bowsher	**Bill Bradley**
Frank C. Carlucci	**Kenneth M. Duberstein**
Constance Horner	**Franklin D. Raines**
Richard Ravitch	**Robert E. Rubin**
Donna E. Shalala	**Vin Weber**

Ex Officio
Bruce Laingen **Strobe Talbott**

The National Commission on the Public Service was initiated by the Brookings Institution Center for Public Service, which is directed by Paul C. Light. It is supported by a grant from the Dillon Fund. The Commission report and further information on the Commission and the many organizations and individuals that assisted it are at www.brookings.edu/Volcker.

Hannah S. Sistare
Executive Director, National Commission on the Public Service

Testimony for the Subcommittee on Civil Service and Agency Organization
Committee on Government Reform, U.S. House of Representatives
April 1, 2003

Chairman Davis, Congressman Davis and Members of the Committee, thank you for inviting the National Commission on the Public Service to testify at this hearing on compensation reform for federal employees, including the pay-for-performance recommendations made by the Commission. Commission Chairman Paul A. Volcker and the Commission Members appreciate this Subcommittee's interest in their findings and recommendations.

As the Commission Report says, "Proper adjustment of public service compensation is a conundrum as old as the Republic." Recognizing the important role of compensation in addressing the challenges facing the federal government, the Commission examined federal pay in all three branches and at all levels. It looked at the way federal pay is currently set, and considered the appropriateness of various non-governmental comparisons. In the end, the Commissioners developed some overarching principles that they believed should guide pay decisions and also addressed the issue in a series of recommendations.

Three principles are suggested by the Commission:

First, government pay must reflect current market conditions if government is to attract and retain the workforce it needs to perform its responsibilities.

Second, the relevant "market" for most of the federal workforce should be comparable jobs and abilities in the general workforce. The relevant "market" for government's senior leadership should be positions demanding comparable responsibility and capabilities in the non-profit workforce.

Third, pay should be tied to performance.

The Commission was aware that studies by the Congressional Budget Office[i], the Office of Personnel Management[ii] and private organizations show that pay disparity with the private sector is not uniform across all government positions. The recently released OPM 2002 Survey of Federal Employees indicates that 64% of federal civilian employees are "satisfied" with their pay, and 56% categorize it as "good." Yet 34% said they are considering leaving the federal service, and only half of that group is leaving to retire. And problems related to pay are well known: agencies have to be

given special pay authority to attract workers with specialized skills; pay compression has resulted in nearly 70% of the SES receiving the same pay; federal judges – whose appointments are for a lifetime – are resigning in growing numbers, with many citing continuing loss of buying power as the reason.

While pay is not the sole reason federal employees come to work, recent surveys conducted by Paul Light, Director of the Center for Public Service at the Brookings Institution, reveal it as a significant inducement. When asked, "Why do you come to work every day," 41% listed pay as their sole reason.[iii]

Although the Commissioners recommended that pay be based on market comparisons, they believed that different markets should be used, depending on the position. For the majority of federal workers, the private, for-profit sector was identified as the appropriate market. The Commission recommended that Congress establish policies that permit agencies to determine the specific relevant market for their employees and to adjust their compensation to its exigencies.

Concurrently, the Commissioners recommended that the existing classification system and the general schedule be terminated. As the Director of the Office of Personnel Management so clearly articulated in her White Paper on federal pay modernization, they were designed for a workforce that no longer exists. The Commission recommended that a "broad-band" system be adopted as the government's default system. In the alternative, an agency would adopt a system which best supported its own mission.

The Commission suggested a different compensation standard for senior government positions, such as federal judgeships, executives and members of Congress. There, the Commission looked toward comparable positions in the private non-profit sector as a guide. Associate Justice Stephen Breyer suggested this standard to the Commission when he testified in July of 2002. The Commission staff subsequently developed a comparison of executive pay for several categories of non-profit entities. These included universities as well as think tanks, labor unions, public interest groups and foundations of relatively significant size. In every case, the compensation of the leadership of these non-profit institutions was notably higher than that of the senior leadership of the federal government. I have included the resulting chart with this testimony for the Subcommittee's information.

Chief Justice William Rehnquist and Associate Justice Breyer took the unusual step of offering public testimony at the Commission's hearings last year. They, and leaders of the federal judiciary across the board, are deeply concerned about the effect of federal judicial pay stagnation on the administration of justice. They noted that between 1969 and 1999, real pay for federal trial court and appellate court judges declined by about 25%. During the same period of time, the real pay of the average American worker increased by 12.4%. I have provided the Subcommittee with copies of charts prepared

by the Administrative Office of the U.S. Courts that illustrate this data. The first shows this change in real pay between 1969 and 1999. The second is a depiction of comparative gains and losses in pay relative to inflation from 1994 and 2000 for selected categories of U.S. workers. It shows that every category gained relative to inflation, except for federal judges and members of Congress. The gain in national average wages was approximately 14%, while the decline for Member of Congress and Federal Judges was nearly 10%.

The value of the constitutional grant of a life term to the federal judiciary is undermined when judges feel they must leave the bench to sustain their income. As Justice Breyer noted, the framers deliberately connected judicial compensation and judicial independence. Chief Justice Rehnquist cited data collected by the Administrative Office of the United States Courts: More than 70 Article III judges left the bench between 1990 and May 2002, whereas during the 1960s, only a handful of Article III judges retired or resigned. When the Administrative Office informally surveyed judges who had recently left the bench, the need for additional compensation for items such as college tuition or living expenses in high-cost cities was repeatedly cited as the reason.

Another area where pay has been effectively capped is the Senior Executive Service. This cadre of senior executives was established to provide the government with a skilled leadership, without all the traditional civil service protections, but with the ability to be rewarded for excellent performance. As a result of SES pay being tied to Executive Level III pay, and the Executive Level pay effectively capped by Congressional pay, we have reached the point now where nearly 70% of the SES earns the same compensation. In his FY 2004 budget the President has recommended increasing the cap for the SES by raising the top SES pay to that of Executive Level II, which would provide some correction.

The Commission also addressed the compensation of political appointees. It recognized that theirs is a somewhat different case, in that they come into government for a relatively short period, often with personal wealth, and can later benefit from the prestige of having had a senior political position. However, they did not feel these were sufficient or even appropriate justification for pay that is substantially lower when compared with those with similar responsibilities, even in the non-profit sector.

Congress began the work of easing the cap on federal pay in 1999 when it raised the President's salary from $200,000 to $400,000 (P.L. 106-58). The Commission recommends that Congress immediately increase the pay of these other "capped" senior government officials, including federal judges and Members of Congress themselves. Should Congress not want to give itself this level of increase, the Commission asked it to de-couple its own pay from that of federal executives and judges. But I will repeat for the record the Commissioner's statement that: "Few democracies in the world expect so much from their national legislators for so little in compensation."

Two additional areas addressed by the Commission bear on the issue of compensation flexibility: First, is the importance of increased and careful oversight, by Congress and responsible executive branch leadership, to assure that the new system and personnel flexibilities stay on track. Concern is sometimes expressed that those in charge will abuse a system with flexibility. Careful and ongoing oversight, including statutory assurance of merit principles of government employment, can ease concerns and prevent that from occurring.

Second, and related, is the importance of ongoing training. Managers and executives who receive appropriate training throughout their careers are much more certain to be good managers and leaders. In fact the Commission believed that adequate and consistently funded training for all federal employees was of great importance. Training is certainly an area where penny wise is pound-foolish.

There is one point I want to note in describing the Commission's approach to these issues. As my testimony indicates, the Commission focused to a greater extent on the pay of top government officials than it did on the pay of the broad federal workforce. There were two important reasons for the emphasis on leadership pay. First, there is a demonstrable critical challenge to effective governance when the leadership of government is significantly underpaid. Second, executive level pay caps are currently a barrier to pay reform, including pay for performance, for the entire federal workforce.

On the issue of performance, the Commission's report repeatedly stresses the important role the Commissioners believe performance should play in the awarding of pay. The experience of the Senior Executive Service illustrates this, as well as my previous point: The SES was established in 1978 with a rewards and incentive system where compensation would be closely tied to performance. Those who performed at the highest levels were supposed to get bonuses and merit awards equal to a substantial portion of their annual pay. Unfortunately, the reward system has been inadequately funded and today, the pay cap has resulted in 70% of the SES receiving the identical pay.

Witnesses at the Commission hearings referred to the existing federal rewards system as "peanut butter." This is the name federal employees have given to the practice of spreading the funds available for performance rewards broadly across the workforce to make up for lagging base pay.

In addition to inadequate funding of awards, the pay cap and the peanut butter syndrome, a fourth barrier to utilizing existing performance incentives is the fact that like the residents of Lake Wobegon, everyone working for the federal government performs above average. In fact, the performance ratings of most of the federal workforces are in the superior category. Of the 700,000 employees who were rated in 2001 using a pass/fail system, 93% passed and just .06% failed. The rest were not rated. Of the 800,000 federal employees who were rated that

year using a five-point system, 43% were rated as "outstanding," 28% as "exceeds fully successful," 18% as "fully successful" and just 0.55% as either "minimally successful" or "unacceptable."[iv]

As a result of the fact that federal pay is not based on performance, and the reality that performance incentives now in law are ineffective, the vast majority of federal pay increases have no relationship to performance. In recommending adoption of pay systems which reward excellence in performance the Commission, led by Chairman Paul Volcker, would again stress the importance of oversight by both the leadership of the Executive Branch and the Congress to make sure the systems are implemented fairly and pursuant to the government's established merit principles.

Thank you again for inviting the National Commission on the Public Service to share its findings and recommendations with the Subcommittee.

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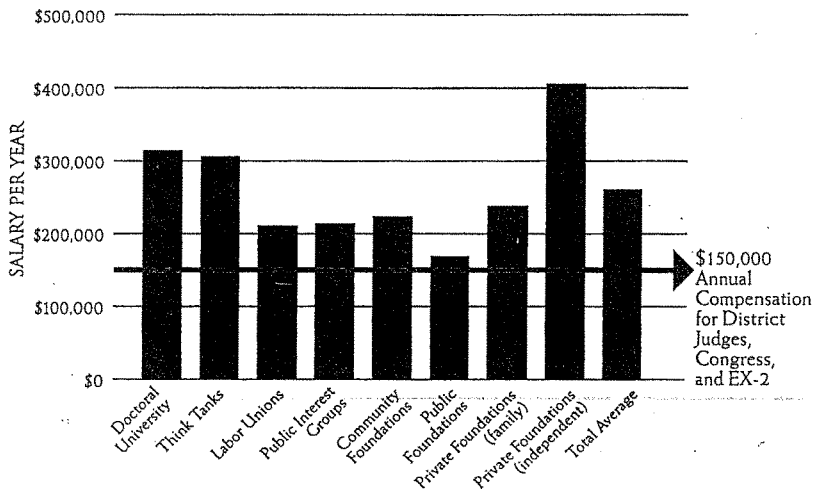
[i] Congressional Budget Office, *Summary of CBO's Work on Employee Pay and Benefits*, November 6, 2002

[ii] Office of Personnel Management, A *Fresh Start for Federal Pay: The Case for Modernization*, (OPM White Paper, April 2002

[iii] Paul C. Light, *The Troubled State of the Federal Public Service*, Washington: Brookings Institution, June 27, 2002, p.6

[iv] Ibid, p.20

EXECUTIVE PAY COMPARISON

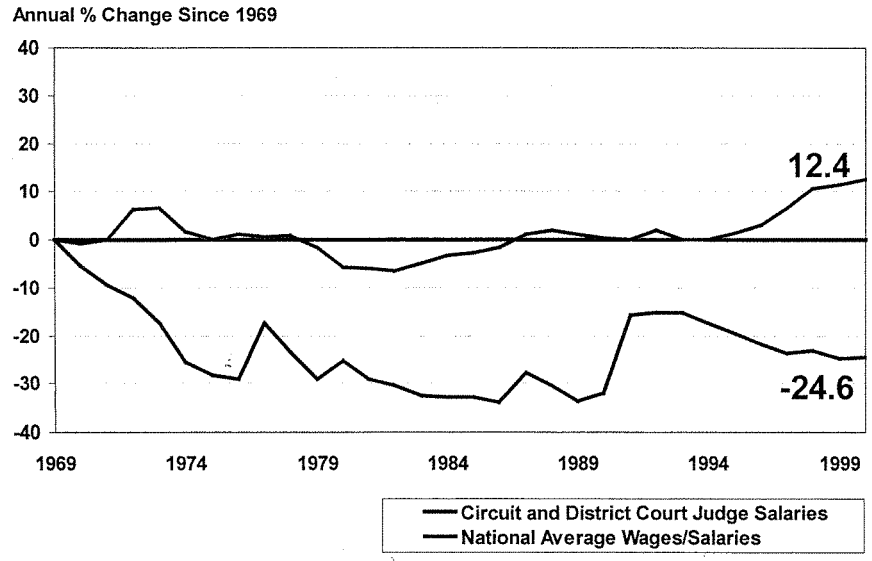


Doctoral university salaries taken from "The Chronicle of Higher Education." Think tank salaries represent those with ≥ $10M in assets, labor union salaries represent those with ≥ $100M in assets, public interest groups represent those with ≥ $10M in assets, community foundations represent those with ≥ $250M, public foundations represent those with ≥ $100M in assets, private foundations (family) represent those with ≥ $250M in assets, private foundations (independent) represent those with ≥ $1B in assets, and total average equals the average salary of an executive level officer from the above groups.

All other salaries are taken from the *National Journal*, March 30, 2002, pp 919-930.

CHART ONE

Decline in Salaries of Judges Compared to Private Sector Wage Gains, Adjusted for Inflation – From 1969 Through 2000

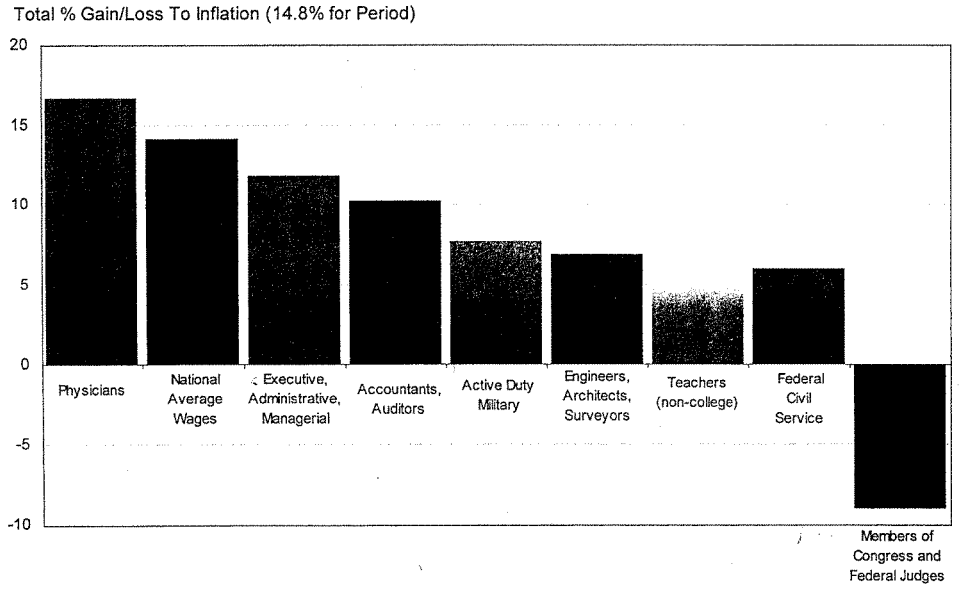


Data derived from the Congressional Research Service and the Bureau of Labor Statistics – Inflation Based on CPI-U Index

Prepared by: Administrative Office of the U.S. Courts

CHART TWO

Comparative Gains/Losses in Pay Relative to Inflation From 1994 to 2000



Data derived from the Bureau of Labor Statistics and the Congressional Research Service

Prepared by: Administrative Office of the U.S. Courts

Mrs. DAVIS OF VIRGINIA. Thank you, Ms. Sistare.

Mr. Blair, I was very pleased to see the thoughtful discussion of the compensation issues in the White Paper that you talked about that OPM issued last April. The White Paper seemed to indict the General Schedule. However, during the debate on Homeland Security Act of 2002, the administration argued that the Department needed the flexibility to abolish the General Schedule. Given that, why does the Human Capital Performance Fund proposal continue to use the General Schedule as the base for Federal employee compensation?

Mr. BLAIR. The Human Capital Performance Fund is really a downpayment on future reforms which we are still working on. The White Paper began this conversation and we are in the process of working with the stakeholders to identify and refine future solutions. The adoption of the proposal of the Human Capital Performance Fund will give incentives to our managers to begin making meaningful distinctions in employee performance. Further, Congress has shown tremendous interest in human capital issues including adoption of the Department of Homeland Security legislation, there was a recent CBO report on Federal compensation, the Volcker Commission recommendations and the like. So we are continuing the conversations and working to refine and propose solutions. Given that, we thought it was a good idea to put forth this idea of the Performance Fund as a meaningful downpayment on such reforms.

Mrs. DAVIS OF VIRGINIA. I continue to be very concerned and I think my colleague alluded to it, that the administration is continuing to be unwilling to ensure parity between the civilian work force and the military. The Human Capital Performance Fund proposal would fall short of parity except presumably for top performers who would need the extra money from the fund just to get parity.

How would OPM measure the results of the Human Capital Performance Fund approach to pay for performance? It seems to me without some clear, hardnosed criteria, we are unable to say one way or another whether the pay-for-performance has been a success. How are we going to do it?

Mr. BLAIR. Under the President's proposal, each agency will apply for a pro rata portion of the fund that would be appropriated to OPM. They will have to come up with specific criteria showing what kind of performance management system they intend to have in place and how they intend to reward performance. So on the front end, you have continual monitoring and oversight by the Office of Personnel Management.

In addition, the President's executive branch management scorecard rates and evaluate agencies on the way they handle the human capital performance. That is the scorecard reds, yellows and greens and OPM is the lead partner in scoring agencies on the human capital portion of that scorecard.

One of the things we take into account is how effective are the agencies performance management systems. So you are going to have continual monitoring and oversight over these management performance systems.

In addition, we expect visual oversight from Congress, GAO, the Inspectors General and a whole host of other bodies interested in

good governance. I think an effective framework for oversight would be established. Agencies will have to apply for this fund each year, so if an agency doesn't meet its obligations and commitment 1 year, it would be unlikely it would be approved the next.

In addition, agencies that would have particularly good incentive programs would be rewarded because approximately 10 percent of this $500 million fund will be held in reserve by OPM to reward agencies that come up with particularly good plans. So we really think we have a strong infrastructure in place to ensure effective management of the fund.

Mrs. DAVIS OF VIRGINIA. To qualify for the plan, would they have to have set specific guidelines so there wouldn't be what I think many of us are concerned about: bias toward an employee one way or the other by a manager?

Mr. BLAIR. I would anticipate that. I think the merit system principles would be at the heart of what we want to do here. That would ensure that this fund is administered in a fair and even-handed manner. We have no intention of doing otherwise.

Mrs. DAVIS OF VIRGINIA. Ms. Sistare, you recommended in your report eliminating the General Schedule for pay and creating six to eight broad bands with relatively wide salary ranges. Do you believe that pay banding without the presence of specific measurable performance standards would work as a concept and did the Commission, when they did the work, do any work on any performance measures?

Ms. SISTARE. The Commission would certainly say that it should be concurrent, that they would have to be done concurrently. If you are going to judge people on performance, you have to have adequate and reliable measures.

Mrs. DAVIS OF VIRGINIA. So we can't just go out there and change the system without everything in place.

Ms. SISTARE. The Commission regarded its recommendations, in some cases, as with the reorganization proposals, as being the work of many years. But they felt the work should begin.

Mrs. DAVIS OF VIRGINIA. Do you propose, and how do you propose, that we get Federal employees to buy into the pay banding because I know we have some that are very nervous about it and very concerned. How do we convince them it is a good idea?

Ms. SISTARE. There are concerns that have been raised about pay banding and performance measurements generally. The Commission felt that if you have adequate oversight both by Congress and the executive branch, training of the people making the judgments, and adequate funding for whatever reward system there is and the training, that should not only allay concerns but should deal with any problems.

Mrs. DAVIS OF VIRGINIA. I see my time is up, so I am going to ask our ranking member, Mr. Davis, do you have questions?

Mr. DAVIS OF ILLINOIS. Thank you very much, Madam Chairwoman.

Let me thank both of you for your testimony.

Mr. Blair, the GAO has stated that Federal agencies should demonstrate that they have modern, effective and credible performance management systems in place before additional pay reform flexibilities are implemented. In your opinion, do Federal agencies have

credible performance management systems in place? If so, which agencies would you highlight?

Mr. BLAIR. I would have to get back to you as to which agencies to highlight but we do have some that do have good performance management systems in place. That said, you bring a very salient point. We have to have good performance measures in place before this is effective and right now, there are no incentives for agencies to have those in place because our pay systems don't really recognize good performance. Until you have a system which provides agency managers and agencies the kinds of incentives it needs to reward your performance, it is going to be hard to get those in place.

Mr. DAVIS OF ILLINOIS. You were here when Representative Ruppersberger testified. Would you see gainsharing having any place in that role in government?

Mr. BLAIR. It is my understanding agencies have the authority now to do gainsharing, so I think what Representative Ruppersberger pointed out was an interesting system and I think there is a lot the government could learn from it.

Mr. DAVIS OF ILLINOIS. Let me ask Ms. Sistare, you have indicated that the existing classification system should be changed, terminated actually, and that the Federal agencies should adopt pay systems that support their respective missions. What impact would this have on the ability of individuals to transfer say from one agency to another, and would it affect their compensation?

Ms. SISTARE. The Commission certainly believed that government could benefit if the path between agencies were more open to employees. I would see the transferring employee going into the new agency and being considered on the basis of that agency's system, just as people going between one business and another in the private sector are then dealing with whatever pay system exists with that new employer.

Mr. DAVIS OF ILLINOIS. So then it would be possible that if one had an opportunity to transfer, they may also have to look at a change in compensation that would not necessarily be an upgrade for them?

Ms. SISTARE. That is true, although it could be the opposite. Maybe I should make one point, which is the Commission definitely felt there should be and would be always a core government work force that would most likely who were career employees, full career, and that people in that work force doing what Paul Volcker calls the core competencies of government would probably have the broadbanding system and would be in many ways alike. So it would be less of an issue there for somebody transferring from one to the other.

Mr. DAVIS OF ILLINOIS. I gather from your testimony that you are really excited about the way we evaluate performance. What criteria would you suggest?

Ms. SISTARE. The results would indicate that it is not really an evaluation process. As you say, maybe the problem is that the criteria aren't there. If a manager or supervisor or an agency doesn't have reliable performance criteria, it is pretty hard to rate people on a spectrum. Also, the law prevents managers from rating on a

curve and really doesn't support them when they do try to make distinctions.

Mr. DAVIS OF ILLINOIS. So you are suggesting that it is fairly subjective. It appears to be fairly subjective right now?

Ms. SISTARE. I believe so.

Mr. DAVIS OF ILLINOIS. Thank you.

Mrs. DAVIS OF VIRGINIA. Thank you, Mr. Davis.

Ms. Blackburn. If the gentlewoman would yield for a moment, I would like to take a second of her time.

Tying into what Mr. Davis said when he was talking about someone transferring from one department to another, would you be suggesting that there be a one-size-fits-all compensation system throughout the Federal Government so that one could transfer or are you suggesting we do something different in each agency?

Ms. SISTARE. No, the Commission was clear they felt the agencies should adopt the systems that best fit their missions and needs but they did believe that many would adopt the pay-banding system and that since they expected OPM would assist in setting up these systems, there would probably be a fair number of agencies that had similar pay systems.

Mrs. DAVIS OF VIRGINIA. Thank you, and thank you, Ms. Blackburn, for yielding to me.

Ms. Norton.

Ms. NORTON. Thank you, Madam Chair.

I appreciate what you are trying to do because what we are dealing with here is the largest employer in the country and yet a mandate to make sure the merit system principles apply and if we didn't have that, we would be back to before the Civil Service system. We do need to study our history to understand how we got to this system in the first place with all of its rigidities as we try to modernize it.

From both your testimonies, I got the impression that I was dealing with a pig in a poke because I couldn't put my finger on how it would work, in part because you obviously are in the beginning stages and I have some appreciation for what you are going through. I chaired the Equal Employment Opportunities Commission and at a time when it had to go through a wholesale reform of the entire agency, this is very difficult.

Choosing one part of the system first does seem to me to be the way to go as opposed to throwing the stuff up and seeing what you can do with the whole system. Yet, you have chosen a part of the system, the SES, which I am left to wonder how much it has to teach up and down the line.

For example, in your testimony, Mr. Blair, you say the administration's SES pay proposal would eliminate the fixed pay levels within the current SES system in favor of an open pay range with a higher pay gap, would be able to make meaningful distinctions in pay based on each individual executive's performance and contribution to the agency's mission and goals.

One of the reasons we have a Civil Service system that is so clumsy is because that is so difficult, to distinguish between a whole bunch of people that may be doing the same or similar work. You said in response to the Chair's question that merit system principles would apply. It would help me a lot if you would give me

at least an example. You would be more compelling in your testimony if you would say, and here is how it would work with respect to even the smallest example.

Throughout this testimony and your testimony too, Ms. Sistare, I cannot find examples to inform my judgment. I am being asked, I guess, to trust you and the history of how we got to the Civil Service system makes me unwilling to trust anybody unless they are willing to lay out how the system would work. So you would help me a lot if you would give me an example of how this would work for somebody in SES with a broad range and yet merit system principles would apply.

Mr. BLAIR. I always like to say trust us but verify, so we will help you on that verification process.

First, with SES, keep in mind where we are coming from on this. We have pay compression of somewhere between 60 and 70 percent SESers are all paid the same. The reason for that is it has been linked to congressional pay and Congress has denied itself pay raises over the course of the past decade and beyond a multitude of times.

In order to justify moving up that pay cap, we want to say we are not going to be giving any across-the-board pay raises to Senior Executive Service members; that the pay raises that will be afforded them, if you are going to increase within the pay range, the pay range will now be, locality pay, Executive Level 2 which is a Cabinet level Secretary salary or Deputy of approximately $154,000, it is going to have to be based on performance.

Right now, SESers are evaluated on a yearly basis and we need to do more on that evaluation. In 2001, 83 percent got the highest rating possible. Some argued that those ratings are a sign of agencies trying to get around the pay compression cap. That said, I think that we do already monitor SES performance. I know in OPM, a relatively small agency, the Director walks through with each and every Senior Executive Service member their performance evaluation.

Ms. NORTON. Is that an example of a merit principle? My question was how do merit principles apply to this individualized pay for performance system that you would put in place?

Mr. BLAIR. We could identify the merit system principles that you are paying fairly, you are recognizing good work, that you are paying by work for equal work for equal value and also aligning the work with the performance of the agency. I think that meets the heart of the merit system principles.

Ms. NORTON. It may well. Let me conclude by saying it all sounds terribly subjective to me in the hands of an individual. Again, this is how we got the system in the first place because it produces all kinds of reactions from people who say how did you reach that conclusion. I think you have a lot of work to do. I think your work is easier, this I will grant you, much easier with SES, much easier the higher up you get.

In your testimony, you say if we cannot demonstrate the value of a performance oriented pay system for our senior executives, how can we expect to foster development of performance oriented pay systems for the rest of the Federal work force and you suggest again, this is some kind of precedent for the rest of the Federal

work force on page 6 when you say, the one-size-for-all pay system doesn't work for senior executives any better than it works for other employees and we are eager to show that a performance oriented pay system can work for senior executives.

I would just like to ask you as you try to figure out how to do this for people at the very top for whom it seems a case can be made for at least the merit system principles being applied for some really open-ended way to pay, I would caution you against believing this is a model for how to deal with what is 2 million people who work in the Federal work force. I think that shows a lack of appreciation for how we got to this system in the first place.

Mr. Ruppersberger talked about morale. The notion of saying to managers in the workplace, hey, we are going to do what we did in the SES, we are going to go to an individualized system, using your language, of judging every employee. All I can say to that, Mr. Blair, is good luck.

Mrs. DAVIS OF VIRGINIA. I thank the gentlewoman. Your time has expired and we have several more panels, so I am going to go on to Mr. Murphy.

Mr. MURPHY. Thank you, Madam Chairman.

I have been trying to go through these reports and figure out some sense and having been an employer myself, I know how difficult it is to evaluate performance. How do you do it? Forget all the jargon. I don't want to hear about performance standards. I want to hear exactly how you do it?

Mr. BLAIR. We go through and evaluate employees.

Mr. MURPHY. Who fills that out?

Mr. BLAIR. The manager or supervisor.

Mr. MURPHY. And where does that data come from?

Mr. BLAIR. From an employee's performance plan on an annual basis.

Mr. MURPHY. So the employer and employee work out that performance plan?

Mr. BLAIR. It is mainly done by the manager or supervisor but with input from the employee.

Mr. MURPHY. Who makes a determination if those things have been met? Is that discussed between the employer and employee, are there outside sources?

Mr. BLAIR. It is done by the manager.

Mr. MURPHY. So it depends how closely the manager is monitoring that person's job. Are there any outside sources? A lot of Federal employees interface with the public. Is there any way of getting information from the public on their satisfaction?

Mr. BLAIR. I believe that might be part of the individual's plan. It would be on an individual basis. I would have to get back to you as to what those look like. I think the point is for the individual employee, we do set up specific performance plans for them.

Mr. MURPHY. I am not closer to the truth of what is going on here. I don't think you are being difficult, I am just trying to understand because these things can be very, very difficult to do and if one doesn't do them right, the whole thing from top down ends up to be a mess.

I know we are all in a performance rated every 2 years for better or worse, reality or fantasy. Whatever it is, we have that and we

have to lay those things out. It is a matter that for employees, many times people talk in not very glowing terms about any government employees. They refer in negative terms to bureaucrats and so forth and many politicians say they are going to cut through red tape and deal with bureaucrats. We wouldn't say that, it would be challengers who would say those things.

Many times we know the value of people working in these aspects but what I am concerning about is how we can get outside information that benefits that employee because I think they always do better if they know an accurate and fair information of how they are doing. How do we get that information? Is there any system set up to do that?

Mr. BLAIR. I don't think we want to have a one-size-fits-all for government. I think it is going to have to be tailor made for each individual agency and even subcomponents within the agency. We want to evaluate that plan and the agency needs to evaluate that plan and make sure they aligned with the mission goals and objectives. I am looking at it from kind of the 30,000 foot level at this point but we want to make sure employees know what is expected of them, know how they are being judged, that performance evaluation always carries with it an element of subjectivity. I think we need to recognize that and put it out on the table but subjective judgments are not inherently unreliable. They just have to be done openly and transparently and done with objective, definable results. That is what we want to make sure we have on the table for employees when we are going to be basing a system or part of their compensation system on performance based plans.

Mr. MURPHY. I would hope in pursuit of this, those guidelines would be fairly objective in terms of what employers are doing because even management needs help in understanding how to do those. Many times the problem occurs because a manager has not clearly stated guidelines. It is unfortunate if the only time that manager sits down with the employee to discuss problems is at the time of their annual review. That is a major flaw with management. They should have done so several times up to that point. I assume we are doing work on that too?

Mr. BLAIR. I agree with you. I think when you do have a problem employee, it shows a failure not just on the part of the employee but on the part of management. This is something employees and managers and the supervisor and the managers' managers need to have constant interaction.

Let us look at what we are up against. We have approximately a payroll of $133 billion a year. That includes paying benefits. Pay can be a very strategic tool in the management's arsenal so to speak but we have neutralized that tool because very little of our pay is performance based.

We gave a 4.1 percent across the board increase last year, it cost well over $5 billion. We have longevity of what we call within-grade step increases of 3 percent a year which up to one-third to one-half employees are eligible for, with only a small component of performance as a part of that. You have to ask, "is that an effective way to manage that much money?"

What we are trying to do, and I think most people agree, that we need to do a better job of rewarding performance. The recent

Federal Human Capital Survey results that OPM released last week, and I believe the Chair referenced this in her statement today, said that most employees, 63 percent, felt good about their pay, were satisfied with their pay.

Interestingly, fewer than half said that pay rewards good performance. We need to do a better job on that. That is what the President's proposal attempts to do, introduce an element of pay-for-performance through the Human Capital Performance Fund.

Mr. MURPHY. I don't disagree with the concept. It can have some fine results provided it does that and provides a fair and clear mechanism for employees to do that. I think that is what employees want. When you have people not satisfied with their job, oftentimes they just want more pay to make up for their own problems with it. I hope these things continue to develop and you can clear it up.

Mrs. DAVIS OF VIRGINIA. Thank you, Mr. Murphy.

Mr. Van Hollen.

Mr. VAN HOLLEN. Thank you, Madam Chairman.

First, a general comment. My colleagues may have already made this point which is, this may be received less suspiciously by many employee groups if you dealt with the pay parity issue. In other words, if people felt they were getting their fair pay increases like the civilian side of the work force with respect to comparison with the other side of the work force as opposed to this incentive pay being carved out of moneys that would otherwise be part of the general pay increase, I think obviously you would get a better reception.

I have a couple questions to followup on what Congressman Murphy and others have asked which really gets to the nub of the issue which is people feeling comfortable that you have a performance plan in place that really measures the individual's performance on a merit basis as opposed to all these extraneous and subjective factors.

I would be very interested and maybe you could supply the committee and you mentioned you have performance plans already in place to provide an analysis of employees. If you could provide the subcommittee with a sort of cross section across various departments, the Departments of State, Defense and the others of the type of performance plans currently there because on the one hand, you say they are already in place and on the other hand, they seem to be giving you results you are not happy with, a kind of bunching of results, so I would be curious if we could get some sense. It is hard to put your hands on this stuff, so if we could get our hands on some stuff you have been using, that would be helpful to me anyway.

Mr. BLAIR. We would be happy to provide that.

Mr. VAN HOLLEN. Thank you. Second, Congressman Ruppersberger was here and talked about gainsharing. In that case, you could see measurable results. It obviously applies more clearly to things where the government is performing a service. He mentioned mowing the grass or providing a particular concrete service where you can measure the cost to the government and determine whether or not that service is being delivered at less or more cost.

I wonder if that is not a better approach. What he is saying is we are going to identify a distinct area of government services, determine how much it is costing us today to provide those services, then we are going to say to the employees, if you provide those services at less cost, you will share somewhat in the benefits and the taxpayers will share in the benefits. It is much easier to identify, I actually think it may be harder to identify things in your Executive Service than things in other areas of government where you may be delivering specific services. I wonder if you could comment on that.

Give us examples. You said gainsharing is allowed in the Federal Government. Give me some examples of where it is in use now and how it is working.

Mr. BLAIR. I would have to get back with you on that. I didn't have the benefit of his statement before I came here, so we would be pleased to provide that for the record.

[The information referred to follows:]

Group Incentive Programs

- Tobyhanna Army Depot
- The United States Mint
- Western Area Power Administration (Department of Energy)
- Veterans Affairs Health Network
- Ann Arbor Healthcare System (Department of Veterans Affairs)

Group Incentive Programs in Federal Agencies

Tobyhanna Army Depot

The Tobyhanna Army Depot overhauls and repairs communications and electronic equipment for the military. There are approximately 2,500 non-SES Depot employees. The Rewarding the Workforce Award, established in 1995, shares the Depot's revenues, determined by its year-end Net Operating Result (NOR), equally among all eligible employees. The NOR is the Depot's primary business performance measure. It reflects the Depot's financial position at the end of the fiscal year after salary, benefits, materials, utilities, and other operating and administrative expenses have been subtracted from its revenue. The award payout system is based on a sliding scale starting at $300 and increased in $100 increments to a maximum of $1,000 per eligible employee. The first two-thirds of the total payout go to the Government, and the final one-third is distributed among the Depot's employees. Individual employee performance contributes to the Depot's overall performance which, in turn, determines whether employees receive an award payout and the amount of the award.

The United States Mint

The United States Mint Gainsharing Program established in 2001 ties award payments to improvements in workforce productivity. Approximately 2, 800 employees are involved in this program. On a quarterly basis, the Mint determines whether its workforce productivity has increased, as reflected by predetermined criteria, such as cost per coin, sales, and customer satisfaction ratings. If so, each employee receives a payout directly proportionate to the size of the quarterly gain.

Western Area Power Administration

The Western Area Power Administration (WAPA), a component of the Department of Energy, developed a program in 1995 to recognize employee contributions towards achieving organizational goals: customer service and reliability, cost containment, and safety. The program recognizes and awards employees for their annual contribution towards achieving the agency's goals. The goals become progressively harder to achieve each year. In FY 2001, if employees achieved 100% of the goals, awards per employee included $500 for safety-related achievements, $350 for achieving reliability and $350 for cost-containment, plus a $300 bonus to recognize a 100% level of success. For 50% of goal achievement, half of the cash award was distributed. Monthly updates on the WAPA intranet website keep employees abreast of their progress. The program helps WAPA reach its goals of customer service and reliability, cost containment, and safety.

Veterans Affairs Health Network

In 1995 the Veterans Affairs Health Network of Upstate New York created a goalsharing program in response to feedback about poor customer service. Motivated by lower than average ratings on the VA National Customer Service Survey, a management and labor partnership established a special reward system to support employee performance linked to organizational goals. The goals, established each year by employee work groups, focus on quality health care, customer service, and cost-effectiveness. When the VA Network reaches the annual goals it sets, every permanent employee member of the Network receives a monetary award. Since the program's inception, patient costs have been reduced by $1000 per patient, patient enrollment increased by 16% above the national average, and the organization moved to tie for first place on the VA National Customer Service Survey.

Ann Arbor Healthcare System

The Ann Arbor Healthcare System, a division of the Department of Veterans Affairs, implemented a program in 1998 to award healthcare and support personnel for their team-based work that achieves strategic goals and improves performance. Employees create cross-departmental teams to establish goals that meet strategic initiatives and results-oriented performance measures. The goals are pre-approved by management to ensure work is directed towards high priority areas. Additionally, a published monetary awards system lists amounts distributed upon achievement of goals. Agencywide participation is measured by tracking awards distribution by job category. For the current year, 110 teams involving more than 810 employees have been authorized to pursue team goals. Seventy teams have completed their work and received incentive awards totaling more than $168,000. Results of the program include tangible savings of more than $2.6 million, as well as considerable improvements to patient care and support processes.

Mr. BLAIR. One of the instances you just described would really work well under the President's proposal for the Performance Fund. For instance, say you have an employee with no chance of promotion at this point but they are doing an outstanding job. Say they identify some procurement savings that can save an agency $2-$3 million a year. Under current rules, we can reward that employee a one-time bonus of $5,000 for the identification and for that good work, but that is not built into his or her base salary and doesn't go toward retirement.

Under the Human Capital Performance Fund, an agency presumably could submit a plan to recognize that kind of productivity and give that employee an award increasing his or her salary by $5,000 a year. That would be built into their base pay, be recognized for retirement purposes and that person would be able to keep it in future years rather than just see it as a one-time bonus or one-time shot.

I am glad to see the committee members' interest in this because we really need to do a better job of honing our systems in order to encourage better performance. When we have a pay system that doesn't do that, it really puts us out of whack and pay is one of the most strategic tools we have. If we can't use that to spur better performance, I am not sure what else we have.

Mr. VAN HOLLEN. Briefly to followup, you are right. The procurement, that is an example where someone's creativity may be able to identify cost savings but there are so many areas in the Federal Government where there is not that kind of direct link to an easy measure of productivity, not like a salesman out there selling widgets.

For example, someone at the State Department or the CIA who is analyzing the situation in Iraq or any other place in the world, coming up with a clear performance standard for how you measure success is what I am having trouble getting my hands on and what is the basic concern of employees with respect to the fairness. There are some things that lend themselves more easily to measuring success and maybe we should focus on those areas on a trial basis or pilot basis rather than trying to do it all at once.

Thank you, Madam Chairman.

Mrs. DAVIS OF VIRGINIA. Thank you, Mr. Van Hollen.

If you all will bear with me, I have one more question because it has been brought up a couple of times. You alluded to it a moment ago, Mr. Blair. The OPM survey showed that nearly two-thirds of the Federal workers were very satisfied with their pay but also revealed that 35 percent were considering leaving their jobs. To me doesn't this indicate that maybe pay is not the source of job satisfaction and maybe we should not be looking at pay reform as reform right now?

Mr. BLAIR. Let me take two stabs at that question. First, I think 35 percent that may be thinking about leaving their jobs may have also included those who are thinking about leaving for retirement purposes. Say even if everyone is satisfied with their job, I think we still need to take a look at how we pay employees.

We have a 50-year-old system that has been amended over the years. The last time it was substantially amended was in 1993 but we do not have performance as a key component in the way we re-

ward our employees. That is the right thing to do. So even if everyone is satisfied with their pay, it still doesn't mean we shouldn't be looking at finetuning and reforming the ways we pay our employees.

Mrs. DAVIS OF VIRGINIA. I think you can see that the members of the committee are possibly interested in this but also very cautious and wary because we don't want to, at least I as the Chair, am not real crazy about going into something and making more of a mess of the system than we might have at the moment.

I look forward to hearing some things back from both of you and I agree, we do probably need to look at some type of change but we want to make sure it is the right change.

Mr. Davis.

Mr. DAVIS OF ILLINOIS. I would like to make sure we all get the information he is going to provide for Mr. Van Hollen.

Mrs. DAVIS OF VIRGINIA. We will make sure when he gets it to the committee, Mr. Davis, that we get to all the members of the subcommittee.

We thank you both for taking time to come and appreciate everything you had to share with us.

If the third panel would come forward. We are going to administer the oath, if you will stand. It is the subcommittee's standard of practice to ask witnesses to testify under oath, so if you will raise your right hands.

[Witnesses sworn.]

Mrs. DAVIS OF VIRGINIA. The witnesses will be recognized for opening statements. We will ask you, as we did the previous panel, to summarize your testimony in 5 minutes and your written statement will be made a part of the record.

I would like to welcome Christopher J. Mihm, Director, Strategic Issues, U.S. General Accounting Office; Max Stier, president and CEO, Partnership for Public Service; and George Nesterczuk, consultant to the Heritage Foundation. Thank you all for being with us today. Mr. Mihm, we will recognize you for 5 minutes.

STATEMENTS OF CHRISTOPHER J. MIHM, DIRECTOR, STRATEGIC ISSUES, U.S. GENERAL ACCOUNTING OFFICE; MAX STIER, PRESIDENT AND CEO, PARTNERSHIP FOR PUBLIC SERVICE; AND GEORGE NESTERCZUK, PRESIDENT, NESTERCZUK AND ASSOCIATES AND CONSULTANT, HERITAGE FOUNDATION

Mr. MIHM. Thank you very much, Chairwoman Davis and Mr. Davis. It is a great honor and pleasure to be here today to testify on results oriented pay reform.

Mr. Davis, I think as you noted in quoting from the Controller General in your opening statement, my major point today is that in order to have effective pay for performance reforms, agencies must have modern, credible and validated performance management systems that are capable of supporting pay and other personnel decisions. Quite simply, pay for performance works only when adequate safeguards including reasonable transparency and appropriate accountability mechanisms are in place.

I would agree with the spirit of what Mr. Blair and Ms. Sistare were saying that modern performance management systems are the centerpiece of those safeguards.

Unfortunately, as you also noted, Mr. Davis, we have quite a way to go with many agencies. The chairwoman quoted in her opening statement from the OPM Governmentwide Survey that suggested the credibility is certainly a problem with the current Federal performance management system. Part of the problem is that executive agencies performance management systems are based on episodic and paper intensive exercises that are not linked to the strategic plans or program goals of the organization. They often have only a modest influence on the pay, use, deployment and promotions of Federal employees.

Leading organizations, on the other hand, use their performance management systems to accelerate change, achieve desired results and to facilitate two-way communication throughout the year so that discussions about individual and organizational performance are integrated and ongoing.

This gets to exactly the point Mr. Murphy raised in his questioning of the last panel. That is, these organizations use their performance management systems not so much as merely once or twice a year just individual expectation setting or rating processes but they are actually used as tools within the organization to manage it on a day to day basis and achieve results that citizens care about.

Chairwoman Davis, today you are releasing a report that we prepared at your and Senator Voinovich's request that shows some of the specific practices that leading public sector organizations here in the United States as well as around the world have used in their performance management systems to create clear alignment between organizational goals and individual day to day activities. It is the so-called line of sight.

Our suggestion would be that Federal agencies consider these practices as they modernize their performance management systems to better ensure that their daily activities are contributing to results. Our hope is that this report, and other work we will certainly make available to the subcommittee, will begin to provide some of the examples that Mr. Murphy and Ms. Norton were asking about, very concrete examples of where organizations are able to achieve this alignment while still adhering to merit principles.

As all the conversation thus far has made clear, we need to continue to experiment with providing agencies with the flexibility to pilot approaches, to setting pay and linking pay to performance. We believe that agencies should be required to demonstrate they have modern performance management systems in place before they are allowed to implement the pay for performance initiatives. This is consistent with the approach Congress took with raising the total amount of annual compensation for senior executives as part of the Homeland Security Act.

The Congress may also want to consider providing guidance on the criteria that OPM should use in making judgments about individual agencies' performance management systems if Congress decides to go forward with the performance fund or other pay for performance initiatives. We believe that the practice as detailed in the

report being released today provides the starting point for that consideration.

In summary, there is widespread agreement that the basic approach to setting Federal pay is broken and we need to move to more market and performance based approach. Doing so will be essential if we want to really maximize the performance of government. However, while reasonable people can and will debate and disagree about the merits of individual reform proposals, we believe that all people should be able to agree that a performance management system with appropriate safeguards must be in place and serve as the fundamental underpinning of any fair, effective and appropriate results oriented pay reform.

The practices used by leading organizations in developing and using their performance management systems to link organizational goals to individual performance and create this vital line of sight between individual activities and organizational results, we believe show the way in how to implement performance management systems with the necessary attributes.

Chairwoman Davis and Mr. Davis, this concludes my statement. I will be happy to take any questions you may have.

[The prepared statement of Mr. Mihm follows:]

United States General Accounting Office

GAO

Testimony

Before the Subcommittee on Civil Service and Agency Organization, Committee on Government Reform, House of Representatives

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RESULTS-ORIENTED CULTURES

Modern Performance Management Systems Are Needed to Effectively Support Pay for Performance

Statement of J. Christopher Mihm
Director, Strategic Issues



GAO-03-612T

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Highlights

Highlights of GAO-03-612T, testimony before the Subcommittee on Civil Service and Agency Organization, Committee on Government Reform, House of Representatives

RESULTS-ORIENTED CULTURES

Modern Performance Management Systems Are Needed to Effectively Support Pay for Performance

Why GAO Did This Study

There is widespread agreement that the basic approach to federal pay is broken and that it needs to be more market- and performance-based. Doing so will be essential if the federal government is to maximize its performance and assure accountability for the benefit of the American people. While there will be debate and disagreement about the merits of individual reform proposals, all should be able to agree that a performance management system with adequate safeguards, including reasonable transparency and appropriate accountability mechanisms in place, must serve as the fundamental underpinning of any fair, effective, and appropriate pay reform.

At the request of the Subcommittee, GAO discussed the key practices for effective performance management that federal agencies should consider as they develop and implement performance management systems as part of any pay reform.

What GAO Found

The need for results-oriented pay reform is one of the most pressing human capital issues facing the federal government today. To implement results-oriented pay reform, commonly referred to as "pay for performance," agencies must have modern, effective, credible, and validated performance management systems that are capable of supporting pay and other personnel decisions. Pay for performance works only with adequate safeguards, including reasonable transparency and appropriate accountability mechanisms in place, to ensure its fair, effective, and responsible implementation. Modern performance management systems are the centerpiece of those safeguards and accountability.

Most federal agencies are a long way from meeting this test. All too often, agencies' performance management systems are based on episodic and paper intensive exercises that are not linked to the strategic plan of the organization and have only a modest impact on the pay, use, development, and promotion potential of federal workers. Leading organizations, on the other hand, use their performance management systems to accelerate change, achieve desired organizational results, and facilitate two-way communication throughout the year so that discussions about individual and organizational performance are integrated and ongoing. Effective performance management systems are not merely used for once- or twice-yearly individual expectation setting and ratings processes, but are tools to help the organization manage on a day-to-day basis.

GAO identified key practices leading public sector organizations both here in the United States and abroad have used in their performance management systems to link organizational goals to individual performance and create a "line of sight" between an individual's activities and organizational results. These practices can help agencies develop and implement performance management systems with the attributes necessary to effectively support pay for performance.

www.gao.gov/cgi-bin/getrpt?GAO-03-612T.

To view the full testimony statement, click on the link above. For more information, contact J. Christopher Mihm at (202) 512-6806 or mihmj@gao.gov.

Madam Chairwoman and Members of the Subcommittee:

I am pleased to be here today to discuss the need for results-oriented pay reform, one of the most pressing human capital issues currently facing the federal government. My major point today is that, as Comptroller General Walker has said, in order to implement such reforms, commonly referred to as "pay for performance," agencies must have modern, effective, credible, and validated performance management systems that are capable of supporting pay and other personnel decisions. Quite simply, pay for performance works only with adequate safeguards, including reasonable transparency and appropriate accountability mechanisms in place, to ensure its fair, effective, and responsible implementation. Modern performance management systems are the centerpiece of those safeguards and accountability.

Unfortunately, most federal agencies are a long way from meeting this test. All too often, we find that agencies' performance management systems are based on episodic and paper-intensive exercises that are not linked to the strategic plans of the organizations and have only a modest impact on the pay, use, development, and promotion potential of federal workers. Leading organizations, on the other hand, use their performance management systems to accelerate change, achieve desired organizational results, and facilitate two-way communication throughout the year so that discussions about individual and organizational performance are integrated and ongoing. Effective performance management systems are not merely used for once- or twice-yearly individual expectation setting and ratings processes, but are tools to help the organization manage on a day-to-day basis. Chairwoman Davis, today you are releasing a report that we prepared at your and Senator Voinovich's request that shows specific practices that leading public sector organizations here in the United States and abroad have used in their performance management systems to create clear linkages between individual performance and organizational success.[1]

There can be little question that modernizing agency performance management systems and linking them to agency strategic plans and desired outcomes should be a top priority. The Office of Personnel

[1]U.S. General Accounting Office, *Results-Oriented Cultures: Creating a Clear Linkage between Individual Performance and Organizational Success*, GAO-03-488 (Washington, D.C.: Mar. 14, 2003).

Management's (OPM) recently released 2002 Federal Human Capital Survey found that better performance management systems are needed in federal agencies. The results show that while 80 percent of federal employees believe they are held accountable for results, most are not satisfied with the recognition or the rewards they receive for a job well done. Specifically, less than half of employees believe that the awards in their work units depend on how well employees perform their jobs and less than a third of employees believe that their organizations' awards programs provide them with an incentive to do their best. Also, less than a third of employees agree that steps are taken to deal with poor performers.

These results appear to reinforce the findings from OPM's white paper on modernizing federal pay issued in April 2002.[2] The paper described the need for the federal pay system to be more performance-oriented, flexible, and market-sensitive as well as a better tool for improving strategic human capital management. It amply demonstrated that the current federal pay system was designed for the heavily clerical and low graded workforce of the 1950s rather than today's knowledge-based government. Similarly, OPM's survey results underscore the findings of the National Commission on the Public Service's recent report, *Urgent Business for America: Revitalizing the Federal Government for the 21st Century.* The commission observed that agencies need greater freedom to connect pay both to the market and to performance. As the nature of the federal workforce has changed, so too should its pay system if we are to effectively compete for top talent and create incentives for both individual and institutional success.

The Congress and the administration are working on initial steps to implement result-oriented pay reform and modern performance management systems across the executive branch.

- The Homeland Security Act of 2002, passed by the Congress in November, provides for the increase of the total annual compensation limit for senior executives (from $171,900 to $198,600 for 2003) in those agencies that OPM and the Office of Management and Budget certify as having performance appraisal systems that, as designed and applied, make meaningful distinctions based on relative performance.

[2]Office of Personnel Management, *A White Paper: A Fresh Start for Federal Pay: The Case for Modernization* (Washington, D.C.: April 2002).

- The administration proposed for the fiscal year 2004 budget to allow managers to increase pay beyond annual raises for high-performing employees. OPM would administer a $500 million Human Capital Performance Fund for the purpose of allowing agencies to deliver additional pay to certain employees based on individual performance or other human capital needs, in accordance with plans submitted to and approved by OPM.

- In addition, in the fiscal year 2004 budget proposal, the administration proposed the creation of a wider, more open pay range for senior executive compensation, thus allowing for pay to be more directly tied to performance. This is consistent with the proposals you and Senator Voinovich are considering.

Today, I will highlight the key practices for effective performance management that federal agencies should consider as they revise their performance management systems to be more results-oriented, customer-focused, and collaborative in nature. These practices are fully discussed in the report that you are releasing today. Next, I will discuss what selected federal agencies have done to implement results-oriented pay reforms, including how we in GAO are implementing a broadbanded pay for performance system as part of our performance management system. Last, I will suggest next steps for results-oriented pay reform for all interested parties as they work together to better link pay to performance.

Key Practices for Effective Performance Management

We identified specific practices that leading public sector organizations both here in the United States and abroad have used in their performance management systems to create a clear linkage—"line of sight"—between individual performance and organizational success. Federal agencies should consider these practices as they develop and implement the modern, effective, and credible performance management systems with the adequate safeguards, including reasonable transparency and appropriate accountability mechanisms in place, needed to effectively link pay to performance. The key practices include the following.[3]

[3]We included the agency examples supporting the key practices primarily from previously issued GAO reports. We did not update the examples, and as a result, the information in the examples may, or may not, have changed since the issuance of these reports.

1. Align individual performance expectations with organizational goals. An explicit alignment of daily activities with broader results helps individuals see the connection between their daily activities and organizational goals and encourages individuals to focus on their roles and responsibilities to help achieve those goals. To this end, for example, the Federal Aviation Administration (FAA) was able to show in fiscal year 2000 how the Department of Transportation's strategic goal to promote public health and safety was cascaded through the FAA Administrator's performance expectation to reduce the commercial air carrier fatal accident rate to a program director's performance expectation to develop software to help aircraft maintain safe altitudes in their approach paths.

2. Connect performance expectations to crosscutting goals. As public sector organizations shift their focus of accountability from outputs to results, they have recognized that the activities needed to achieve those results often transcend specific organizational boundaries. High-performing organizations use their performance management systems to strengthen accountability for results, specifically by placing greater emphasis on fostering the necessary collaboration, interaction, and teamwork across organizational boundaries to achieve these results. In this regard, the Veterans Health Administration's Veterans Integrated Service Network (VISN) headquartered in Cincinnati implemented performance agreements in 2000 for the "care line" directors, such as primary care or mental health directors, that included improvement goals related to that care line for the entire VISN. To make progress towards these goals, the mental health care line director had to work collaboratively with the corresponding mental health care line managers at each of the four medical centers to establish consensus among VISN officials and external stakeholders on the strategic direction for the services provided by the mental health care line across the VISN, among other things.

3. Provide and routinely use performance information to track organizational priorities. High-performing organizations provide objective performance information to individuals to show progress in achieving organizational results and other priorities and help them to manage during the year, identify performance gaps, and pinpoint improvement opportunities. Having this performance information in a useful format also helps individuals track their performance against organizational goals and compare their performance to that of other individuals. For example, the Bureau of Land Management's (BLM) Web-based data system, called the Director's Tracking System, collects and makes available on a real-time basis data on each senior executive's

progress in his or her state office towards BLM's organizational priorities, such as the wild horse and burro program, and the resources expended on each priority.

4. Require follow-up actions to address organizational priorities. High-performing organizations require individuals to take follow-up actions based on performance information available to them. By requiring and tracking such follow-up actions on performance gaps, these organizations underscore the importance of holding individuals accountable for making progress on their priorities. For example, the Federal Highway Administration required senior executives to use 360-degree feedback instruments to solicit employees' views on their leadership skills in 2001. The senior executives were to identify action items based on the feedback and incorporate them into their individual performance plans for the next fiscal year. While the 360-degree feedback instrument was intended for developmental purposes to help senior executives identify areas for improvement and is not included in the executives' performance evaluations, executives were held accountable for taking some action on the 360-degree feedback results and responding to the concerns of their peers, customers, and subordinates.

5. Use competencies to provide a fuller assessment of performance. High-performing organizations use competencies, which define the skills and supporting behaviors that individuals need to effectively contribute to organizational results, and are based on valid, reliable, and transparent performance management systems. To this end, the Internal Revenue Service (IRS) implemented a performance management system in fiscal year 2000 that requires executives and managers to include critical job responsibilities with supporting behaviors (broad actions and competencies) in their performance agreements each year. The critical job responsibilities and supporting behaviors are intended to provide executives and managers with a consistent message about how their daily activities are to reflect the organization's core values.

6. Link pay to individual and organizational performance. High-performing organizations seek to create pay, incentive, and reward systems that clearly link employee knowledge, skills, and contributions to organizational results. At the same time, these organizations recognize that valid, reliable, and transparent performance management systems with adequate safeguards for employees are the precondition to such an approach. In the Canadian Province of Ontario, an individual executive's performance pay is based on the performance of the provincial government

as a whole, the executive's home ministry, the ministry's contribution to governmentwide results, as well as the individual's own performance. The amount of the award can range up to 20 percent of base salary.

7. Make meaningful distinctions in performance. Effective performance management systems seek to achieve three key objectives to help make meaningful distinctions in performance: (1) they strive to provide candid and constructive feedback to help individuals maximize their contribution and potential in understanding and realizing the goals and objectives of the organization, (2) they seek to provide management with the objective and fact-based information it needs to reward top performers, and (3) they provide the necessary information and documentation to deal with poor performers. For example, IRS established an executive compensation plan for determining base salary, performance bonuses, and other awards for its senior executives that is intended to explicitly link individual performance to organizational performance. As part of this plan, IRS converts senior executive performance appraisal ratings into points to help ensure realistic and consistent performance ratings. Each IRS business unit has a "point budget" for assigning performance ratings, which is the total of four points for each senior executive in the unit. For fiscal year 2001, an "outstanding" rating converted to six points; an "exceeded" rating to four points, which is the baseline; a "met" rating to two points; and a "not met" rating to zero points. If the business unit exceeded its point budget, it had the opportunity to request additional points from the Deputy Commissioner. IRS officials indicated that none of the business units requested additional points for the fiscal year 2001 ratings.

The senior executive performance appraisal ratings and bonuses for fiscal year 2001 show that IRS is beginning to make distinctions in pay related to performance. For fiscal year 2001, 31 percent of the senior executives received a rating of outstanding compared to 42 percent for fiscal year 2000, 49 percent received a rating of exceeded expectations compared to 55 percent, and 20 percent received a rating of met expectations compared to 3 percent. In fiscal year 2001, 52 percent of senior executives received a bonus, compared to 56 percent in fiscal year 2000. IRS officials said that IRS is still gaining experience using the new compensation plan and will wait to establish trend data before it evaluates the link between performance and bonus decisions.

8. Involve employees and stakeholders to gain ownership of performance management systems. High-performing organizations have found that actively involving employees and stakeholders in developing performance management systems and providing ongoing training on the systems helps increase their understanding and ownership of the organizational goals and objectives. As one of the single most important safeguards that they can put in place, these leading organizations consulted a wide range of employees and stakeholders early in the process, obtained direct feedback from them, and engaged employee unions or associations. For example, in New Zealand, an agreement between government and the primary public service union created a "Partnership for Quality" framework that provides for ongoing, mutual consultation on issues such as performance management. Specifically, the Department of Child, Youth, and Family Services and the Public Service Association entered into a joint partnership agreement that emphasizes the importance of mutual consideration of each other's organizational needs and constraints.

9. Maintain continuity during transitions. The experience of successful cultural transformations and change management initiatives in large public and private organizations suggests that it can often take 5 to 7 years until such initiatives are fully implemented and cultures are transformed in a substantial manner. Because this time frame can easily outlast the tenures of top political appointees, high-performing organizations recognize that they need to reinforce accountability for organizational goals during times of leadership transitions through the use of performance agreements as part of their performance management systems. For example, the Ontario Public Service institutionalized the use of performance agreements in its performance management system to withstand organizational changes and cascaded the performance agreements from top leadership to front line employees.

Creating a Results-Oriented Approach to Federal Pay

With the performance management practices of leading organizations in mind, we need to fundamentally rethink our approach to federal pay and develop an approach that places a greater emphasis on a person's knowledge, skills, position, and performance rather than the passage of time, the rate of inflation, and geographic location. Under the current federal pay system, the overwhelming majority of each year's increase in federal employee pay is largely unrelated to an employee's knowledge, skills, position, or performance. In fact, over 80 percent of the cost associated with the annual increases in federal salaries is due to longevity and the annual pay increase. In addition, current federal pay gaps vary by

the nature of the person's position; yet the current method for addressing the pay gap assumes that it is the same throughout government. We must move beyond this outdated, "one size fits all approach" to paying federal employees. Under authorities granted by the Congress, a number of agencies are at various stages in using approaches in their pay and award systems that are designed to be more flexible and results-oriented.

U.S. General Accounting Office. We at GAO believe it is our responsibility to lead by example. Our people are our most valuable asset, and it is only through their combined efforts that we can effectively serve our clients and country. By managing our workforce strategically and focusing on results, we are helping to maximize our own performance and ensure our own accountability. By doing so, we also hope to demonstrate to other federal agencies that they can make similar improvements in the way they manage their people.

We have identified and made use of a variety of tools and flexibilities, some of which were made available to us through the GAO Personnel Act of 1980 and our human capital legislation enacted in 2000, but most of which are available to federal agencies. The most prominent change in human capital management that we implemented as a result of the GAO Personnel Act of 1980 was a broadbanded pay-for-performance system. The primary goal of this system is to base employee compensation primarily on the knowledge, skills, and performance of individual employees. It provides managers flexibility to assign and use employees in a manner that is more suitable to multi-tasking and the full use of staff. Importantly, careful design and effective implementation is crucial to obtaining the benefits of broadbanding in an equitable and cost-effective manner. Under our current broadbanded system, analyst and analyst-related staff in grades 7 through 15 were placed in three bands. High-performing organizations continually review and revise their performance management systems to support their strategic goals. In that spirit, we expect to modify our banded system in the future based on our experience to date.

In January 2002, we implemented a new competency-based performance management system that is intended to create a clear linkage between employee performance and our strategic plan and core values. It includes 12 competencies that our employees overwhelmingly validated as the keys to meaningful performance at GAO. The competencies are

- achieving results,
- maintaining client and customer focus,
- developing people,
- thinking critically,
- improving professional competence,
- collaborating with others,
- presenting information orally,
- presenting information in writing,
- facilitating and implementing change,
- representing GAO,
- investing resources, and
- leading others.

These competencies are the centerpiece of our other human capital programs, such as promotions, pay decisions, and recognition and rewards.

Under our revised system, pay-banded employees are placed in one of five pay categories based on their demonstrated competencies, performance, and contributions to organizational goals. Merit pay increases across these five categories range from up to about $5,700 for some of those in the top pay category to no merit increases for those in the lowest category. In addition, those in the top two categories receive bonuses, referred to as "Dividend Performance Awards," of $1,000 and $500, respectively.

As a result of GAO's implementation of its new competency-based performance management system and other changes to key human capital programs, GAO has been able to achieve greater dispersion in its performance appraisals and merit pay decisions. For example, for fiscal year 2002, the GAO-wide average performance appraisal rating was 2.19 (out of 5) compared with 4.26 (out of 5) for fiscal year 2001. Similarly, under the new system, no employees received a score of 4.7 or higher,

while 19 percent of employees received a score of 4.7 or higher for fiscal year 2001.

Federal Aviation Administration. The Congress granted FAA wide-ranging personnel authorities in 1996 by exempting the agency from key parts of Title 5. Among the initiatives FAA subsequently introduced were a pay system in which compensation levels are set within pay bands and a performance management system intended to improve employees' performance through more frequent feedback with no summary rating.

The pay band system includes plans tailored to specific employee segments: a core compensation plan for the majority of nonunion employees and negotiated versions of the core compensation plan for employees represented by unions; a unique pay plan for air traffic controllers and air traffic managers; and an executive pay plan for nonpolitical executives, managers, and some senior professionals.

Under its core compensation plan, all eligible employees can receive permanent pay increases, called organizational success increases, based on the FAA Administrator's assessment of the extent to which the entire agency has achieved its annual goals. In addition, notably high-performing individuals may receive additional permanent pay increases, called superior contribution increases, based on supervisory recommendation.[4] The criteria for awarding a superior contribution increase include collaboration, customer service, and impact on organizational success.

At the end of the performance evaluation cycle, employees receive a narrative performance summary instead of a year end rating that defines employees' performance in specific categories. That is, FAA's performance management system does not use a multi-tiered rating system to rate individual employee performance. We have previously raised concerns that such approaches may not provide enough meaningful information and dispersion in ratings to recognize and reward top performers, help everyone attain their maximum potential, and deal with poor performers. Moreover, FAA employee performance summaries reflect an assessment of achievements based on outcomes and expectations, while professional competencies such as collaboration and customer service are elements of the compensation system. As a result, the performance management

[4]Under the core compensation plan, employees who do not meet minimum requirements do not receive either of the permanent pay increases.

system is not directly linked to pay elements in FAA's compensation systems.

In February 2003, we reported that FAA's human capital reform efforts were still in progress.[5] While FAA has established preliminary linkages between its reform goals and the agency's program goals, we found that the lack of explicit linkage will make it difficult to assess the effects of the reform initiatives on the program goals of the organization even after data, measurable goals, and performance measures for human capital management efforts are established. FAA has acknowledged the importance of establishing these elements and has repeatedly said that it is working to collect and analyze data and develop performance goals and measures. However, it has not completed these critical tasks, nor has it established specific steps and time frames by which it will do so.

Internal Revenue Service. IRS was granted broad authority related to its human capital management through the IRS Restructuring and Reform Act of 1998. The Restructuring and Reform Act gave the Secretary of the Treasury various pay and hiring flexibilities not otherwise available under Title 5, such as the authority to establish new systems for hiring and staffing, compensation, and performance management.[6] Some of these flexibilities are intended to allow IRS managers more discretion in rewarding good performers and in making employees accountable for their performance.

[5]U.S. General Accounting Office, *Human Capital Management: FAA's Reform Effort Requires a More Strategic Approach*, GAO-03-156 (Washington, D.C.: Feb. 3, 2003).

[6]U.S. General Accounting Office, *Human Capital: Effective Use of Flexibilities Can Assist Agencies in Managing Their Workforces*, GAO-03-2 (Washington, D.C.: Dec. 6, 2002).

IRS implemented new performance management systems for executives and managers for fiscal year 2000 and for the front line employees for fiscal year 2001. As an initial step, IRS implemented a pay for performance system for senior executives beginning in fiscal year 2001, which emphasizes performance in determining compensation and makes meaningful distinctions in senior executive performance.[7] In July 2002, we reported that IRS had not completed all the elements of the redesign that it envisioned.[8] IRS said that it expects to integrate the new systems with its overall human resources systems linking evaluations to decisions about developmental needs, rewards and recognition, and compensation. IRS anticipates that the complete redesign and implementation of the performance management systems will take about 5 years.

OPM Personnel Demonstration Projects. Personnel demonstration projects, authorized by OPM under the authority provided by the Civil Service Reform Act of 1978, provide a means for testing and introducing beneficial change in governmentwide human resources management systems. Over the past 25 years, 17 demonstration projects have been implemented across the federal government. Twelve of these demonstration projects have implemented some form of pay for performance compensation system. OPM reports that demonstration projects that have implemented pay for performance have shown increased retention of high performers.[9]

To become a demonstration project, a federal agency obtains authority from OPM to waive existing federal human resources management law and regulations in Title 5 and propose, develop, test, and evaluate interventions for its own human resources management system that shape the future of federal human resource management.[10] Under the demonstration project authority, OPM approves project plans and regulations, approves project

[7]U.S. General Accounting Office, *Results-Oriented Cultures: Using Balanced Expectations to Manage Senior Executive Performance*, GAO-02-966 (Washington, D.C.: Sept. 27, 2002).

[8]U.S. General Accounting Office, *Performance Management Systems: IRS's Systems for Frontline Employees and Managers Align with Strategic Goals but Improvements Can Be Made*, GAO-02-804 (Washington, D.C.: July 12, 2002).

[9]U.S. Office of Personnel Management, *Demonstration Projects and Alternative Personnel Systems: HR Flexibilities and Lessons Learned* (Washington, D.C.: September 2001).

[10]No waivers of law are permitted in areas of employee leave, employee benefits, equal employment opportunity, political activity, merit system principles, or prohibited personnel practices.

evaluation plans, provides technical assistance to agencies, publishes plans, and disseminates results. The agencies are responsible for designing and implementing project plans and regulations; consulting with unions and employees about project design; and designing, conducting, and funding evaluations.

For example, the Department of Defense (DOD) implemented a personnel demonstration project covering members of its civilian acquisition, technology, and logistics workforce in 1999. Recognizing the need to reform and modernize its acquisition performance management system in order to perform efficiently and effectively, DOD designed the project to provide incentives and rewards to multi-skilled personnel, allow managers to compete with the private sector for the best talent and make timely job offers, and provide an environment that promotes employee growth and improves local managers' ability and authority to manage their workforces.

The project replaced 22 occupational families with 3 career paths; reduced the 15 General Schedule grades to 3 to 5 pay bands; and implemented a contribution-based compensation and appraisal system, which measures an employee's contribution to the mission and goals of the organization. This compensation system is designed to enable the organization to motivate and equitably compensate employees based on their contribution to the mission. Salary adjustments and contribution awards are to be based on an individual's overall annual contribution when compared to all other employees and their current level of compensation. Contribution is to be measured using a standard set of competencies that apply to all career paths. These competencies are (1) problem solving, (2) teamwork/ cooperation, (3) customer relations, (4) leadership/supervision, (5) communication, and (6) resource management.

A detailed evaluation of project results is due to OPM in May of this year that is to assess such fundamental issues as the extent to which the demonstration project improved the link between pay and contribution to organizational goals and objectives. Preliminary data indicate that the attrition rate for high contributors is declining while the attrition rate for low contributors is increasing. DOD officials we spoke with told us that increased pay setting flexibility has allowed organizations to offer more competitive salaries, which in turn has improved recruiting.

Next Steps for Results-Oriented Pay Reform

We believe that as part of the exploration now under way of using more market- and performance-based approaches to federal pay, we need to continue to experiment with providing agencies with the flexibility to pilot alternative approaches to setting pay and linking pay to performance.

In the short term, the Congress may wish to explore the benefits of broadbanding by (1) giving OPM additional flexibility that would enable it to grant governmentwide authority for all agencies (i.e., class exemptions) to use broadbanding for certain critical occupations and/or (2) allowing agencies to apply to OPM (i.e., case exemptions) for broadbanding authority for their specific entities or occupations. However, agencies should be required to demonstrate to OPM's satisfaction that they have modern, effective, credible, and validated performance management systems in place before they are allowed to use broadbanding or related pay for performance initiatives. This is consistent with the approach that the Congress took with raising the increase of the total annual compensation limit for senior executives as part of the Homeland Security Act. The Congress may also want to consider providing guidance on the criteria that OPM should use in making judgments about individual agencies' performance management systems. We believe that the practices we described today could serve as a starting point for that consideration.

In summary, there is widespread agreement that the basic approach to federal pay is broken and we need to move to a more market- and performance-based approach. Doing so will be essential if we expect to maximize the performance and assure the accountability of the federal government for the benefit of the American people. Reasonable people can and will debate and disagree about the merits of individual reform proposals. However, all should be able to agree that a performance management system with adequate safeguards, including reasonable transparency and appropriate accountability mechanisms in place, must serve as the fundamental underpinning of any fair, effective, and appropriate results-oriented pay reform. The practices that have been used by leading organizations in developing and using their performance management systems to link organizational goals to individual performance and create a line of sight between an individual's activities and organizational results show the way in how to implement performance management systems with the necessary attributes.

Chairwoman Davis and Members of the Subcommittee, this concludes my statement. I would be pleased to respond to any questions that you may have.

Contact and Acknowledgments

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Mrs. DAVIS OF VIRGINIA. Thank you, Mr. Mihm.

Mr. Stier.

Mr. STIER. Thank you very much, Madam Chairwoman and Congressman Davis. It is a pleasure being here particularly with Chris who has done wonderful work at GAO and George Nesterczuk and the panel coming, including Colleen Kelley who is on our advisory board.

It is great the committee is doing this. I think you are to be commended. When we talk about Civil Service reform, oftentimes the elephant in the room that goes unrecognized is the issue of compensation and compensation reform. It is a tricky set of issues but it is terrific that you are focusing on it today and bringing together so many people to share their experiences with you.

It is particularly important to be focusing on it today given the challenges the Federal Government faces with respect to its human capital and I also think it is about time. There has been research, there has been 25 years of demo project experience. There are expected agencies that have been experimenting and in fact, there are answers to questions raised by members—other agencies that have been attempting gainsharing. PTO is an example and others. Clearly the GAO report is going to shed some interesting light on that. So this is terrific.

I would begin by noting that the merit principles themselves talk about a form of recognizing excellence. The law requires, "Appropriate incentives and recognition should be provided for excellence in performance." That is in the law today but unfortunately it has not, I think, been adequately implemented. I think much of the committee's attention should be focused on how do you get that to be a reality in today's workforce.

I would make three very quick points. The first is that this issue is not easy but it is worth tackling, very much so. The present system I believe is very much broken. You have the White Paper from OPM which is very instructive. Very importantly, look at what the employee surveys are telling us. In the year 2000, the Merit Systems Protection Board did a survey asking "If you perform better in your present job, how likely is it that you will receive more pay?" Fifty-four percent said unlikely versus 35 percent saying likely. The most recent survey we have from OPM, the 2003 survey, again the chairwoman has raised some of these statistics, only 30 percent agree with the proposition that "Our organization's awards program provides me with an incentive to do my best." Only 45 percent of employees agreed with the statement that "Arbitrary action, personal favoritism and coercion for partisan, political purposes are not tolerated." That is a real problem.

I would note that number, according to the OPM report, was 5 percent higher among the employees surveyed in the alternative personnel systems and demo projects. That may not be management nirvana but it is a statistically significant improvement and it says it is possible to do better even under the existing system with some of the experimentation that has taken place.

Second, the potential gains here are absolutely enormous. If you believe that better performance will receive better rewards it increases employee commitment. That is something you see all over the private sector research. Watson and Wyatt did a survey in

which they found an 82 percent level of commitment for employees who believe they will receive better pay for better performance versus a 35 percent level of employee commitment for those who did not.

We also can see examples in the public sector, Bonneville Power Administration and GAO both talked about in great detail in the written testimony.

The third point I would like to raise is that the issue of pay for performance really needs to be looked into in larger context. Many of the members of the committee have raised this already. We need to be reviewing this as performance management, a culture of results, and not simply a pay reform issue. It is really a comprehensive system we need to be talking about, not only the evaluation system raised here but really an ongoing dialog between managers and employees about the way contributions are made by individuals to meet the organizational needs of the agency.

That means that ultimately you have to start with clear organizational goals and ongoing communication—something that oftentimes is not accomplished in agencies today—in order for employees to be able to fully commit to the process.

Clearly, we need to be looking at individual agencies before we allow them to move forward to a system that is going to be more directed toward tying rewards to performance. It is something we really need to do. There are lots of ways to do it. We have good examples out there. Obviously the groups you have involved in the testimony today need to be involved in that process. We look forward to helping in whatever way we can.

[The prepared statement of Mr. Stier follows:]



PARTNERSHIP FOR PUBLIC SERVICE

Testimony of

Max Stier
President and CEO
Partnership for Public Service

Before the

Subcommittee on Civil Service and Agency Organization
Committee on Government Reform
House of Representatives

on
Federal Employee Compensation Reform

April 1, 2003

Thank you, Chairwoman Davis and Members of the Subcommittee, for the invitation to testify before you today on an issue that represents perhaps the greatest remaining challenge facing the federal civil service today: reform of an inflexible and outdated federal compensation system. As President and CEO of the Partnership for Public Service, my objective and that of the Partnership itself is to help the federal government recruit and retain the highly qualified, motivated, and effective workforce that the government and the nation so very much needs. An effective compensation system is one component of a performance management strategy necessary to achieve that goal. As the Subcommittee's hearing today would indicate, the current federal compensation system does not contribute to the federal government's ability to attract and retain the best and brightest.

The Partnership suggests that the Subcommittee undertake its review of compensation reform in the context of a larger discussion about how best to give managers more flexibility to properly reward and incentivize superior performance and to effectively deal with inferior performance. As the administration has already recognized, agencies should demonstrate that they have implemented or are ready to implement improved performance management systems before additional resources are dedicated to bolstering federal compensation.

It is vitally important that government workplaces are places where initiative, superlative effort and tangible results are rewarded. The dynamics of workforce culture are, in truth, the key drivers of our government's effectiveness and productivity. At the same time, the next generation of talent that the government needs to recruit is not attracted to government jobs in part because of a serious perception problem that such jobs do not reward initiative. These perceptions pose substantial recruitment challenges that can only be overcome by sustained attention to the hard work of making sure that effort leading to results and workplace rewards (including non-monetary rewards) are closely tied.

In pursuing these goals of increased organizational effectiveness and improved recruiting competitiveness, we would urge the Subcommittee to be mindful of two essential

elements of successful performance management systems. The first is an acceptance of responsibility by agency leaders, managers and supervisors for the successful implementation and administration of effective performance management systems. These issues cannot be left to HR administrators. The second key element for success is the ongoing solicitation of employee input. The failure to engage employees in the design of a performance management system is one of the critical fault lines that lead to failure. Employee input and ongoing feedback is necessary to increase "buy-in" and ensure a shared understanding between employees and managers of goals and performance measures.

We already know that most federal employees view the promotion decisions of their supervisors with great skepticism. Only 45 percent of federal employees responding to a recent Merit Systems Protection Board (MSPB) survey reported that their supervisors promote the best qualified person, and 75 percent of employees said they were not promoted because the supervisor had someone else in mind before announcing the job was open to competition. Likewise, a significant portion of federal supervisors did not think that their organization's merit promotion process allowed them to select the best-qualified applicant. When you think about the fact that promotions are already a "pay for performance" system that is deeply imbedded throughout the government workplace, then you begin to see why improving the credibility of managerial decision-making in administering reward systems within the workplace is a key challenge and opportunity facing both agency leaders and policymakers. In many ways, the system is broken. The question, therefore, is not whether it is advisable to attempt compensation reform, but how best to undertake a project of such compelling importance to the health of our government workplaces.

Almost a year ago, the U.S. Office of Personnel Management issued its white paper, "A Fresh Start for Federal Pay: The Case for Modernization," which does an excellent job of laying out the problems inherent in a pay and classification system originally developed in 1949 and which has changed little even as the federal work environment and workforce needs have changed dramatically. As OPM concludes in their white paper:

> The divergence between the Federal pay system and the broader world of work where the war for talent must be fought has led observers to call for reform of the Federal system. To support achievement of the Government's strategic goals, a new, more flexible system may be called for, one that better supports the strategic management of human capital and allows agencies to tailor their pay practices to recruit, manage, and retain the talent to accomplish their mission.

Similarly, the January 2003 report of the National Commission on the Public Service, "Urgent Business for America: Revitalizing the Federal Government for the 21st Century," took a comprehensive approach in identifying the very significant challenges facing the federal government as it struggles to keep pace with the growing demands of the modern and increasingly complex world. While the Commission made a number of sweeping recommendations dealing with the organization and leadership of government, it was quite targeted when it came to the federal government's pay and classification:

> We recommend that the General Schedule classification system be abolished....As a default system, we recommend a "broadband" system under which the 15 pay grades and salary ranges would be consolidated into six to eight broad bands with relatively wide salary ranges. Managers would be able to determine individual pay based on competence and performance. Other agencies might adopt systems with an entirely different form....we envision the development of modern personnel management approaches that afford agencies far more flexibility and responsiveness in packaging attractive job offers at the entry level, while fitting talent to task across the full spectrum of federal activity....

The General Accounting Office, in its January 2003 report, "High-Risk Series: Strategic Human Capital Management," pays particular attention to the need for effective performance management systems in the federal government, and also notes that:

> Ultimately, an effective performance management system must link pay and incentive programs to individual knowledge, skills, and contributions

> to achieve organizational results. However, this link will never be achieved without modern and effective performance management strategies. In that regard, leading organizations understand the importance of creating effective incentives and rewards for high-performing employees that place a greater emphasis on knowledge, skills, and contributions to achieving organizational results...rather than the passage of time, the rate of inflation, or geographic location, as so often is the case today.

Finally, we also find ourselves in agreement with the National President of AFGE, Mr. Bobby Harnage, when he noted in testimony on July 17, 2001, before the House Subcommittee on Oversight of Government Management, Restructuring and the District of Columbia that:

> No one engaged in the discussion over how to solve the federal government's human capital crisis disputes the fact that the pay and benefits package provided by the federal government needs improvement.

The issue then, is not whether the current method of compensating federal employees is broken, but rather what needs to be done to fix it and to ensure it supports an effective performance management system. On that point, there are considerable differences of opinion. For its part, the Partnership for Public Service is persuaded that movement towards a more performance and market-sensitive pay system is the right course of action and long overdue. I would also note that the recent release by the Office of Personnel Management of the results from their 2002 Federal Human Capital Survey also made it clear that federal employees themselves seem to agree with this assessment. For example:

- Only 39 percent of federal employees think that their work units are able to recruit people with the right skills.
- Fewer than half of all federal employees are satisfied with the recognition they receive for doing a good job.

- Similarly, fewer than half of the federal workforce believes there is any connection between job rewards and how well they do their job.

Designing a 21st Century Compensation Strategy for the Federal Government

Having established that the federal government's current compensation and classification system is in need of a major overhaul that will enable it to become more market-sensitive as well as performance-sensitive, the next logical step is development of a design strategy to achieve that goal. Fortunately, the federal government need not start from scratch in this regard. For more than 20 years, the government has been developing information about what does and doesn't work within a federal work environment through "demonstration projects" authorized by the Civil Service Reform Act of 1978 (starting with the Naval Weapons Center at China Lake) and from the experiences of federal organizations that were given special statutory flexibilities in this regard (for example, the Federal Aviation Administration, Patent and Trademark Office, and the Internal Revenue Service). There is also a large body of research from the private sector that can be adapted for the public sector.

Some clear conclusions emerge from the body of evidence that has been gathered over the last couple of decades. One is that a performance-based pay system can work in the federal government but it cannot simply be dropped into place and expected to achieve the intended results. As with any worthwhile and effective human resources management policy, program, or practice, an employee classification and compensation system that is successfully performance and market-sensitive will require concentrated effort, resources, and a long-term commitment to making it work. In addition to providing some lessons about what can work via the demonstration project authority, the Civil Service Reform Act of 1978 (CSRA) also provided an early lesson with regard to what does not work. This lesson was the experiment with "merit pay" that started with federal supervisors and managers at the GS-13 through 15 grade levels and which was to be gradually extended to the rest of the federal workforce.

The CSRA merit pay approach was designed as a government-wide system driven by a five-level performance appraisal process designed around a set of "elements and standards" developed for each position. Every supervisor and manager attended required training on how the system was to operate and their responsibilities for making it work. A key aspect of this merit pay system was the abolishment of "within grade increases," in favor of annual pay adjustments driven by each supervisor's and manager's annual performance appraisal The early experience with this merit pay was unsatisfactory due to funding limitations that greatly restricted the monetary differences that could be made among employees with different performance ratings and the fact that some supervisors and managers received smaller pay increases than they would have received with the same performance rating under the old system. Adjustments were made in this early attempt at a government-wide performance-sensitive pay system and it was reconfigured as the Performance Management and Recognition System (PMRS). After several years experience under the PMRS, however, the hoped for benefits still did not materialize to a sufficient degree and Congress allowed the PMRS to sunset and the covered employees were converted back to the "old" general schedule system.

What was learned from the general failure of the PMRS and the success of some "pay for performance" systems tailored for specific federal organizations under demonstration projects or via special legislation, is that a performance-sensitive pay system can work in the federal government, but that there are a number of conditions that must be present and some general principles that should be applied. In designing a 21st Century compensation strategy for the federal government, therefore, we recommend that Congress and the Administration pay particular attention to incorporation of the following principles or "success factors:"

1. Recognition that "one size does not fit all," particularly with regard to performance-sensitive pay systems. Even organizations within the same large federal department or agency can have very different cultures, missions, workforce demographics, and work or outcome measures. It's possible, perhaps even likely, that what might make sense for high level scientists and engineers in the collaborative environment of a

research laboratory is very different from the system that would be successful in a production-oriented environment such as an IRS Service Center or an SSA or VA claims processing center where there are clear quantity and quality standards in place that can be used to determine an employee's individual contribution to the mission of the organization. Any changes in the statutory framework regarding federal compensation should provide considerable flexibility that allows federal organizations to develop a customized approach tailored to the unique needs and work environment of the organization while remaining within the broad framework of the law. Evaluation of the relative success of an organization's program would be based on results achieved (e.g., productivity improvements, employee and "customer" feedback, and other outcome measures) rather than simple adherence to the mechanics of a system.

2. Federal pay should be market-sensitive. Again, this is not a one size fits all proposition. Pay must be different for different talent pools, geographies, etc. Agencies should be allowed to target critical talent and take into account what the OPM white paper calls "strategic rewards" in referring to the combination of compensation, benefits, opportunities for learning and development, and the work-environment. We are not arguing that the federal government needs to be the market leader in terms of base pay, particularly when it offers some very competitive intrinsic rewards, but neither should it be at the back of the pack. In this regard, we also note that even with the advent of some sensitivity to geographic differences via the locality wage adjustments that can be made under the Federal Employees Pay Comparability Act (FEPCA), different occupations at the same grade in the same region are paid the same regardless of local labor market conditions that may vary widely by occupation. This does not make sense.

3. Developing sufficient pay flexibility to allow the federal government to become truly an employer of choice for its fair share of the "best and brightest" in the talent pool will require flexible position classification strategies that allow federal departments and agencies the options of using more relevant systems, such as a competency-based

or "pay banding" approach to pay setting. While such systems are not "magic bullets" in the war for talent and require considerable skill and preparation on the part of an agency, such approaches have been demonstrated to be effective in attracting and retaining employees in hard to fill or "shortage category" occupations. This will also help improve the competitiveness of pay across pay levels. It has been noted, for example, that the median salaries paid by the federal government for some hard to fill occupations, such as engineers and scientists, appear to already be competitive with the private sector. What this masks, however, is that entry-level salaries offered to new college graduates in these occupations are often significantly below those offered by the private sector. The difference is that the federal sector salary increases in the first several years of employment are often more rapid than in the private sector as employees move via career ladder promotions geared to the two-grade interval federal position classification system. Some of the most highly qualified new college graduates, however, are more likely to be enticed by starting salary than the promise of future promotion possibilities. A more flexible classification system could allow the federal government to be more competitive when it matters the most.

4. Clearly, most well-designed pay or performance management systems can be thwarted by ineffective or poorly prepared managers and supervisors. Therefore, any effective fixes to the current compensation and classification system will be largely dependent upon senior leadership and management support and "ownership." Once given more effective tools, and training and support in using these tools, managers must be held accountable for achieving cost-effective results, i.e., they should be able to demonstrate their ability to recruit and retain motivated and productive employees who contribute to the agency's mission.

5. An effective performance-sensitive pay system must also gain the confidence of the employees that they will be treated fairly and that their relative performance and contributions to their agency's mission accomplishment is linked in a meaningful way to their job rewards. Federal employees and/or their representatives should be

involved in the early planning stages of any new system and throughout its implementation. Thereafter, employees should have the opportunity to provide meaningful feedback on how well the system is operating and that feedback should help drive any mid-course corrections or adjustments that are needed.

6. A performance-sensitive pay system must also clearly be driven by a performance management system that establishes credible and transparent measures of the work done or contributions made by individuals or employee teams. In any credible performance management system –
   - agency strategy must be clearly articulated;
   - leaders and managers must work with employees to identify the right individual or team goals that link their efforts to mission;
   - managers must devote appropriate time and attention to ongoing counsel and feedback and employee development;
   - managers must conduct meaningful year-end sessions with employees, including constructive feedback about their accomplishments and career-development goals; and,
   - employee feedback should be sought and used to improve the system.

7. Finally, movement to the type of performance-sensitive and market-sensitive classification and compensation system described above represents a major culture shift for most federal departments and agencies. To successfully make this leap into the 21st Century will require a long-term commitment by the government and by political and career managers. Fortunately, we already have more than 30 different federal agencies or organizations that have already experimented with various performance management approaches that seek to create a stronger link between pay and performance (see the attached chart). Two of those organizations are highlighted in the following text. There are some useful lessons to be learned from these attempts, including the fact that there are indeed viable alternatives to the unsatisfactory status quo that still exists in most federal agencies.

Two Case Studies: Bonneville Power Administration and GAO

As we have already noted, there is no "one-size-fits-all" performance management system that is appropriate for all government agencies. Each agency must have the flexibility to craft appropriate performance measures and to choose how to link organizational goals to individual job responsibilities. Within this context, there are terrific examples of agencies that have successfully implemented performance management systems that have resulted in better results for the agency mission, increased employee satisfaction and increased employee commitment.

Bonneville Power Administration

This agency within the Department of Energy markets wholesale power to 11 million customers in the Pacific Northwest. Operating much like a business, they have been self-financing since 1998 and reinvest the revenue from their power sales ($4.5 billion in 2001) in fish, wildlife and energy conservation programs. Their customer satisfaction surveys repeatedly show that they do a terrific job at delivering valuable services and stewarding a vast network of natural resources. In short, BPA is the kind of high-performing organization that government should strive to emulate.

How does such an organization manage its workforce? One of the keys to BPA's organizational success is ensuring that managers really own their responsibilities to manage effectively, including the obligation to recognize and reward performance. BPA managers sign performance management contracts that link 50 percent of leader's financial rewards to their people management skills, including communicating with employees, empowering employees, creating a community among diverse people, collaborating effectively and building workforce excellence. These contracts promote an ongoing dialogue between supervisors and employees about performance and goal achievement. BPA has worked hard to communicate with its employees about the new performance plans by holding accountability training and sessions on the plans. At the beginning of each Fiscal Year, employees meet with supervisors to negotiate what they will be responsible for producing over the course of the year. Employee performance is

rated according to a "balanced scorecard," which includes measures of employee contributions to company-wide objectives. Employee responsibilities are broken down into four key categories: stakeholder, financial, internal and learning and growth.

To keep employees motivated and energized as they work toward the annual goals on their plans, BPA provides many opportunities for rewards and recognition. Although many rewards are non-monetary, BPA has made a real financial commitment to the success of its performance management system. In 1998, BPA tripled the money available for awards from 3 percent to 9 percent of base salary. While recent economic challenges have reduced the bonus pool funding, the intent of sharing rewards remains. The agency distributes awards on both an individual and a group basis, with team awards making up more than half the total amount of awards given. BPA also administers targeted development programs to give employees the skills they need to achieve their annual goals.

The results of these emphases on managerial accountability and effective employee communications have been dramatic. According to BPA's 2002 employee survey (modeled on Fortune Magazine's "Best Places to Work" survey), 72 percent of respondents agreed with the following statement: "Taking everything into account, I would say this is a great place to work." These results represented sharp increases over the 67 percent in 2001 and 57 percent in 2000 who felt BPA was a great place to work. In addition, the organization topped the list in 14 of 17 categories of OPM's organization effectiveness surveys in 2002. BPA's customers and constituents, whom the agency also surveys, have similarly registered a steady increase in customer satisfaction over this same time period. This correlation is not surprising. Committed employees produce organizational results.

General Accounting Office

The experience of the General Accounting Office under the leadership of Comptroller General David Walker provides another set of important lessons about the importance of employee engagement in developing an effective and comprehensive performance management system. In 1999, after Comptroller General Walker arrived at the GAO, he

conducted GAO's first employee feedback survey, which revealed widespread dissatisfaction with GAO's performance management system and a desire for greater transparency and more consistency in the ratings process.

GAO's old performance management system was behaviorally based, meaning it focused more on activities rather than results. GAO, drawing from best practices in the private sector and Mr. Walker's own experience as a leading HR consultant, devised a new system which is competency based, flows from the agency's strategic plan and which was used to develop performance standards for employees. Significantly, focus groups of affected employees were used to determine the required competencies. This process helped achieve crucial employee buy-in for the new system, as there was 85 percent agreement among analysts on the selected competencies. As an added bonus, the new performance standards that emerged helped GAO to identify gaps in the organization's required knowledge, skills and abilities.

Successful implementation of the new system relied heavily on extensive employee communication and training. GAO developed a web-based training tool to teach employees how to use the new system. A tutorial video with simulation exercises is available twice a day on the intranet, and employees are encouraged to access the video from their desktops.

External consultants were tasked to develop a training course for managers called "Having constructive conversations about performance." The course is designed to ensure that dialogue and feedback about employee performance and business results are continuous. Most importantly, the agency has focused on educating managers about the difference between performance management and simply filling out a performance appraisal form.

GAO does not claim to have the perfect system yet, but as they continue to adjust and fine-tune based on experience, results and employee feedback, they are clearly moving in the right direction. These important steps augur well for GAO's prospects in transitioning to a performance management system that effectively links individual performance to organizational goals. Congress would be well-served by keeping the

Comptroller General's model in mind as it undertakes to craft a set of guidelines that will allow the rest of government to follow suit.

OPM's Proposed Human Capital Performance Fund and SES Pay for Performance

Having identified several "success factors" that will determine the degree to which federal compensation reform, and in particular pay-for-performance initiatives, will succeed, I will now turn to the two proposals recently put forth by the Administration: an SES Pay for Performance proposal and the establishment of a Human Capital Performance Fund. The former would significantly expand the pay range for federal senior executives and provide some much needed relief from the effects of pay compression. The SES proposal would also give federal agencies significantly more flexibility to set pay within the new and broader pay range and would seek to more closely link any annual adjustments within that range to the performance of each executive and the results they achieved. The proposed Human Capital Performance Fund would, for the first time, provide a relatively substantial amount of funding to be used to adjust the base pay of employees based solely on individual or group performance and contributions to the agency.

We applaud the intent behind both proposals to provide additional pay-setting flexibility to federal agencies to develop a closer link than currently exists between base pay and the performance and contributions of the individual or executive. These are clearly steps in the right direction with regard to systems design. We also recognize, of course, that the details regarding how these legislative proposals—if passed—are implemented and funded will determine whether the hoped for benefits are realized and whether any unintended negative effects are avoided or minimized. In that regard, we offer a few more specific observations on each proposal as follows:

SES Pay for Performance:

If the federal government is going to take pay reform seriously and move to a more market and performance-sensitive compensation system, the Senior Executive Service is the right place to start. If we are going to attempt to do a better job of holding employees

accountable for results that matter and recognizing those who do an especially good job of achieving those results, it sends the right message to the rest of the workforce to start at the top. Further, the federal government's ability to recruit and retain highly qualified senior executives in any number of critical jobs has clearly suffered as a result of pay compression and the inability within the existing system to adequately reward in any ongoing manner the truly stellar performers. Also, the fact that at least 7 out of every 10 senior executives will be eligible to retire within the next five years makes it even more imperative for the federal government to develop additional tools for agency leaders to use on a targeted basis to attract or retain critical talent in the SES. We think this proposal deserves serious consideration and implementation in at least some form.

Our endorsement is based on a deeply help belief that federal executives should be assessed and compensated based upon their success in meeting organizational and managerial objectives under the Government Performance and Results Act and the President's Management Agenda. We have an opportunity with this legislation to revise existing performance appraisal systems from the current process-oriented, subjective assessments that are still too common to an approach which articulates and measures objective benchmarks for the accomplishment of organizational and managerial goals.

A hallmark of a true pay for performance system for the SES, therefore, will be its ability to provide a transparent and credible means for making meaningful distinctions among executives regarding pay adjustments based on their accomplishments and contributions. Correspondingly, a challenge for that system will be its ability to make those distinctions without de-motivating executives who also had success in achieving their objectives but perhaps not as much success as some others experiencing a truly banner year. In this regard, we would recommend that the focus remain on measurable outcomes and achievements (and appropriate differential pay adjustments based on those outcomes) with less emphasis placed on the assignment of individuals to performance categories. To be sure, we expect federal senior executives, as a group, to be high performers and to regard themselves as members of a senior leadership team. While OPM will logically

take the lead in the design and implementation of this system, they will also need to work closely with federal agencies and executives and the Senior Executive Association.

Human Capital Performance Fund:

As with the SES proposal, flexibility to recognize high performing federal employees is an essential component in the federal government's effort to recruit and retain quality staff. The administration's proposal can enable federal managers to differentiate and reward performance and make a significant dent in addressing the factual basis underlying current perceptions that pay and rewards are not linked to performance accomplishments. A significant challenge here will be to ensure that the human capital performance fund does not become a substitute for adequate funding of the federal compensation and performance management systems. To succeed and to have credibility among employees, the fund should be a method of making pay adjustments under a fully-funded and market-sensitive compensation system. The federal workforce is too important and the demands being made upon government are too great to do otherwise.

Finally, the legislation calls upon OPM to manage this fund and allocate monies to agencies based upon OPM's review and approval of a plan submitted by each agency outlining how they intend to use the share of the fund. While guidance and oversight by OPM each agency's plans for and use of the fund helps to provide some assurance that the funds will be used appropriately, serious consideration should be given in the out years to allowing an agency with an established track record of success in this regard to receive funding directly through the appropriation process rather than through OPM. OPM, however, should continue to have general oversight responsibility as it does now for other federal HR programs.

Madam Chairwoman and Members of the Subcommittee, I want to again thank you for allowing me to share with you the perspectives of the Partnership for Public Service on these issues that are so important to the future of the federal workforce. We would be

happy to assist the Subcommittee in any way we can as you seek to ensure that the federal government has the world-class, highly motivated workforce that it needs for the challenges that lie ahead. I would be happy to answer any questions you may have.

An Initial Review Identified 32 Examples of Performance Management Efforts with Links to Pay

Demonstration Projects	Title 5 Exempt/Special Authorities	Title 5
Navy – China Lake	Veterans Health Administration	The US Mint
National Institute of Standards and Technology	National Credit Union Administration	HHS (PSC Group)
Commerce Department – NOAA/other groups	Federal Aviation Administration	Defense Logistics Agency
DoD Acquisition Workforce	Patent and Trademark Office	GSA (Public Buildings Service)
Air Force Research Laboratory	Student Financial Assistance	Tobyhanna Army Depot
Army: Aviation Research, Development and Engineering Center	Internal Revenue Service	Red River Depot
Army: Missile Research, Development and Engineering Center	Bureau of Alcohol Tobacco and Firearms	
Naval Sea Systems Command Warfare Centers	General Accounting Office	
Army Medical Research and Material Command	Central Intelligence Agency	
Army Research Laboratory	US Postal Service	
Army Engineer Research and Development Center		
Naval Research Laboratory		
Pacer Share (McClellan Air Force Base)		



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MISSION STATEMENT

The Partnership for Public Service (www.ourpublicservice.org) is a non-partisan, non-profit organization dedicated to recruiting and retaining excellence in the federal civil service. Through an aggressive campaign of agency reform, legislative advocacy, focused research and educational efforts, the Partnership encourages talented people to choose federal service for some or all of their careers and works with the government to help retain high-achieving federal employees.

The need for action is urgent. In the next five years, well over half of the federal workforce may qualify for retirement. Within the same period, 71 percent of the government's senior managers will reach retirement age. To replace these experienced workers, and to ensure quality service to the public, the government must continue to attract talented workers.

Even after the September 11 tragedies, the federal government is seldom viewed as the "employer of choice" for the best of our country's labor pool. A recent nationwide public opinion poll commissioned by the Partnership found that private sector jobs are significantly more attractive to college graduates seeking challenging work and financial reward, and the non-profit sector is more appealing than government to those who want to "make a difference." Polls also indicate, however, that more and more graduates are interested in contributing to their society and community.

These attitudes and demographic realities present the government with substantial challenges but also suggest that there are unprecedented opportunities to engage a new generation seeking meaningful ways to serve.

To meet this challenge, the Partnership for Public Service is pursuing a comprehensive five-part strategy:

(1) A partnership with federal agencies to help create a work environment for the 21st century that allows government to better support and retain its talented workers;

(2) A legislative reform agenda to address outdated laws that keep the government from attracting and retaining highly skilled employees, and to implement management practices more comparable to those in the private sector;

(3) A practical research plan to increase our understanding of the human capital crisis and its possible solutions;

(4) An education and outreach effort to inform talented mid-career professionals about employment opportunities in government and a national college and university campaign to inform students about federal jobs (www.calltoserve.org); and

(5) A communications program designed to improve public understanding and perception of government service.

In pursuing this strategy, the Partnership is building coalitions with the Administration, lawmakers, corporate leaders, federal employees, academic institutions and other interested groups. The Partnership is guided by a Board of Governors comprised of prominent, committed individuals who provide advice and expertise and serve as spokespersons for the importance of public service.

The Partnership was founded by Samuel J. Heyman in 2001 and is incorporated as a 501(c)(3) non-profit organization. The Partnership is located in Washington, D.C.

Mrs. DAVIS OF VIRGINIA. Thank you, Mr. Stier. We appreciate that.

Mr. Nesterczuk.

Mr. NESTERCZUK. Thank you, Madam Chair and Mr. Davis. Thanks for this opportunity to address the committee on the question of compensation of Federal employees. It is a very timely issue. Although current surveys may indicate some satisfaction with current pay systems, historically it has always been an irritant in the work force, maybe a reflection of economic conditions outside.

Let me summarize of the key points I made in my written testimony so that I can stay within the 5-minute time limit.

There is no question in my mind that the pay system is, if not broken, certainly dysfunctional in many instances. If we look at the past 15 years and the experience of agencies coming to Congress seeking relief and getting relief for special circumstances, I think there is a message there for the Civil Service Subcommittee to seriously take to heart.

FIRREA exempted the banking regulators of financial institutions from Title V pay restrictions way back in 1986–1987. The FAA was taken out from under Title V and established its own separate pay system back in 1996. The IRS followed suit in 1998 and that is 100,000 employees in that case. The Transportation Safety Administration followed in 2001 with a separate pay system and the Department of Homeland Security. So you are looking at 300,000 to 400,000 employees that are going to be out from under the General Schedule.

There is a clear message there which is agencies are focusing on their missions. They find the pay system is not supporting getting their job done. OPM has historically had special pay authority but clearly it is not adequate. That was intended to rifleshoot individual occupations in specialized locations where local labor market conditions dictated exemptions from the General Schedule. The agencies are clearly looking for much more sweeping reforms.

Let me now address the question of performance management, performance recognition in the Federal Government, a whole separate issue. Pay for performance is not really a play these days in the Federal Government, except perhaps at the SES level where performance is more strictly adhered to.

The two concepts are clearly divorced in the minds of most Federal employees. The culture just doesn't recognize pay and performance as being related. Pay adjustments annually are pretty much automatic. Twice a year adjustments for many employees, every 2 or 3 years for everybody else in 3 to 4 percent increments, so a 6 to 7 percent pay increase, regardless of how well you do your job is a demotivator to go out and try harder if your cohort is not contributing to the process. So performance is used as an adjunct.

We do have performance recognition systems or cash awards, bonuses for the SES, Presidential rank awards, but where is the fundamental underpinning for making those awards? If a performance management system results in 80 to 90 percent of employees being rated above average, then what are the criteria that are used to make decisions for those cash awards, those rank awards, the incentive awards for rank and file employees. There is a huge amount of cynicism in the work force because they clearly under-

stand there is some other system at play here which is being relied on to support the bonus decisions.

We need a very robust, transparent performance measuring system that makes meaningful distinction in relative performance among employees. Until that is on the table, you are not going to be able to marry pay and performance.

There are a number of options that the committee is looking at today in realm of pay reforms. As I said, we go back to the basic problem and agencies are speaking up telling you they do need some kind of pay remedies. Pay banding is a credible alternative. It has been tested for 25 years now. Yes, there are some shortcomings with it. It tends to inflate the overall payroll but those are issues that can be managed.

I think the notion of using OPM as a watchdog working with agencies to ensure they implement the right kinds of responsive performance management systems to go along with the pay banding reforms is probably a suitable approach.

Moving to SES paybanding, the open pay system for the SES with a raise cap is very important. That is a key element in the chain of command from the President, Cabinet Secretaries to agency heads down at the career work force. They need to be motivated and rewarded for their efforts and the pay compressions that historically reoccur every few years which is not only a big demotivator for performance but tend to encourage people to leave the work force.

Finally, the Human Capital Performance Fund I think is an excellent idea. It is a marginal in the overall picture of the overall payroll of $100-$120 billion and $500 million is a marginal increment in that but it is new money for the agencies. It is the kind of incentive they need to get their performance management systems up to snuff.

Thank you.

[The prepared statement of Mr. Nesterczuk follows:]

Testimony of
George Nesterczuk
President, Nesterczuk and Associates
before the
Subcommittee on Civil Service and Agency Organization
Committee on Government reform
U. S. House of Representatives
on compensation reform for federal employees
April 1, 2003

Chairman Davis and members of the Subcommittee, thank you for the opportunity to testify today on the matter of compensation reform for federal employees. My name is George Nesterczuk and I am President of Nesterczuk and Associates, a management consulting firm located in Vienna, VA.

It is my understanding that the Subcommittee is giving serious consideration to proposing changes this session in the way federal employees are compensated. This is a rather broad topic and it contains a number of complex facets. I will limit my testimony to the pay component of compensation and more specifically to the white-collar pay systems captured by the General Schedule and the Senior Executive Service.

Let me begin with a fairly safe statement – dissatisfaction with federal pay has been a long standing irritant at all levels of the federal workforce. Federal pay is tied to a highly structured position classification system that is deemed by many critics to be too rigid and that attempts to be all things to all people, i.e. a "one size fits all" system. The combination of this classification system together with pay tables structured for longevity results in a pay system viewed as not sufficiently competitive at entry and that quickly stagnates at mid career. Presumably, despite the criticism, federal compensation (pay plus benefits) meets some employee expectations or else agencies would face periodic depopulation of their workforces.

Brief Historical Perspective

The pay system of today has its roots back in the 1940s and 1950s. The workforce in those years was much more clerical and administrative with a contingent of technicians and far fewer professionals than today. There was also a large contingent of blue-collar workers. Employees came in at entry level and could count on lifetime employment with careers spanning 30 to 40 years. The 10 steps of each of the 15 grades of the General Schedule were well suited to the career progressions of the dominant occupations of those earlier periods. Similarly the comparable grade and step structure of the Wage Grade Schedule fit the blue-collar workforce as well.

The missions and workloads of federal agencies today have evolved dramatically from those earlier days, as have the means by which work is accomplished. Automation and information technology have revolutionized the work place. They have also permitted enterprises to focus on core competencies and outsource supporting activities. Today's

labor force is more mobile and career progression in many fields is characterized by frequent job changes. Lifetime employment with one employer is no longer the norm and mid career changes are more common than rare.

During this period of radical change in the labor force and in the workplace many government management systems have lagged significantly behind. Counted among the laggards is the federal pay system.

Differentiation of Pay Systems Already Exists

Some differentiation of pay systems does already exist. The Executive Schedule attempts to deal with pay at the highest management levels of federal agencies and Cabinet departments. Congressional pay is linked to Level II of this pay schedule. Judicial pay was also linked to the Executive Schedule until it was severed during the 1980s. Legislative branch and judicial branch employees have their own separate pay schedules. Separate schedules have been established for the Foreign Service and the Public Health Service.

Early on, the General Schedule was extended beyond grade 15 to include "super grades" GS 16 to GS 18 as a recognition of the growing complexity of jobs in the federal sector. These were later converted to the Senior Executive Service (SES) with the passage of the Civil Service Reform Act of 1978. The SES pay system consists of 6 levels, the first being 120% of GS 15 step 1 and the highest pegged to Level IV of the Executive Schedule (EX IV). In recent years locality pay has been extended to apply to the SES and locality adjusted SES pay is now capped at EX III.

To this day the General Schedule still accounts for the largest share of the government's nearly $120 billion annual payroll and covers nearly 1.8 million part time and full time employees spread across more than 400 different occupations.

Recent Trends

Contemporary criticism of the General Schedule ranges from the dubious 30% underpayment "compared to" private sector salaries to the uncompetitive pay set at entry levels. Criticisms of the system include that it is too inflexible to reward or motivate outstanding performers, that it does not allow for accelerated career paths for some high tech or high demand occupations, that pay at the managerial levels is too low, and that pay compression at the top is created by the higher SES and EX pay levels. Some of the criticism is well founded though many problems could be mitigated using flexibilities allowed under existing civil service rules.

Nevertheless many agencies have turned to their authorizing committees over the past twenty years to seek relief from perceived pay constraints. In 1986 the financial regulatory agencies were given authority to establish separate pay systems outside of Title 5 USC in order to remain competitive with the institutions they were regulating. Soon the top pay scales in these agencies exceeded their counterparts in the civil service

by 30% to 50%. Recently, the Securities and Exchange Commission used similar arguments concerning its inability to hire and retain lawyers, accountants, and securities specialists to gain its own authority to establish an independent pay system.

In 1996 the FAA was removed from coverage under Title 5 USC and within two years air traffic controllers negotiated a three-year contract providing for salary increases of up to 30%. The IRS followed in 1998 with a reform bill that allowed the agency to establish a banded pay system and permitted the creation of up to ten highly paid positions supplemented by a performance bonus of up to 50% of salary. The Transportation Safety Administration was next in 2001 with full authority to establish an independent pay system, followed most recently by the creation of the Department of Homeland Security holding similar pay authority. Other examples exist and additional agencies are even now submitting requests for legislative exemptions to the current pay system.

The trend seems rather clear. In the absence of government wide pay reform agencies will continue to address this problem on a piecemeal basis.

What About Performance?

But what of performance, as in "pay for performance"? In the federal workplace pay and performance are addressed as two completely divorced concepts. Annual pay increases based on ECI are provided as automatic adjustments to the pay scales. Additional longevity pay increases of one pay step (approximately 3% of pay) are awarded annually, bi-annually, or every three years depending on how far along in grade the employee has progressed. Denial of a longevity increase is subject to appeal and thus they are considered automatic and very rarely denied.

With up to two increases per year, pay is viewed as an entitlement independent of an individual's performance. Performance is associated with behavior that may be rewarded with additional pay if the boss likes you. That kind of cynical view among federal employees has grown over time in the absence of any credible performance management or performance measuring system. With inflated performance reviews resulting in 80% to 90% of employees being rated as performing above average, it is not surprising that fellow employees wonder what criteria were used to determine who among them is to receive performance awards. The lack of transparency seriously undermines the credibility of current performance recognition procedures.

Furthermore, if an employee can receive a 6% to 7% pay increase annually (3% annual inflation adjustment plus 3.3% step increase plus 0.5% to 1.5% locality increase) without putting out special effort then a 1% or 2% performance bonus will not seem terribly significant. Performance bonuses must be comparable to or greater than annual pay adjustments if they are to be meaningful.

In spite of the cynicism, a large number of performance recognition programs and activities are in place across the federal government. The largest and most visible are the annual SES bonuses, ranging from 5% to 20% of salary, and the Presidential Rank

awards to Senior Executives (35% of salary for Distinguished Executives and 20% of salary for Meritorious.) For employees below the SES agencies use incentive awards, and special act cash awards to recognize individual accomplishments. These awards typically range from a few hundred dollars to a few thousand. Agency heads can authorize up to ten thousand dollars for an individual award while the Director of OPM can approve awards of up to $25,000. Awards in excess of $10,000 are very rarely proposed. In addition to cash awards agency performance recognition programs utilize large numbers of non-cash awards. All of these focus on special accomplishments rather than sustained performance and do not affect base pay determinations nor benefits based on base pay.

Performance -- Recent History

After a significant effort to strengthen performance management and link pay and performance in the 1980s, the last ten years witnessed a significant erosion and decline. The merit pay system that had been established following passage of the Civil Service Reform Act was allowed to languish until finally repealed in 1993. The GM system was a pay for performance system for GS 13-15 managers and employees. Steps in those grades were abolished to permit more rapid movement at grade based on individual performance. A pool consisting of a fixed percentage of GM payrolls was used to pay performance bonuses as well. The system operated like a pay banded system though the bands were very narrow (1 grade bands).

The GM system covered over 130,000 employees. Those that advanced quickly through their grade were pleased with the system. Those that did not constantly compared their progress with the step they would have achieved had they remained in a GS system. Over time the grumbles of the lesser performers exceeded the cheers of the high performers and the system was abolished. There are important lessons to be learned in the demise of the GM system about managing expectations in any pay for performance system.

By 1998 performance management in federal agencies was in full retreat. OPM regulated performance expectations downward by permitting agencies to place their employees into two level performance evaluation systems, i.e. pass-fail systems. By the year 2000 hundreds of thousands of federal employees had been moved from multilevel rating systems to the greatly simplified pass-fail ratings. Notable among federal agencies to move to "pass-fail" were the Social Security Administration and the Department of the Navy. While administration of "pass-fail" systems is indisputably easier than multi-level rating systems one must wonder how management at these agencies could undertake the task of making meaningful distinctions among employees for purposes of making awards or establishing pay. Unless of course the distinctions are based on non-performance factors such as say height, weight, color of hair, age, or the old standbys of seniority and personality.

What are the Options for Pay Reform?

A necessary condition for pay for performance is the existence of a robust performance management and recognition system. In the absence of meaningful distinctions in

performance among employees a perception is created that decisions are based on cronyism. Employees need to have confidence that performance evaluation systems will be transparent and administered fairly. Managers must be held accountable for making performance management systems work and not be rewarded for making them fail.

Pay Banding -- The preferred pay reform now appears to be pay banding. Pay banding was recently recommended by the National Commission on Public Service in its final report as the means to reforming the federal pay system. It offers the benefit of simplifying the classification requirements attendant to pay setting and in it's simplest form reduces the fifteen grades and ten steps of the General Schedule to four or five overlapping bands providing a continuum of salary options. It also provides the added benefit of resolving the entry level pay problems facing recruiters, it allows fast tracking for high performing employees, and it eliminates the mid career plateau by permitting a continuum of pay increases throughout each band.

Care must be taken however to manage the overall payroll since experience has shown that pay banded populations tend to drift to the top of the band over time producing payroll inflation. Early demonstrations resulted in 20% payroll inflation of banded systems after just four years of implementation. Furthermore, for pay-banded systems to be fully effective, the setting of pay at the bottoms and tops of each band must reflect labor market realities. Currently pay bands are tied to specific GS grade levels. These in turn are set by employment surveys without regard to turnover statistics (accessions, separations) or recruitment experience (applicant to vacancy ratios, qualified applicants to hires ratios) among federal agencies. Thus all of the shortcomings of "pay comparability" surveys are mapped into the pay bands from the outset.

SES Pay Band – The Administration in its 2004 Budget Proposal included a provision to consolidate the current 6 pay levels of the SES into one band. The lower level would be set at 120% of GS 15 step 1 and the top would be rise to EX II (currently $154,700). The proposed increase in top pay for senior executives will alleviate some of the compression sustained by 60% of today's senior executives at the current top of the pay scale (EX III). This recurrent problem of SES pay compression will persist as long as Congressional pay is tied to the Executive Schedule. Pay compression at the top ultimately radiates down to affect the top of the General Schedule. Eventually it creates a crisis in retention among the most senior employees. A periodic resetting of the top of the SES band as proposed by the Administration is a reasonable short-term fix to this problem.

Human Capital Performance Fund – The Administration has also proposed a hybrid pay for performance system for General Schedule employees. The Administration proposes to set aside $500 million dollars (about 0.5% of payroll) to be made available as additional pay for high performing individuals. The award would be based on an employees actual performance and the amount added to base pay as a performance based pay increase. The amount would be treated as basic pay for purpose of retirement and benefit calculations. The fund would be administered by OPM but would be available to agencies that establish performance management systems that permit meaningful distinctions in relative performance among employees. Since the fund is administered by OPM, agency

employees will know that the funding will be there and will not be cut to accommodate other agency needs.

Although modest in size, the Fund should serve as an excellent inducement to reverse the trend back to meaningful performance management at federal agencies. Performance systems that make meaningful distinctions among relative performance are a necessary precursor to participation in the OPM administered program. Based on subsequent experience the scope of the Performance Fund can be expanded.

"Superior Pay" – A number of agencies in recent years have been granted special authority to create positions compensated at $150,000 or higher, what I have called "superior pay". In effect the pay was set higher than Congressional pay but lower than the cabinet Secretary level. The number of such positions has been restricted to 10 or 20 in any given agency. This practice should be continued, keeping controls on the overall number of such positions, as a means of relieving the serious pay compression that periodically sets in at the senior levels of government as the result of linkages to Congressional pay. By creating these pressure valves throughout government Congress establishes needed precedents to lay a foundation to subsequently raise pay ceilings. One alternative to consider is to grant OPM statutory authority to establish these positions on an as needed basis. OPM could manage a government wide pool of perhaps 250 to 300 such positions and move them around agencies based on agency justifications.

Conclusion

Let me conclude by summarizing some key points. First, it is clear from the trend of the past fifteen years that federal agencies are seeking ways around Title 5 USC pay constraints. The pay system needs to be reformed either centrally or reforms will be achieved piecemeal. Based on past experience the top of the pay scale is likely to rise and individual pay levels will rise with it thereby inflating the overall payroll.

It will therefore be important to channel growth in pay in directions that produce the most return to the government and taxpayers. The growth should be channeled in the direction of performing employees. Federal agencies seeking authority to reform pay should therefore be required to institute robust performance management systems that produce meaningful distinctions in relative performance among employees.

Pay banding has proven to be a well received alternative to the current General Schedule but it must be carefully administered to avoid unnecessary payroll inflation. Rather than move to a sweeping government wide reform, agencies should be provided authority through OPM to implement pay banded reforms on their own timetables and suited to their specific workforce and mix of occupations.

Pay compression at senior levels is a recurring problem that is largely created by linkages of pay to the Executive Schedule. It is aggravated during periods when Congress is reluctant to vote itself a pay raise. The Administration proposal to move the SES into a single banded system capped at EXII of the Executive Schedule is a sound proposal.

Consideration should also be given to establishing a small pool of highly compensated positions to be managed by OPM to relieve pay pressures at the top of the pay scale.

That concludes my remarks and I would be happy to respond to any questions that you might have.

Mrs. DAVIS OF VIRGINIA. Thank you, Mr. Nesterczuk.

Mr. Mihm, I will start with you. Do Government agencies have the capacity to measure individual and group performance well enough to make pay-for-performance more than a guessing game or worse, a matter of favoritism?

Mr. MIHM. When we look across Federal agencies performance management system, we don't see the systems yet in place that will allow them to make those meaningful distinctions or to adequately measure individual performance. There are plenty of efforts underway in that regard. Some agencies are really making some enormous progress in that but we think there is plenty of work that virtually all agencies need to undertake in order to be able to these world class performance management systems in place.

Mrs. DAVIS OF VIRGINIA. You at GAO have an internal pay for performance system and it is pretty new?

Mr. MIHM. Yes. We started it as a result of legislation Congress granted us in 1980. In the year 2000–2001, we went through a rather fundamental change in updating that system. That is the new part, yes.

Mrs. DAVIS OF VIRGINIA. Is it too early to tell if it is a success?

Mr. MIHM. I am a homer for it, I like it, so yes, it is an overwhelming success.

Mrs. DAVIS OF VIRGINIA. Would everybody in your agency say that?

Mr. MIHM. In the true spirit of oversight, there are checks we have in place. There are employee attitude surveys that we take periodically to make sure that there is trust and confidence in the system.

One of the things we did going into it to try and make sure we wouldn't have problems in implementation at the back end is really drill employee involvement. In every step in the process, it was deep, it was serious and it was across the agency that employees were involved. We went to a focus of paying for core competencies, our employees were deeply involved in identifying the competencies that we would need to be successful in the future, validating those competencies and were subsequently assessed on those competencies.

While we are far from perfect and are always looking to update it and learn from others, we are quite confident and quite pleased with the progress we have made in the first year.

Mrs. DAVIS OF VIRGINIA. Is that how you got the employees to gain ownership in it, by getting them involved and letting them be a part of the process and determining how the system would work?

Mr. MIHM. Yes, ma'am. Fundamentally, that is what does it for you. You have to have employees involved. In fact, when we looked overseas at performance management systems and pay for performance, we saw instances where they crashed and burned because they did not get their employees and the unions, we are talking about the representatives of the employee unions, involved as well. They had to pull back and start all over again. There is simply no other way you can do it if employees don't feel a sense of ownership.

Mrs. DAVIS OF VIRGINIA. Mr. Stier, what do you think would be a proper timeframe for implementation of pay-for-performance?

Mr. STIER. Enough time to make it work. I think you have to do this in pieces and I think that starting with the SES—I think you can parallel track this—is a very good idea for some of the major reforms you are talking about. That is the leadership group. It is a small group you are talking about, 7,000 people total, governmentwide. If you can't get it right with your executives, then you are going to have a very difficult time doing it throughout the Government.

That doesn't mean that if the same system that is applied to the SES either across Government or the same system applied to the SES as to the General Schedule. I really do believe that you start there.

I also think you find your agencies that are ready. There are some agencies out there that have done significant work. GAO is a good source of information. I also think you need to provide an incentive to make this work. You need to incentivize the agencies to start focusing on their performance evaluation process and not only that, but the whole shebang, the objectives they have as an agency, how do they connect the overall agency objectives to the individual employee contribution. If you don't start that process now, it is going to be very difficult to ever get there.

I don't mean to be ducking your question but I honestly believe this is going to be a long-term process but you can get pieces of it done here and now.

Mrs. DAVIS OF VIRGINIA. It was a tough question.

Mr. Nesterczuk, I have one section of NASA in my district. One of the things I have heard from them is being able to employ, retain, recruit good folks. They proposed legislation that would give it more hiring and pay flexibility to help recruit and retain a quality work force. The labor unions have countered that bonus pay is a poor substitute for across the board pay increases that would reward the loyal workers instead of those who threaten to leave to extort more pay. How do you respond to that?

Mr. NESTERCZUK. I don't think it is a question of loyalty, it is a question of performance. We are not talking about 100 percent of the work force that needs to be rewarded and recognized. These recognition systems don't have to begin with the notion that gee, we have to make this work for 100 percent of the people. If you accept the notion that 70 to 80 percent of your work force is doing perfectly fine, needs a minimum amount of supervision, the work doesn't change drastically day to day, you can put them almost on automatic pilot. Clearly, interaction with a supervisor is called for to make sure everything is on track but it is that smaller number of employees that are essential to getting quick turnaround, critical jobs, some unknown circumstance drops into the middle of the workplace and not everyone is going to deal with it, just the handful of people. Those are the folks you need to incentivize. You need to focus your performance management systems on recognition of those key people.

The same applies to recruitment and retention. It is not a matter of retaining 100 percent of the work force because most of them are perfectly happy working at their level of competence in the environ-

ment they are in. You don't have to make special considerations for them. It is the ones that are critical to getting your job done that you need to make sure you take care of.

Mrs. DAVIS OF VIRGINIA. So do you think it is fair to pay people who are doing the same job different pay?

Mr. NESTERCZUK. If they are doing the same quality of work on the same job, they should be paid the same but there are other aspects. There is timeliness, quality, volume, doing extra work. Those are the differentiators within a group. Those are the people whose performance you recognize.

My experience is that in a group in a cohort, everyone knows who the extra special employee is. They are the person the employees go to when they don't want to talk to their supervisor about resolving a problem. Their view of it is, if the supervisor doesn't know who the star is, then the supervisor is not worth a damn anyway.

Mrs. DAVIS OF VIRGINIA. Thank you.

Mr. Davis.

Mr. DAVIS OF ILLINOIS. Thank you, Madam Chairman.

Let me ask each of you how do we determine relative importance of missions? This notion that if you are doing a job in one place, it may not be comparable to doing a job in another place? How do we make that distinction?

Mr. MIHM. I can start on that. As your question suggests, it is not easy to do at all. There are a number of ways we have seen organizations here and abroad have done it. One way is they try and tackle it directly, try and make judgments about those that are the more important or less important missions and success under those missions.

We have an example in our report about the Province of Ontario which starts at the provincial level and then tries to cascade it down throughout the entire province in government.

Here, what we often find is a focus on core competencies. That is, for each individual, normally an occupation group or grade, what are the particular competencies that would be needed that have been validated to be shown as leading to organizational results and then let us pay off those competencies, let us pay to the extent people exhibit those competencies and then let us pay to the extent that they achieve or contribute to the achievement of organizational goals.

In other words, here in the United States we often don't deal with that question directly. We don't try and make judgments across missions. We just make judgments on did the person exhibit the core competencies we are looking for and did they contribute to organizational goals as specified in a performance contract at the beginning of the assessment year?

Mr. STIER. Congressman Davis, I would like to add that I was moving away from the microphone out of respect for Chris, not out of fear of the question.

I would say, and I am not sure I fully grasp the entire range of your question.

Mr. DAVIS OF ILLINOIS. Let us say I am a physician and I am working for the Bureau of Primary Health Services and somebody

else is working for the Center for Disease Control. Are we comparable physicians?

Mr. STIER. I would say, Congressman Davis, that in some sense it is not dissimilar from the issues that face all organizations in this country or any market-based system. I think we have a situation with the Federal Government today that by and large is not sufficiently sensitive to the market. We need to have a pay system that is more market sensitive and more performance sensitive in order for the Government to be able to attract and keep the people it needs to get the job done.

I think in the specific example you gave for CDC, for example, we would need to ensure that CDC has the ability to pay either existing talent it has to meet that job or talent it does not have to attract that talent in order to be able to get its mission done. As an organization, the Partnership for Public Service believes that the Government would be much better served if it had a system that both provided the necessary resources to get the talent it needs and also a system in place to allow that talent to maximize its capacity to perform. That system would be one that recognizes and rewards excellence.

Mr. NESTERCZUK. I think there are two elements to that question as I see it. One is the apportioning down, cascading down of an agency's mission to various components of that agency and making sure they understand how it is they contribute to the overall mission of the agency. That way in that context, you can do a performance evaluation and the employee understands what it is that is expected in the overall context of the agency. It is the cascading down process first from the top of the agency.

The other aspect of that question I will take off from what Max responded, the question of market testing, the value of a physician in one context and one component versus another. That could change over time. In 1 year, the CDC could play a far more critical role in handling an epidemic or crisis than perhaps a local service physician in some remote community, public health service. So it is difficult to respond globally.

However, I don't have any problems with the notion of agencies establishing compensation systems independent of each other. That serves as kind of an internal market within the Federal community. God knows there are enough jobs in the private sector that have no comparability to the Federal Government and vice versa. We are trying to establish market comparisons with the private sector when a lot of our own occupations don't fit over there, so creating a market within the Federal Government has perhaps a very salutary benefit.

I would argue for you that to a certain extent we already have the beginnings of that in some of our occupations. For example, in law enforcement, there is a definite pecking order of agencies, with the FBI sitting on top and everyone who is in a law enforcement job series would love to wind up in the FBI but they might start at the Federal Building Service, perhaps move over to be a guard in the print shop in the Government Printing Office, then work their way up through the ranks through Customs or DEA or others.

There is a drift from some agencies and there is a pay differential that goes along with that, greater opportunities for career advancement as you go into different agencies. So we have a market in the Federal workplace but we don't reflect that in the pay structure.

Mr. DAVIS OF ILLINOIS. Am I understanding each of you to suggest that in order for pay-for-performance to work, employees must be intricately involved in devising the system?

Mr. NESTERCZUK. Yes, absolutely.

Mr. MIHM. Yes, and where they are involved, it works or can work and where they are not involved, it does not work.

Mr. DAVIS OF ILLINOIS. Thank you very much.

Mrs. DAVIS OF VIRGINIA. I just have one question for you, Mr. Nesterczuk.

We just went through the battle last year with the Homeland Security Act. Do you see that as a model for transitioning our Federal agencies into a more flexible personnel system? Do you believe that human resources is one of its successes or failures?

Mr. NESTERCZUK. I think there are better models. I think Chapter 47 of Title V, the demonstration project authority, sets out a number of rules of engagement so to speak, the parts of Title V Civil Service that you shouldn't touch that are kind of core and common to all versus the ones where perhaps there are better ways of getting the job done like pay or appeals processes, the classification system and a number of things where you are allowed to experiment.

I think using a Chapter 47 model to try to bring agencies together or to permit an agency to engage in a demonstration project is far better. We have 25 years of experience with that, it has worked in the past, it has tested legislative language. The experiences that I have seen with the FAA in 1996, the IRS in 1998 and TSA in 2001, where you basically tell the agencies start from scratch, although IRS wasn't quite scratch, the others were, can be very problematic for an agency.

The first day the FAA was out from under Title V it administratively reimposed all of Title V, all of those hideous rules and regulations of the Civil Service Code right back on itself because it couldn't start from scratch, it couldn't start from zero. So the Title V rules are a good starting point and the Chapter 47 allows you to drop and substitute various components and pieces of it as you mature, as you go along, as you gain experience. I think that is probably a far better model for reform.

Mrs. DAVIS OF VIRGINIA. Would you recommend that we do demonstration projects if we were to go more to reform?

Mr. NESTERCZUK. Yes. I would use Chapter 47 type language to allow OPM to extend pay reform authority to agency A once it submitted a plan, how it proposes to do it, why it wants to do it, etc., but this would be much broader. There would be restrictions, so you would need to lift some of those restrictions but the construct, that is what would propose. Let agencies come to OPM when they are ready to tackle it rather than go governmentwide because they all need to tailor it depending on the kinds of occupations they are dealing with, the kinds of turnover they got, recruiting problems, they need to tailor those things to their best needs.

Mrs. DAVIS OF VIRGINIA. You gentlemen agree? You are both shaking your heads yes.

Mr. Davis, do you have anything else for this panel?

Mr. DAVIS OF ILLINOIS. No.

Mrs. DAVIS OF VIRGINIA. Gentlemen, thank you very much for coming. I hope we didn't keep you here too long and I appreciate all the information you gave us.

I do apologize that we have a long hearing today but this is an issue we wanted to hear from everyone. Now we get to hear from the workers themselves. If I could get panel four to come forth.

For the fourth panel, we will go through the same drill, so if you will remain standing, we will administer the oath. Thank you all for being patient and waiting.

It is the subcommittee practice to ask witnesses to testify under oath, so if you will raise your right hands.

[Witnesses sworn.]

Mrs. DAVIS OF VIRGINIA. The witnesses will now be recognized for opening statements. We will ask you to summarize your testimony in 5 minutes and your full written statements will be included in the record.

I would like to welcome Colleen Kelley, national president, National Treasury Employees Union; Jacqueline Simon, public policy director, American Federation of Government Employees; Bill Bransford, counsel, Senior Executives Association; and Karen Heiser, Federal Managers Association. Thank you all again for being here today and for your patience.

Ms. Kelley, we will start with you and you will be recognized for 5 minutes.

STATEMENTS OF COLLEEN M. KELLEY, NATIONAL PRESIDENT, NATIONAL TREASURY EMPLOYEES UNION; JACQUELINE SIMON, PUBLIC POLICY DIRECTOR, AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES, AFL–CIO; BILL BRANSFORD, COUNSEL, SENIOR EXECUTIVES ASSOCIATION; AND KAREN HEISER, FEDERAL MANAGERS ASSOCIATION

Ms. KELLEY. Thank you very much, Chairwoman Davis and Ranking Member Davis.

On behalf of the 150,000 Federal employees represented by NTEU, we very much appreciate the opportunity to be here today with you.

The Federal Government has failed for many years now to invest in its most important resource, its employees. One of the original Volcker Commission conclusions in 1989 was that, "The gap between what government and the private sector pays has grown far beyond the point where government can hope to recruit and retain qualified staff."

Although the fiscal year 2003 Federal pay raise was recently settled, it did not come without a fight and the administration continues to show a lack of concern for what failure to properly compensate the Nation's public employees means for the future of public service by proposing a 2 percent pay increase sending the unmistakable message for 2004 that the work is not valued, vital and critical.

NTEU was very disappointed that the recent Volcker Commission report did not adequately address the problems with rank and file pay and we have reservations concerning the recommendations for more flexibility in setting Federal pay.

Pay for performance means something different to everyone. One thing is certain, however. Where pay-for-performance has been implemented, very complicated questions and concerns have been raised that have not yet been resolved.

The GAO recently released its study of the Federal Aviation Administration's market-based pay for performance system. When the GAO interviewed FAA employees concerning the new system, nearly two-thirds of the employees interviewed either disagreed or strongly disagreed that the new pay system is fair to employees.

Concerns about Federal supervisors and managers having more control in the pay-setting process are not unique to the FAA. A demonstration on pay banding at the Bureau of Alcohol, Tobacco and Firearms began in early 2000 with the first round of salary reviews set for that October. Managers received little or no training on writing pay for performance evaluations. Appraisals were then forwarded to a performance review board [PRB] which had the authority to downgrade evaluations. If the individual supervisor was unable to write a well documented appraisal, the employee suffered. The authority the PRB was given to downgrade evaluations led to the belief that the Bureau was operating with a fixed pool of money. Some employees had to have their evaluations lowered in order for others to receive pay raises. This perception of manipulation by management led to employee skepticism. A fair and unbiased performance appraisal system must be an underlying principle when judging employees.

In 1996, the House debated legislation to give more weight to performance appraisals in down-sizing situations. Members raised serious concerns about the lack of formal performance appraisal guidance and questioned their tendency to be subjective, unfair, overinflated and biased against minorities. The proposal was defeated.

Evidence also points to pay for performance schemes in the private sector producing poor results. Three years ago the Ford Motor Co. implemented a performance measurement program and unwittingly created a culture of backstabbing as employees tried to outdo one another instead of working together as a team. Instead of cooperation, the system fostered in-fighting and divisiveness.

Similarly, the Fairfax County, VA School District was forced to terminate its merit pay system when it became clear that teachers were being pitted against each other and cooperation and team work were discouraged. Moreover the school district's commitment to its merit system plan waned as soon as the program began costing money.

As I stated earlier, pay for performance means something different to everyone you ask. What is consistent, however, are the problems in designing a quality pay for performance system. Employees must be encouraged to work together rather than compete against one another. A system that promotes individual achievement over group effort is bound to create additional problems. A

pay for performance system designed to be used only when budgets are flush will breed contempt.

The performance evaluation system used to rate employees will fail absent employee feedback and commitment to the process and appropriate manager training in using the new system is key to ensuring the system will be perceived as valid.

In summary, NTEU believes that proposals to more closely link pay with performance must embody several core principles. Employees and their unions must be full partners in the design and implementation. Pay for performance is not cost neutral. Agencies must have adequate resources to implement a pay for performance system.

Proposed changes must be communicated effectively and clearly to employees. Development and implementation of a performance-based appraisal system must be subject to bargaining with employees and their unions and managers must be trained to provide fair and unbiased evaluations of employee performance.

Thank you again for the opportunity to testify and I look forward to any questions you might have.

[The prepared statement of Ms. Kelley follows:]



Testimony
of

Colleen M. Kelley
National President
National Treasury Employees Union

on

Federal Compensation Reform

April 1, 2003
1:00 pm

Subcommittee on Civil Service
Committee on Government Reform
2247 Rayburn Building

Chairwoman Jo Ann Davis, Ranking Member Danny Davis, thank you very much for the opportunity to appear before you today on the topic of federal employee compensation. I am Colleen Kelley, the National President of the National Treasury Employees Union (NTEU), and I appear today on behalf of the more than 150,000 federal employees and retirees represented by NTEU.

First, I want to offer my congratulations to you, Congresswoman Davis, on assuming the Chair of the Civil Service and Agency Organization Subcommittee. NTEU looks forward to working with you and your staff on the many issues likely to come before your Subcommittee in the coming months.

The topic of this hearing is extremely timely and I think it is safe to say that we all share the same goal – to take the appropriate steps to make the federal government an employer of choice. We must do a better job of retaining our current employees and the knowledge and skills they bring to the federal government while at the same time, taking the appropriate steps to entice a new crop of young leaders into public service.

The federal government has failed for many years now to invest in its most important resource – its employees. What we are seeing today is the effect of that failure. The first Volcker Commission issued its report more than a decade ago in 1989. One of

the original Volcker Commission's conclusions was that "the gap between what government and the private sector pays has grown far beyond the point where government can hope to recruit and retain qualified staff." The report continued, "if it (the federal government) is to remain a credible career choice, government simply cannot permit the purchasing power of federal pay to decline year after year and the gap between public and private pay for comparable jobs to widen."

In large measure, enactment of the Federal Employees Pay Comparability Act (FEPCA) in 1990 grew out of the Volcker Commission recommendations. Although it represented a fundamental change in how federal pay would be set, it too, has failed. FEPCA has failed because the resources necessary to make it successful were never forthcoming. Whether this Congress recommends reviving FEPCA or establishing a new pay system, a commitment must be made to commit the necessary resources to make it successful.

Unfortunately, the outlook for a fair and appropriate pay setting process for federal employees continues to be mired in politics. Although the Fiscal Year 2003 federal pay raise was recently settled, it did not come without a fight. While recommending an average 4.1% pay raise for the Nation's military employees, the President recommended only a 2.6% pay raise for federal civilian employees in 2003. A chorus of bipartisan and bicameral support in favor of pay parity between the Nation's federal civilian and military employees sprang up in Congress and a 4.1% pay raise was included in the FY 2003 Budget Resolution and subsequent appropriations measures.

Despite this display of bipartisan support, the President ignored Congress' intent and implemented a 3.1% pay raise for federal workers prior to the end of the last calendar year. When Congress returned to finish work on the 2003 appropriations measures early in 2003, it again restated its strong support for the minimum 4.1% pay raise for federal employees, a raise that will finally be provided to the Nation's civil servants retroactively in the coming weeks.

Unfortunately, the Administration continues to show a lack of concern for what failure to properly compensate the Nation's public employees means for the future of public service. In its Fiscal Year 2004 budget proposal, the Administration called for only a 2% pay increase for federal workers, sending the unmistakable message -- even to those employees on the front lines of helping secure the nation's borders -- that their work is not as important, not as valued, and not as vital as that of their military counterparts.

We cannot hope to solve the crisis in public service absent a commitment to establish a fair process for setting federal salaries. It is ironic that as frequently as critics of federal government employees claim to want to mold the federal government to be more like private sector employers, pay is one area they often don't seem interested in addressing with a private sector solution. Where would our country's best companies be if they set their employees' salaries without regard to the labor market within which they existed?

NTEU is grateful to you, Chairwoman Davis, for your leadership on this critical issue. Your willingness to contact Budget Committee Chairman Nussle in support of continuing the tradition of pay parity between the Nation's military and civilian workforces was instrumental in the Budget Committee's adoption of pay parity language as part of its Fiscal Year 2004 Budget Resolution. In fact, despite the Administration's opposition, both the House and Senate Budget Resolutions contain language supporting continued pay parity between military and civilian employees of the federal government in 2004. This is an important step in the right direction and one that NTEU heartily applauds.

NTEU was disappointed, however, that the recent Volcker Commission Report did not adequately address the problems with rank and file federal employee pay. While the report offered a number of recommendations in other areas, it failed to propose solutions to this core problem. While the Commission recommends increasing salaries for highly paid top ranking executives, it does not address the pressing need to establish a fair and credible process for setting federal pay to make government service more competitive with the private sector. Likewise, the report largely ignores the growing budget crisis that leaves federal agencies without the resources necessary to do the work expected of them by the American public. Front-line federal employees feel this lack of resources directly and are frustrated by the continuing necessity of doing more with less.

NTEU also has reservations concerning the Volcker Commission's recommendation for the federal government to adopt a pay system that offers agencies more flexibility in setting federal pay and more closely ties pay to performance. The term "pay for performance" has come to mean something different to just about anyone you ask. One thing that is certain, however, is that in places where some version of pay for performance has been implemented, complicated questions and concerns have been raised that have yet to be resolved.

The General Accounting Office (GAO) recently released its study of the Federal Aviation Administration's (FAA) 7 year overhaul of its pay and personnel systems. The FAA replaced its pay system, which had been based on the General Schedule grade and step system, with what it calls a market-based pay for performance system. When the GAO interviewed FAA employees concerning the new system, nearly two-thirds of the employees interviewed "disagreed, or strongly disagreed that the new pay system is fair to all employees." This sense of unfairness, and employees' view that they will not be treated equitably by their managers, has led a greater number of them to seek union representation – the percentage of the FAA workforce who are members of unions jumped from 63% to almost 80% following the implementation of the new pay system.

Concerns about federal supervisors and managers having more control in the pay setting process are by no means unique to the FAA. The group, FPMI Communications, undertook a poll of federal workers last October on the subject of pay for performance.

Fully two-thirds of the respondents in that poll believed that giving managers more authority on pay would lead to too much favoritism.

A demonstration on pay banding at the Bureau of Alcohol, Tobacco and Firearms (BATF) is another good case in point. The BATF program began in early 2000, with the first round of salary reviews scheduled for October of that year. Performance standards and critical job elements needed to be in place prior to implementation of the first salary reviews, however, insufficient thought was given to their development and haphazard standards resulted. As is far too frequently the case, managers received little or no training on how to write pay for performance evaluations for this new system. Although NTEU was given the opportunity to review and comment on the proposed standards, our suggestions largely went unused.

Under the BATF program, once performance appraisals were written by managers, they were forwarded to Performance Review Boards (PRBs) that further reviewed the evaluation and issued a final rating of employees. That rating was subsequently entered into a pay matrix that would determine whether or not the employee would be entitled to a performance based raise.

The PRB was given the authority to downgrade evaluations when compared to other employees in the same pay band and job series. And, in fact, evaluations were downgraded. Employees working for poorly trained managers who were, therefore, unable to write a clear, well-documented appraisal suffered under this

system. No matter how stellar their performance, if the individual's supervisor was unable to document that performance in a well-written appraisal, the employee would not be eligible for a performance increase. In addition, the authority the PRB was given to downgrade performance evaluations led to the belief among many of our members that the Bureau was operating within a fixed pool of money. In other words, some employees had to have their evaluations downgraded in order for others to receive pay raises. There is no question that this perception of manipulation of the process by management led to employee skepticism about the overall performance appraisal system.

Another feature of the BATF program was one that permitted employees to provide a self-evaluation as well as any external information regarding their individual performance that they thought would be helpful in their review. This could include customer letters or recognition by a professional association or other information the employee thought complimentary to his or her performance review. Although this part of the program was voluntary, most employees were given no training or guidance on developing these self-assessments, further leading to skepticism concerning the program.

While a fair and unbiased performance appraisal system must be an underlying principle in any pay for performance system, the same basic principles must be heeded when judging employees in other situations. In 1996, Congress strongly supported this principle during consideration of a proposal (H.R.3841) to give added weight to the use of performance evaluations during Reductions in Force (RIFs) of federal employees. Members of the House of Representatives raised serious questions

during floor debate on this bill concerning the lack of formal guidance for performance appraisals and questioned their tendency to be subjective. In a September, 1996 speech on the House floor, Representative Cardiss Collins, the Ranking Member on the House Government Reform Committee, stated "...performance appraisals are routinely challenged as being subjective and unfair, over inflated and biased against minorities." The proposal was soundly defeated. However, little has changed since 1996 concerning performance appraisals.

Evidence also points to pay for performance schemes in the private sector producing less than desired results, especially when implemented in large or complex organizations. Approximately three years ago, the Ford Motor Company implemented a Performance Management Program and unwittingly created a culture of backstabbing as employees tried to outdo one another instead of working as a team. Instead of cooperation, the system fostered infighting and divisiveness.

Individual employees were rated against each other and instead of working toward a common goal, employees became primarily focused on individual performance. The previous culture of team problem solving and risk taking gave way to a situation where employees were unwilling to make suggestions or propose solutions that might result in their being rated lower than their fellow employees. The federal government, much like Ford Motor Company, relies on employees working together to deliver results. Ford was forced to dismantle key components of their Performance Management

Program in the face of sinking employee morale. There are lessons here for the federal government as well.

Similarly, the Fairfax County, Virginia School District was forced to terminate its merit pay plan when it became clear that teachers were being pitted against each other and cooperation and teamwork were being discouraged. Moreover, the School District's commitment to its merit pay plan waned as soon as the program began costing the district money.

Merit pay awards in Fairfax County were scheduled to be 10% salary increases that would be included in base pay and counted toward retirement. When the time came to award these increases, the School Board, facing a budget crunch, reduced the merit raise amount from 10% to 9% and deemed it a bonus instead of a salary increase that would count toward retirement benefits. Still facing budget concerns, the Board subsequently abolished merit pay entirely.

The Texas legislature passed a merit pay law in 1984, but just like Virginia, they too, encountered fiscal problems and scaled back their program. When 100,000 teachers qualified for merit pay, the state changed the rules retroactively to reduce the number of qualified teachers by approximately one-third.

As I stated earlier in my testimony, pay for performance means something different to almost anyone you ask. What seems to be consistent across the board,

however, are the problems in designing a quality pay for performance system. Employees must be encouraged to work together rather than compete against one another. A system that promotes individual achievement over group effort is bound to create additional problems. A pay for performance system designed to be used only when budgets are flush will breed contempt for the system and will not work. Development of the performance evaluation system used to rate employees will fail absent employee feedback and commitment to the process. And, appropriate manager training in using the new system is key to ensuring that the system will be perceived as valid.

In summary, NTEU believes that any changes in pay setting procedures that are designed to more closely link pay with performance must embody several core principles. These include:

1) Stakeholders, including employees and the unions that represent them must be full partners in the design and implementation of any pay for performance system.

2) A Pay for Performance plan for the federal government must only apply to within-grade pay increases. Annual pay raises based on the increase in the Employment Cost Index (ECI) as well as locality pay raises must continue to apply to prevent federal salaries from slipping further behind private sector wages.

3) Pay for performance is not cost neutral. Failure to provide agencies with adequate resources to implement a pay for performance system will doom the system to failure.

4) Proposed changes must be communicated effectively and clearly to employees. Employee perceptions that pay for performance demonstration projects have not treated all employees fairly must be addressed and resolved prior to the implementation of any pay for performance system.

5) Development and implementation of a performance appraisal system must be subject to bargaining with employees and their union representatives.

6) Managers must be appropriately trained to evaluate employee performance. Writing a fair and unbiased performance appraisal requires a level of skill and sophistication that most managers in the federal government do not currently possess.

Thank you very much for this opportunity to appear before your Subcommittee. I would be happy to answer any questions.

Mrs. DAVIS OF VIRGINIA. Thank you, Ms. Kelley.

Ms. Simon.

Ms. SIMON. Madam Chair and Ranking Member Davis, I want to thank you very much for the invitation to testify today and specifically for your willingness to listen carefully to all points of view.

I appear today on behalf of the more than 600,000 Federal employees represented by AFGE. I will focus my remarks on two items. The first is an attempt to provide an accurate description of the General Schedule which has been maligned and mischaracterized beyond recognition by some advocates of pay-for-performance. The second will be to highlight many concerns AFGE has about individualized pay for performance systems.

The version of the General Schedule I will describe is one that was established as the result of the enactment of the bipartisan FPCA in 1990. FPCA introduced numerous flexibilities into the allegedly rigid and never changing GS system: locality pay differentials, special pay rates for certain occupations, critical pay authority, recruitment and retention flexibilities that allow hiring above the minimum step of any grade, recruitment, retention and relocation bonuses, payment of travel and transportation expenses for job candidates and new hires, allowing up to 2 weeks advance pay as a recruitment incentive, allowing time off incentive rewards, allowing cash performance-awards, waiver of dual compensation restrictions, changes to law enforcement pay, special occupational pay systems, and flexibilities for Title V health care positions and many more. In addition, FPCA retained the GS allowance for quality step increases, salary increases awarded on the basis of extraordinary performance.

The basic structure of the GS is a 15 grade matrix with 10 steps per grade. Movement within a grade or between grades depends on the satisfactory performance of job duties over time. That is, whether a worker gets a step increase depends on performance. The GS classification system also supports performance by determining the standards against which a worker's performance will be measured when opportunities for movement arise. Most important, the GS system is based upon the merit system principle of equal pay for substantially equal work, which goes a very long way toward preventing pay discrimination on the basis of race, ethnicity or gender.

Pay-for-performance is pushed by some on the basis of four unproven contentions: that it will improve productivity, recruitment, retention and will effectively punish poor performers. Even its proponents are reluctant to say that it will do anything at all to solve the real and longstanding fact that Federal salaries are too low across the board, the comparability problem that FPCA might have fixed over the past decade if it had been funded.

Do the pay systems that set out to reward some individuals for productivity improvement and punish others who are judged to have made smaller or negative contributions to productivity actually work? The facts suggest they do not. Research from academics without a financial interest in the outcome of the debate show that individualized pay-for-performance systems don't deliver on their promises and are notorious for eating up enormous managerial resources and making everybody unhappy.

More specifically, the research shows that pay-for-performance undermines team work, encourages a focus on the short term and leads people to sharpen their political skills and personal ties to the supervisor rather than to improve the mission of the organization. Individual pay-for-performance gives workers the incentive to make themselves look good and their co-workers look bad. It dissuades people from sharing knowledge and working cooperatively.

Since salary money always comes in a fixed pot, pay-for-performance becomes a high stakes competition between workers within a unit with one worker's gain being another worker's loss.

Pay consultants and personnelists love individual pay-for-performance because if administered in a way that uses even a pretense of fairness, it requires an enormous managerial and supervisory hierarchy. The Navy's China Lake system which some consider a worthy successor to the GS is an incredibly complex system with pages and pages of evaluation documents that each manager must fill out for each individual under him on an almost continual basis. Pay-for-performance advocates and contractors realize all this will have to be checked and rechecked for accuracy and completion for every single 1 of the 1.8 million Federal employees.

I will close by mentioning OPM's recent poll. Although AFGE felt that some of the questions in the draft we saw were biased in a way that would lead respondents to send a message of support for pay-for-performance, what they seem to have gotten instead was a message that employees are relatively satisfied with the existing pay system and do not hold their managers in adequately high regard to trust them with vast new powers and discretion over pay.

The only question that really needs to be asked of Federal employees is, are you willing to trade the annual pay adjustment passed by Congress which includes a locality adjustment and any step increases for which you are eligible for a unilateral decision by your supervisor every year on whether and by how much your salary will be adjusted.

AFGE supports the congressional attention toward the inadequacy of Federal pay. We support those who seek to reward Federal employees for excellence but rewards for extraordinary performance must be supplements, not substitutes, for a fully funded regular pay system.

Thank you very much and I would be happy to answer any questions.

[The prepared statement of Ms. Simon follows:]



STATEMENT BY

JACQUELINE SIMON
PUBLIC POLICY DIRECTOR
AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES, AFL-CIO

BEFORE

THE HOUSE COMMITTEE ON GOVERNMENT REFORM
SUBCOMMITTEE ON CIVIL SERVICE AND AGENCY ORGANIZATION

REGARDING

REPLACING THE GENERAL SCHEDULE WITH PAY FOR PERFORMANCE

ON

APRIL 1, 2003

American Federation of Government Employees, AFL-CIO
80 F Street, NW, Washington, D.C. 20001 * (202) 737-8700 * www.afge.org

Madam Chairwoman and Subcommittee Members:

On behalf of the more than 600,000 federal employees represented by the American Federation of Government Employees, AFL-CIO (AFGE), I thank you for the opportunity to testify today on the question of whether a shift from the General Schedule to some sort of "Pay for Performance" plan would be in the interests of taxpayers, agencies, and federal employees.

The buildup to this hearing has included an ideological campaign to impugn the General Schedule and create a sense that replacing it is an urgent need for our nation. The campaign has included an Office of Personnel Management (OPM) White Paper, General Accounting Office (GAO) condemnation and high-risk designation, a blue-ribbon commission's blessing upon the manufactured conventional wisdom, conferences by interested parties parading as disinterested experts touting "studies" that demonstrate the fatal shortcomings of the General Schedule and glories that await their own design for a new federal pay system.

The manufacturing of an echo chamber consensus on the need to replace the General Schedule with pay for performance has been impressive. Replacing the General Schedule, according to the ideological campaign, is the answer to the government's self-inflicted human capital crisis, the reason the Bush Administration has had to force agencies to privatize 850,000 federal jobs, and perhaps most absurdly, the best way to make sure the government succeeds in preventing further terrorist attacks. If only they could figure out a way to link the General Schedule with obesity, traffic jams, overcrowded schools, and prescription drug prices, perhaps even federal employees could be convinced.

Some of the campaign's signature slogans include the charge that the General Schedule is a system that rewards only "the passage of time" rather than performance, and that it is an anachronism designed for a late 19th and early 20th century government populated mostly by clerks and typists rather than the "information based" government of today. Neither charge is really true, but every good marketer knows that repetition breeds plausibility, and today they have at least the ring of truth. After all, the General Schedule does provide financial recognition for experience gained over time, and the federal government has had a pay system since the late 19th century, so the slogans aren't outright lies. They are, however, highly misleading.

In my testimony today, I will focus on both the broad question of whether individualized pay for performance is a wise choice for the federal pay system, as well as the specific system that has been rumored to have emerged as the favored candidate to replace the General Schedule, the Navy's China Lake Demonstration Project Pay for Performance Plan. The question of whether the China Lake Plan is a worthy successor to the General Schedule is a worthwhile one, especially in response to pay for performance advocates' usual practice of

limiting the discussion to whether a fantasized perfect model is preferable to the easily-maligned real system. In addition, I will discuss briefly the General Schedule, since it too deserves an accurate description so that proposed alternatives are not considered or evaluated against an easily dismissed or derided "straw dog."

The version of the General Schedule I will discuss is the one that was established as a result of the enactment of the bipartisan Federal Employees Pay Comparability Act (FEPCA) in 1990. Despite the insistence of some anti-General Schedule ideologues who claim that it is an aged and inflexible historical relic untouched by history, the fact is that the General Schedule has been modified numerous times, in some cases quite fundamentally. FEPCA's distinguishing feature, the locality pay system, has not even had a full decade of experience, since its implementation began only in 1994 after passage in 1992 of technical and conforming amendments to FEPCA that established both locality pay and Employment Cost Index (ECI)-based annual pay adjustments.

FEPCA introduced a panoply of pay flexibilities into the *allegedly* rigid and never-changing General Schedule:

- special pay rates for certain occupations
- critical pay authority
- recruitment and retention flexibilities that allow hiring above the minimum step of any grade
- paying recruitment or relocation bonuses
- paying retention bonuses of up to 25% of basic pay
- paying travel and transportation expenses for new job candidates and new hires
- allowing new hires up to two weeks advance pay as a recruitment incentive
- allowing time off incentive awards
- paying cash awards for performance
- paying supervisory differentials to GS supervisors whose salaries were less than certain subordinates covered by non-GS pay systems
- waiver of dual compensation restrictions
- changes to Law Enforcement pay
- special occupational pay systems
- pay flexibilities available to Title 5 health care positions, and more.

In addition, FEPCA retained agencies' authority for quality step increases, which allow managers to reward extraordinary performance with increases in base salary that continue to pay dividends throughout a career.

The basic structure of the General Schedule is a 15-grade matrix with ten steps per grade. Movement within a grade or between grades depends upon the satisfactory performance of job duties and assignments over time. That is, an employee becomes eligible for what is known as a "step" increase each year for

the first three years, and then every three years thereafter up to the tenth step. *Whether or not an employee is granted a step increase depends upon performance (specifically, they must be found to have achieved "an acceptable level of competence").* If performance is found to be especially good, managers have the authority to award "quality step increases" as an additional incentive. If performance is found to be below expectations, the step increase can be withheld.

The federal position classification system, which is separate and apart from the General Schedule and would have to either continue or be altered separately and in addition to any alteration in the General Schedule, determines the starting salary and salary potential of any federal job. As such, a job classification determines not only initial placement of an individual and his or her job within the General Schedule matrix, classification determines the standards against which individual worker's performance will be measured when opportunities for movement between steps or grades arise. **And most important, the classification system is based upon the concept of "equal pay for substantially equal work", which goes a long way toward preventing federal pay discrimination on the basis of race, ethnicity, or gender.**

The introduction of numerous pay flexibilities into the General Schedule under FEPCA was only one part of the pay reform the legislation was supposed to effect. It was recognized by President George Bush, our 41st President, the Congress, and federal employee unions that federal salaries in general lagged behind those in the private sector by substantial amounts, although these amounts varied by metropolitan area. FEPCA instructed the BLS to collect data so that the size of the federal-non-federal pay gap could be measured, and closed gradually to within 90% of comparability over 10 years. To close the pay gap, federal salary adjustments would have two components: a nationwide, across-the-board adjustment based upon the Employment Cost Index (ECI) that would prevent the overall gap from growing, and a locality-by-locality component that would address the various gaps that prevailed in specific labor markets.

Unfortunately, neither the Clinton nor the George W. Bush administration has been willing to comply with FEPCA, and although some small progress has been made, on average federal salaries continue to lag private sector salaries by about 22%. The Clinton administration cited, variously, budget difficulties and undisclosed "methodological" objections as its reasons for failing to provide the salary adjustments called for under FEPCA. The current administration ignores the system altogether, and for FY04 has proposed allocation of a fund with 0.5% of salaries to be allocated via managerial discretion. Meanwhile, the coming retirement wave, which was fully anticipated in 1990, has turned into a full-fledged human capital crisis due to highly irresponsible and untargeted downsizing and privatization in the intervening years, as well as a stubborn refusal to implement the locality pay system which was designed to improve recruitment and retention of the next generation of federal employees.

China Lake

The Navy's China Lake plan started out as a demonstration project under title 6 of the Civil Service Reform Act. It was initiated in 1980, modified in 1987, expanded in 1990, extended indefinitely in 1994 (made into a "permanent" alternative personnel system), and expanded again in 1995. The employees covered by the China Lake plan are approximately 10,000 scientists, engineers, technicians, technical specialists, and administrative and clerical staff—a workforce that is not typical of any government agency, or even a minority of work units in any one agency.

Although the China Lake plan is often referred to as a model for pay for performance, the rationale given to OPM at its inception, and to Congress in its progress reports, was to improve the competitiveness of salaries for scientists and engineers. Nevertheless, the China Lake model is a performance-based pay system that differs from the General Schedule in terms of its classification of jobs into pay bands that are broader than the grades and steps in the GS matrix. Thus it is often called a broadbanding system.

OPM's evaluation of the China Lake plan was positive. They judged it a success in improving overall personnel management at the two demonstration laboratories studied. OPM cited the "simplified delegated job classification based on generic standards" as a key factor in the demo's success, as the time spent on classification actions was reduced, and the official report was that conflict between the affected workers and management declined. In the 10-year period of evaluation, average salaries rose by 3% after taking into account the effects of inflation. The China Lake plan made an explicit attempt to link pay increases within its "broad bands" to individual performance ratings. Starting salaries were also "flexible" within the bands.

It is important to note that the China Lake demo predated the passage of FEPCA by a decade. Indeed, China Lake's experience was invoked throughout the debate over reforming the federal pay system in the years leading up to FEPCA's passage in 1990, and many of FEPCA's flexibilities were based upon positive experiences accumulating in the China Lake demo.

It is worth describing at length the mechanics of the China Lake pay for performance system, apart from its equally elaborate classification system. I do this in part to show how China Lake's design may be appropriate to some scientists and engineers, but not to all federal employees since many are in occupations and workplaces that place extreme or even total limitations on creativity, individual initiative, or individualized performance. I also include this description to show that administrative ease is <u>not</u> one of pay for performance's virtues if the pay for performance system attempts to build in safeguards that limit the role of bias, favoritism and prejudice, as has been attempted at China Lake.

Instead of the General Schedule's 15 grades, China Lake has five career paths grouped according to occupational field. The five occupational fields are Scientists/Engineers/Senior Staff, Technicians, Technical Specialists, Administrative Specialists, and General Personnel. Each career path has classification and pay levels under the broadband concept that are directly comparable to groupings of the General Schedule. Within each career path are included many types of jobs under an occupational heading. Each job has its own career ladder that ends at a specific and different point along the path. Each broad band encompasses at least two GS grades. The China Lake plan describes itself as being "anchored" to the General Schedule as a "reality check." For those keeping count, the China Lake broadband has at least as many salary possibilities as the General Schedule, and at most as many as 107,000, since salaries can really be anywhere between the General Schedule's minimum or maximum.

Movement along an individual career path is the key factor to consider, as the overall plan has been suggested as a pay for performance model. As such, it is important to note that although some individuals may have an opportunity to move up to the top of a career path, not all can. Each job has its predesignated "top out" level. The promotion potential for a particular position is established based on the highest level at which that position could be classified, but individuals' promotions will vary. Promotion potential for a given position doesn't grow just because movement is nominally based upon performance. The only way to change career paths is to win a promotion to another career path altogether, i.e. get a new job. One can move along a pay line, but one may not shift to a higher pay line.

The description of the China Lake system involves pages and pages of individualized personnel actions involving the classification and reclassification of workers, and the setting of salary and salary adjustments. It is certainly neither streamlined nor simple, and asks managers on a continuous basis to evaluate each individual worker on numerous bases. In terms of bureaucratic requirements, and a presumption that managers have the training, competence, available time, commitment, and incentive to be as thorough as this system expects them to be for every single employee under them, the China Lake plan seems unrealistic at best. Further, the plan lacks adequate opportunity for employees to appeal their performance appraisals and the attendant pay consequences.

Unlike some of the radical "at will" pay and classification systems advocated by those who believe that any rules or regulations or standards or systems constitute intolerable restrictions on management flexibility, the China Lake plan retains a requirement to tie salary to job duties and responsibilities, not an individual worker's personal characteristics.

General Schedule versus "Pay for Performance"

AFGE's invitation to testify today included a request to address the broad issue of pay for performance as it was addressed in the Volcker Commission report. The following represents AFGE's views on the question of whether replacing the General Schedule with a pay for performance system is appropriate or desirable.

The rationales offered by proponents of pay for performance in the federal government have generally fallen under one of four headings: improving productivity, improving recruitment prospects, improving retention, and punishing poor performers. Perhaps the most misleading rationale offered by advocates of pay for performance is that its use has been widespread in the private sector. Those who attempt to provide a more substantive argument say they support pay for performance because it provides both positive and negative incentives that will determine the amount of effort federal workers put forward. Advocates of pay for performance wisely demur on the question of whether pay for performance by itself is a strategy that solves the problem of the relative inferiority of federal salaries compared to large public and private sector employers. That is to say, when pay for performance is referred to as complying with the government's longstanding principle of private sector comparability, what they seem to mean is comparability in *system design*, and not comparability in salary levels.

Does a pay system that sets out to reward individual employees for contributions to productivity improvement and punishes individual employees for making either relatively small or negative contributions to productivity improvement work? The data suggest that they do not, although the measurement of productivity for service-producing jobs is notoriously difficult. Measuring productivity of government services that are not commodities bought and sold on the market is even more difficult. Nevertheless, there are data that attempt to gauge the success of pay for performance in producing productivity improvement.

Although individualized merit pay gained prominence in the private sector over the course of the 1990's, there is good reason to discount the relevance of this experience for the federal government as an employer. Merit based contingent pay for private sector employees over the decade just past was largely in the form of stock options and profit-sharing, according to BLS data. The corporations that adopted these pay practices may have done so in hope of creating a sense among their employees that their own self interest was identical to the corporation's, at least with regard to movements in the firm's stock price and bottom line. However, we have learned more recently, sometimes painfully, that the contingent, merit-based individual pay that spread through the private sector was also motivated by a desire on the part of the companies to engage in obfuscatory cost accounting practices.

These forms of "pay for performance" that proliferated in the private sector seem now to have been mostly about hiding expenses from the Securities and Exchange Commission (SEC), and exploiting the stock market bubble to lower actual labor costs. When corporations found a way to offer "performance" pay that effectively cost them nothing, it is not surprising that the practice became so popular. However, this popularity should not be used as a reason to impose an individualized "performance" pay system with genuine costs on the federal government.

Jeffrey Pfeffer, a professor in Stanford University's School of Business, has written extensively about the misguided use of individualized pay for performance schemes in the public and private sectors. He cautions against falling prey to "six dangerous myths about pay" that are widely believed by managers and business owners. Professor Pfeffer's research shows that belief in the six myths is what leads managers to impose individualized pay for performance systems that never achieve their desired results, yet "eat up enormous managerial resources and make everyone unhappy."

The six myths identified by Professor Pfeffer are:

(1) labor rates are the same as labor costs;

(2) you can lower your labor costs by lowering your labor rates;

(3) labor costs are a significant factor in total costs;

(4) low labor costs are an important factor in gaining a competitive edge;

(5) individual incentive pay improves performance; and finally,

(6) the belief that people work primarily for money, and other motivating factors are relatively insignificant.

The relevance of these myths in the context of the sudden, urgent desire to impose a pay for performance system on the federal government is telling. Professor Pfeffer's discussion of the first two myths makes one wish that his wisdom would have been considered before the creation of the federal "human capital crisis" through mindless downsizing and mandatory, across-the-board privatization quotas. Pfeffer's distinction argues that cutting salaries or hourly wages is counterproductive since doing so undermines quality, productivity, morale, and often raises the number of workers needed to do the job. Did the federal government save on labor costs when it "downsized" and eliminated 300,000 federal jobs at the same time that the federal workload increased? Does the federal government save on labor costs when it privatizes federal jobs to contractors that pay front-line service providers less and managers and professionals much, much, much more?

Salaries for the 1.8 million federal employees cost the government about $67 billion per year, and no one knows what the taxpayer-financed payroll is for the 5 million or so employees working for federal contractors. But as a portion of the total annual expenditures, it is less than 3%, according to Congressional Budget Office (CBO) projections. Regarding the relevance of low labor costs as a competitive strategy, for the federal government it is largely the ability to compete in labor markets to recruit and retain employees with the requisite skills and commitment to carry out the missions of federal agencies and programs. Time and again, federal employees report that competitive salaries, pensions and health benefits; job security, and a chance to make a difference are what draw them to federal jobs. They are not drawn to the chance to become rich in response to financial incentives that require them to compete constantly against their co-workers for a raise or a bonus.

Professor Pfeffer blames the economic theory that is learned in business schools and transmitted to human resources professionals by executives and the media for the persistence of belief in pay myths. These economic theories are based on conceptions that human nature is uni-dimensional and unchanging. In economics, humans are assumed to be rational maximizers of their self-interest, and that means they are driven primarily, if not exclusively by a desire to maximize their incomes. The inference from this theory, according to Pfeffer, is that "people take jobs and decide how much effort to expend in those jobs based on their expected financial return. If pay is not contingent on performance, the theory goes, individuals will not devote sufficient attention and energy to their jobs."

Further elaboration of these economic theories suggest that rational, self-interested individuals have incentives to misrepresent information to their employers, divert resources to their own use, to shirk and "free ride", and to game any system to their advantage *unless* they are effectively thwarted in these strategies by a strict set of sanctions and rewards that give them an incentive to pursue their employer's goals. In addition there is the economic theory of adaptive behavior or self-fulfilling prophesy, which argues that if you treat people as if they are untrustworthy, conniving and lazy, they'll act accordingly.

Pfeffer also cites the compensation consulting industry, which, he argues, has a financial incentive to perpetuate the myths he describes. More important, the consultants' own economic viability depends upon their ability to convince clients and prospective clients that pay reform will improve their organization. Consultants also argue that pursuing pay reform is far easier than changing more fundamental aspects of an organization's structure, culture, and operations in order to try to improve; further, they note that pay reform will prove a highly visible sign of willingness to embark on "progressive reform." Finally, Pfeffer notes that the consultants ensure work for themselves through the inevitable

"predicaments" that any new pay system will cause, including solving problems and "tweaking" the system they design.

In the context of media hype, accounting rules that encourage particular forms of individual economic incentives, the seeming truth of economic theories' assumptions on human nature, and the coaxing of compensation consultants, it is not surprising that many succumb to the temptation of individualized pay for performance schemes. But do they work? Pfeffer answers with the following:

> Despite the evident popularity of this practice, the problems with individual merit pay are numerous and well documented. It has been shown to undermine teamwork, encourage employees to focus on the short term, and lead people to link compensation to political skills and ingratiating personalities rather than to performance. Indeed, those are among the reasons why W. Edwards Deming and other quality experts have argued strongly against using such schemes.
>
> Consider the results of several studies. One carefully designed study of a performance-contingent pay plan at 20 Social Security Administration (SSA) offices found that merit pay had no effect on office performance. Even though the merit pay plan was contingent on a number of objective indicators, such as the time taken to settle claims and the accuracy of claims processing, employees exhibited no difference in performance after the merit pay plan was introduced as part of a reform of civil service pay practices. Contrast that study with another that examined the elimination of a piece work system and its replacement by a more group-oriented compensation system at a manufacturer of exhaust system components. There, grievances decreased, product quality increased almost tenfold, and perceptions of teamwork and concern for performance all improved.[1]

Compensation consultants like the respected William M. Mercer Group report that just over half of employees working in firms with individual pay for performance schemes consider them "neither fair nor sensible" and believe that they add little value to the company. The Mercer report says that individual pay for performance plans "share two attributes: they absorb vast amounts of management time and resources, and they make everybody unhappy."

One further problem cited by both Pfeffer and other academic and professional observers of pay for performance is that since they are virtually always zero-sum propositions, they inflict exactly as much financial hardship as they do financial benefit. In the federal government as in many private firms, a fixed percentage of the budget is allocated for salaries. Whenever the resources available to fund salaries are fixed, one employee's gain is another's loss. What incentives does this create? One strategy that makes sense in this context is to make others look

[1] "Six Dangerous Myths about Pay", by Jeffrey Pfeffer, Harvard Business Review, May-June 1998 v. 76, no.3, page 109 (11).

bad, or at least relatively bad. Competition among workers in a particular work unit or an organization may also, rationally, lead to a refusal on the part of individuals to share best practices or teach a coworker how to do something better. Not only do these likely outcomes of a zero-sum approach obviously work against the stated reasons for imposing pay for performance, they actually lead to outcomes that are worse than before.

What message would the federal government be sending to its employees and prospective employees by imposing a pay for performance system? At a minimum, if performance-based contingent pay is on an individual-by-individual basis, the message is that the work of lone rangers is valued more than cooperation and teamwork. Further, it states at the outset that there will be designated losers – everyone cannot be a winner; someone must suffer. In addition, it creates a sense of secrecy and shame regarding pay. In contrast to the current pay system that is entirely public and consistent (pay levels determined by Congress and allocated by objective job design criteria), individual pay adjustments and pay-setting require a certain amount of secrecy, which strikes us as inappropriate for a public institution. An individual-by-individual pay for performance system whose winners and losers are determined behind closed doors sends a message that there is something to hide, that the decisions may be inequitable, and would not bear the scrutiny of the light of day.

Beyond compensation consultants, agency personnelists, and OPM, who wants to replace the General Schedule with a pay for performance system? The survey of federal employees published by OPM on March 25 may be trotted out by some as evidence that such a switch has employee support. But that would be a terrible misreading of the results of the poll. AFGE was given an opportunity to see a draft of some of the poll questions prior to its being implemented. We objected to numerous questions that seemed to be designed to encourage a response supportive of individualized pay for performance. We do not know whether these questions were included in the final poll. The questions we objected to were along the lines of: Would you prefer a pay system that rewarded you for your excellence, even if it meant smaller pay raises for colleagues who don't pull their weight? Do you feel that the federal pay system adequately rewards you for your excellence and hard work? Who wouldn't say yes to both of those questions? Who ever feels adequately appreciated, and who doesn't secretly harbor a wish to see those who *appear* to be relatively lazy punished? Such questions are dangerously misleading.

The only question which needs to be asked of federal employees is the following: Are you willing to trade the annual pay adjustment passed by Congress, which also includes a locality adjustment, and any step or grade increases for which you are eligible, for a unilateral decision by your supervisor every year on whether and by how much your salary will be adjusted?

It is crucial to remember that the OPM poll was taken during a specific historical period when federal employees are experiencing rather extreme attacks on their jobs, their performance, and their patriotism. The Administration is aggressively seeking to privatize 850,000 federal jobs and in many agencies, is doing so in far too many cases without giving incumbent federal employees the opportunity to compete in defense of their jobs. After September 11, the Administration began a campaign to strip groups of federal employees of their civil service rights and their right to seek union representation through the process of collective bargaining. The insulting rationale was "national security" and the explicit argument was that union membership and patriotism were incompatible. Some policy and lawmakers used the debate over the terms of the establishment of the Department of Homeland Security as an opportunity to defame and destroy the reputation, the work ethic, loyalty, skill and trustworthiness of federal employees. And out of all of this has come an urgent rush to replace a pay system based upon objective criteria of job duties, prerequisite skills, knowledge, and abilities, and labor market data collected by the BLS with a so-called pay for performance system based on managerial discretion.

In this historical context, federal employees responded to a survey saying that they were satisfied with their pay. In fact, 64% percent expressed satisfaction and 56% believed that their pay was comparable to private sector pay.

But as the representative of 600,000 federal employees, AFGE would suggest that they are satisfied with their pay system, not their actual paychecks. Since the alternatives with which they have been threatened seem horrendous by comparison, expression of satisfaction with the status quo in a survey sponsored by an agency determined to give managers discretion or "flexibility" over pay is no surprise.

Perhaps more important for the subject of pay for performance in the context of the survey is the fact that 80% report that their work unit cooperates to get the job done and 80% report that they are held accountable for achieving results. Only 43% hold "leaders" such as supervisors and higher level management in high regard; only 35% perceive a high level of motivation from their supervisors and managers, and only 45% say that managers let them know what is going on in the organization.

In this context, it seems reasonable to ask if the majority of employees are relatively satisfied with their pay, why the frantic rush to change? If federal supervisors and managers are held in such low regard, how will a system which grants them so much new authority, flexibility, unilateral power, and discretion be in the public interest? How will a pay system that relies on the fairness, competence, unprejudiced judgement, and rectitude of individual managers be viewed as fair when employees clearly do not trust their managers? Given that less than a third of respondents say managers do a good job of motivating them,

is pay for performance just a lazy manager's blunt instrument that will mask federal managers' other deficits?

No discussion of federal pay is complete without consideration of funding. To the extent that pay for performance is proposed as a replacement for the General Schedule that would be "budget neutral" and exclude additional funding, AFGE will work in opposition. Federal salaries are too low, and they are too low not just for prospective employees, or employees in "hard to fill" positions or employees who intend to stay in government for short periods – federal salaries are too low for all federal employees. There may be legitimate disputes about the size of the gap between federal pay and non-federal pay, but it is indisputable that federal salaries are too low across-the-board.

AFGE is supportive of Congressional attention toward the inadequacy of federal pay. We are also supportive of those who are looking for ways to reward federal employees financially for excellent and extraordinary performance. But at the same time we must caution that rewards for excellence and extraordinary acts must be supplements to a fully funded regular pay system, not substitutes; and these supplements must be fully and separately funded.

We are also highly concerned about the introduction of managerial discretion over pay in the context of recent aggressive attempts on the part of this administration to disparage and dismantle important elements of the merit system and provisions of title 5 which protect federal employees from discrimination in hiring, firing, pay, classification, performance appraisal, and which provide for collective bargaining. The current system makes sure that winning a federal job is a matter of what you know, not whom you know. The current system makes sure that the salary and career development potential of that job are a function of objective, job description criteria, not a manager's opinion of an individual worker's "competency" or skin color, gender, religion, age, political affiliation, or union status. Deviations from these protections are not warranted. Our nation has prospered and our government programs have benefited from having a professional, apolitical civil service that is strongly protected from corruption and discrimination. Introducing individualized pay systems that grant enormous power to federal managers regarding pay represents a grave danger to this protection.

The advocates of pay for performance in the federal government have the burden of demonstrating exactly how and why the General Schedule prevents federal managers from managing for excellence and productivity improvement. They must demonstrate exactly how and why each of the merit system principles will be upheld in the context of political appointees' supervision of managers who will decide who will and will not receive a salary adjustment, who will receive a higher salary for a particular job and who will receive a lower salary for the same job. They must demonstrate exactly how and why individualized pay for performance is superior to systems that provide financial reward for group and

organizational excellence. They must demonstrate exactly how and why paying some people less so that they can pay others more will contribute to resolving the federal government's human capital crisis and attract the next generation of federal workers to public service. They must demonstrate exactly how and why agencies will invest in the training, oversight, and staffing necessary to administer elaborate, federal employee by federal employee pay for performance plans fairly and efficiently. And they must demonstrate that they will be able to secure adequate funding so that pay for performance does not degenerate into a false promise, where discretion is exercised to award higher salaries only to recruit and/or retain particular individuals rather than to reward actual performance.

This concludes my testimony, and I would be happy to answer any questions Members of the Subcommittee may have.

Mrs. DAVIS OF VIRGINIA. Thank you, Ms. Simon.

Mr. Bransford.

Mr. BRANSFORD. Thank you, Madam Chair and Mr. Davis.

On behalf of the Senior Executives Association, we appreciate the invitation to testify this afternoon on the subject of Federal pay. We also appreciate your allowing me to testify at the last minute in place of Jerry Shaw who was unable to be here.

SEA is the only organization that represents the interests of career senior executives and I will comment today on matters of concern surrounding the executive pay system. The more detailed remarks of Jerry Shaw and supporting documentation have been submitted for the record.

Pay compression, which you have already heard about this afternoon, is a longstanding problem in executive pay ranks that hopefully will be relieved this year. The problem has been caused by the existence of a pay cap on executive pay that has not increased in 5 of the last 10 years because Congress did not vote itself a pay raise. This caused salaries at the bottom of the executive corps to rise but the top stayed constant. Today, nearly 70 percent of senior executives are paid the same.

The administration has proposed to lift the caps on base pay and locality pay one level for each. If enacted, this will result in an increase in the cap that limits locality pay from $142,500 to $154,700. We welcome this proposal from the administration and look forward to the bill Senator Voinovich is about to introduce that includes the administration's provisions.

As I will explain in more detail, we do have some concerns about some parts of the administration's proposal and we do seek some adjustments.

In addition to lifting the pay cap, the administration also proposes to eliminate SES pay levels of which there are now six and to replace them with one pay band with a minimum pay of $102,000. Agencies would only be able to pay salaries in excess of the old cap if they have a certified performance appraisal system. The administration's proposal contains no provision preventing reduction of SES pay.

We have the following concerns about the administration's proposal. First, we support executive pay banding but we believe three bands would be better for management of the SES than one broad band. The nature of SES positions and the experience level of executives varies and we believe this justifies having distinguishing characteristics in the SES system other than simply the amount of salary.

Second, we do not support lowering the minimum base pay from its current $116,500 to $102,000 as proposed by the administration. We believe this unnecessarily cheapens and degrades what should be a prestigious corps. We suggest that senior executives should make more than GS–15s and that someone who is appointed to the SES should be paid consistent with historical patterns. We also note that reducing the minimum SES pay at the same time that efforts are being made to recruit more minorities and women into the SES could be viewed as having a discriminatory effect.

Third, OPM has announced its intention to allow SES salaries under the new cap only for those agencies that have a certified per-

formance appraisal system under OPM and OMB regulations. This certification would be for 2 years but could be revoked at any time. We support a system that makes meaningful distinctions based on relative performance but we urge that it be administered only by OPM and that once certified, an agency could rely on the certification for 4 years, not the up to 2 years as currently required. We seek to exclude OMB from the process to prevent undue politicization.

Fourth, we ask that there be no pay cap on locality pay. We see no reason to artificially limit locality pay granted to every other Federal employee. A cap on locality pay will just create a new form of pay compression.

Fifth, we propose a new method for adjusting the pay cap be implemented so that the cap on base pay is increased each year by the amount of the annual GS pay increase. This will not result in an automatic pay raise, just the authority to pay it and we note this is consistent with the Volcker Commission report that talks about executive pay and congressional pay being developed separately.

Sixth and last, we ask that safeguards be implemented on reduction of SES pay. We propose that reductions of up to 3 percent be allowed with a review by the agency performance review board as is current practice and that reductions greater than that be reviewed by the MSPB. Reductions in pay currently are simply not subject to any appeal by senior executives.

These reforms we suggest are not difficult or cumbersome. They meet the administration's stated concerns of pay for performance and not granted an across the board pay increase. We urge the rapid consideration of the administration's executive pay proposal as modified by our proposals to provide appropriate safeguards and system adjustments to protect the integrity of the SES and to prevent it from being politicized.

Thank you for the opportunity to present our views.

[The prepared statement of Mr. Shaw follows:]



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TESTIMONY
of

G. JERRY SHAW

General Counsel

Before the

HOUSE SUBCOMMITTEE ON CIVIL SERVICE AND AGENCY ORGANIZATION

April 1, 2003

The Senior Executives Association (SEA) is appreciative of the opportunity to present testimony before the Subcommittee and is grateful to the Chairman and the members of the Subcommittee for devoting their time and efforts to address what we believe is a deepening crisis in the civil service.

My testimony will be limited to those pay issues specifically affecting the career executive corps since SEA is the only organization representing its interests. The primary issue to be discussed today is the problem of pay compression and its solution.

These are the regrettable facts: SEA was founded in large part due to the severe pay compression which existed in 1980, we have had to return to this issue over and over during the last 23 years, and, today, we find ourselves in an even worse position with regard to pay. Indeed, pay compression has reached such critical proportions that, unless corrected, it threatens to destroy the Senior Executive Service.

After being frozen five of the last ten years, the pay cap has filtered down through the ranks of the SES and approximately 70% of all career executives receive the same pay. In 1994, total pay at the ES-6 level was capped in one locality. This year, however, ES-4, ES-5, and ES-6 (the top three ranks) are all capped at Executive Level III (the statutory maximum for SES base plus locality pay) in all 32 localities. Likewise, ES-3 is now capped in 15 localities. In Houston and San Francisco, even ES-2 is capped and receives the same pay as the top rank of the SES. (See 2003 Pay Chart, Attachment I.)

If the Executive Schedule (which sets the statutory maximums for the SES) had mirrored the General Schedule national comparability raise since 1994, EL-II (the pay rate for Members of Congress) would be $ 171,000 this year instead of $154,700.

This situation is unfair and would be unthinkable in any private sector corporation, yet both the Administration and Congress have tolerated it. Finally the Administration has proposed some relief, and Senator Voinovich is moving toward introducing legislation in the Senate that will help. SEA welcomes the Administration's proposal and the action in the Senate but does have concerns about the Administration's proposal, which we will address.

Pay Compression Concerns

We believe it is instructive to consider the underlying concerns and attitudes, which form the arguments that have hindered resolution of the pay problem and may continue to prove troublesome, even with the Administration's changed position.

First, the pay problem is viewed by some as overblown because career executives are not retiring in record numbers. While executives may not be retiring in record numbers, many are prepared to retire as soon as they are eligible.

- Many will retire because they are demoralized by the failure to solve the pay problem - which signals they are not valued - while they continue to face extraordinary managerial and program demands at their agencies.
- Many will retire because they are unable to continue resisting very attractive offers from private industry (and to justify doing so to their families).
- Many will retire because they know that, in retirement, they will see greater increases in their annuities than they have seen in their pay. From 1994 to 2001, the average annual COLA adjustment on retirement annuities was 2.5%, higher than the average SES pay increase of 1% over those years.
- Those who have stayed on after September 11, feeling a sense of responsibility to their agencies and their country, cannot be expected to do so indefinitely.

And it is worth noting that, as more and more executives are covered by FERS, and not the "golden handcuffs" of CSRS, there will be even less incentive to remain in such conditions as exist at present.

With the number of executives projected to be eligible to retire by fiscal year 2005 (fully 70% of the corps) and with the critical challenges facing the Federal government, the question which must be asked is - can we afford to wait until the ranks of the career corps are depleted before resolving the pay problem? This is a dangerous game to play.

It is particularly dangerous because of the impact it is having on the "feeder" groups of GS-14's and 15's who could be expected to take the place of these executives.

To understand the human impact of this problem, we point to one Justice Department executive's words to SEA that summed up the problem:

> "I love and believe in the mission of government and the importance of having bright, caring and responsible people serving that mission. As an executive nearing retirement eligibility and feeling very burned out by pay stagnation and the compromises it has forced on those I love, I am trying desperately to do the succession planning my office will need to manage in the years to come. I never thought that I would be considering leaving on (my retirement) eligibility (date), but now I project I will. I feel I have no choice if I am to provide adequately for my family. I have never been so disheartened at the possibilities - my best and brightest repeatedly advise me that they see no future for themselves in government despite their love for it and commitment to it."

Second, some view the cost of resolving executive pay compression as inhibiting. The fact is that in 2002 the Congressional Budget Office stated the first year cost of

implementing new pay caps as $24 million, hardly a prohibitive price to pay to keep the talent in government that we need.

Third, some view resolution of pay compression as an effort to provide comparability with private industry and view data indicating a government/private industry pay gap as flawed. SEA has never argued for - and neither would career executives expect - comparability with private industry. However, the cost of public service has become too high and represents an unreasonable sacrifice. Rather, there should be a reasonable relationship between the two sectors.

To understand how government executives compare with their private sector peers, SEA contracted with the Hay Group from 1993 to 1996 to conduct annual studies comparing compensation of SES positions with that of comparable positions in private industry. A representative sample of SES positions was selected (across a range of agencies, SES pay rates, and functions) from Hay's data bases of SES evaluated positions. Using Hay's job content evaluation points, SES positions were compared to their precise counterparts which Hay had evaluated in a wide variety of industrial organizations and service industries, as well as in some nonprofit organizations and local governments.

These precise comparisons of government executives' pay to that of their exact counterparts in private industry provide data which is not open to the criticisms directed at other, more general pay studies.

Results from the 1996 study, "Comparative Analysis of SES Base Salary, Total Annual Cash Compensation, Benefits and Total Remuneration," were as follows:

- Average SES total cash compensation (including bonuses) ranged from 42% to 68% of that of average industry total cash compensation for jobs of the same difficulty.

- Put another way, SES total compensation for these positions would have to be increased by a range of 46% to 137% to attain comparability with private industry.

SEA discontinued supporting these studies because the four that were conducted showed a gap that was steadily increasing each year and that was not expected to be reversed.

Fourth, a resolution of pay compression is viewed as providing inappropriate across-the-board increases, as contrasted to providing "pay for performance." First, we are compelled to note that pay compression did not build because of poor performance by the executive corps; it built because of the unwillingness of Congress to either abide by the annual pay adjustment provisions of the Ethics Reform Act or to exempt just itself from annual adjustments and permit them to be applied to the rest of the Executive Schedule.

Second, and even more important, SES is a pay for performance system. In fact, it can be viewed as a model pay for performance system. The current performance management system gives agencies the flexibility and discretion they need to ensure that they can use performance information to adjust pay and to reward (or penalize) executives, as appropriate.

An executive's pay rank can be increased to reward his or her performance, and that performance can also be recognized by payment of an annual bonus, as well as by awarding a Presidential Rank of Distinguished or Meritorious Executive. The bonuses are totally at the discretion of the agency head, are granted or denied totally on the basis of performance, and do not constitute pay increases, but rather recognize the accomplishments of an executive in a given year. At present, there is suspicion that the bonus system is being used as a pay supplement in some agencies. While the Senior Executives Association strongly prefers to resolve pay compression head on, rather than relying on bonuses, the use of bonuses as a pay surrogate is not unexpected or unreasonable under the circumstances.

Apart from the ability to reward performance, however, agencies are free to reduce an executive by one pay rank each year and are only required to provide a reason for doing so. In the small percentage of cases when an agency must deal with a poor or non-performer, the agency need only be willing to take the performance appraisal process seriously.

In fairness, that requires that the executive be given 1) performance standards which reflect the agency's goals and the superior's expectations, 2) an opportunity to meet those standards and 3) feedback during a progress review. Indeed, the current performance management system provides for precisely this process, however, a 1999 survey of Senior Executives conducted by the Office of Personnel Management in cooperation with SEA found that 8% of all career executives did not have a performance plan and 14% had a performance plan developed 2 or more years ago.

Further, the current system gives agencies virtually unfettered and unreviewable discretion to remove non-performing Senior Executives from the SES. That is so because the statute allows, and in some cases requires, removal of an executive who receives an unsatisfactory performance appraisal. An executive who receives an unsatisfactory annual summary rating must be reassigned or transferred within the SES but also may be removed; an agency MUST remove from the SES an executive who receives two unsatisfactory annual ratings in any 5 year period. Underlying the agency's authority to deal with non-performers is the fact that performance appraisals and ratings are not appealable.

To the degree that these tools have not been used to fully realize the "pay for performance" nature of the SES, then only one conclusion is possible - political appointees and other superiors who supervise Senior Executives do not have the disposition, or are unwilling to

invest the time and energy, to use the tools at their disposal. And no amount of process or structure changes will magically cause them to do so.

Fifth, some view the tie with congressional pay as presenting an insurmountable barrier to resolving pay compression. Resolving compression should not relate to congressional pay. This is the finding of the Volcker Commission Report and if SEA's proposals, which we discuss today, are adopted, current Senior Executive base pay will still be less than Congressional pay, and reasonable and certain provisions for future pay cap increases will assure this problem is not revisited again any time soon.

Sixth, some believe that pay compression is best resolved by providing special pay schemes on an agency or occupational basis. As a result, for example, the Internal Revenue Service has authority to pay 40 employees (who must come from outside the agency or the government) up to the salary of the Vice President, and the Securities and Exchange Commission has recently been given authority for a separate pay system.

SEA opposes such solutions. First, the proliferation of such special authorities continues a piecemeal attack which does nothing to address a pay problem which is most severe in the SES ranks government-wide. To the contrary, it removes any impetus that does exist for addressing pay compression.

Second, special authorities are sometimes justified by the need to bring higher priced talent in from outside government, as in the IRS. Thus, we are apparently content, on the one hand, to continue to drive experienced, talented executives out of government by our refusal to address pay compression and, on the other hand, to recruit higher paid executives from outside government. The message we send to federally "grown" executives is that they are worth less than those hired from outside government, that they have erred in devoting their careers to public

service. We fail to see the wisdom of this solution and urge, instead, addressing the overall executive pay problem.

There is a paradox here upon which we am compelled to comment. Ever since the establishment of the Senior Executive Service by the Civil Service Reform Act of 1978, OPM and others have regularly bemoaned the failure of the SES to produce a corps of generalist executives - and have regularly suggested the removal from the SES of executives with technical or professional skills and competencies. Yet special pay authorities often would reward exactly such executives, provided they are recruited from the private sector.

The Administration's Proposal

The Administration has recently proposed raising the base pay cap to Executive Schedule Level III and the locality pay cap from Executive Schedule Level III to Executive Schedule Level II. In essence, this would raise the locality pay cap from $142,500 to $154,700. The proposed budget also seeks to eliminate the current Senior Executive Service ES 1 to 6 pay level system, replacing it with one band of pay for the SES. Under the Administration's plan, the increased payments that would be allowed by raising the two pay caps would be available only to those agencies which have a certified performance appraisal system that makes meaningful distinction based on relative performance. This would be done through OPM regulations that would implement a similar provision imposed last year by the Homeland Security Act that lifts the pay cap for overall compensation (including bonuses, awards and allowances) only for those agencies which have a certified performance appraisal system. OPM has stated its intention to promulgate regulations imposing a similar requirement before agencies could pay salaries under the new raised pay caps.

The lowest base pay of the planned band would be $102,000, with the highest base pay being Executive Level III or $154,700. Increases in pay, including annual comparability increases, would be at the discretion of a supervisor. The Administration proposal is silent with regard to decreases in pay except that officials have said that there will be no decreases during the first year. However, there is nothing in the proposal itself that prohibits decreases in pay after the first year implementation of the plan, and other provisions of law fail to provide appeal rights to Senior Executives whose pay is reduced. This differs from all other Federal employees who do have rights of review if they suffer a pay reduction.

SEA's Recommendations

To address all of the above concerns and to respond to the Administration's recent proposal to lift pay caps, the Senior Executives Association proposes the following amendments to the Administration's plan:

1. The SES (Senior Executive Service) cap for base pay should be raised to Level III, as proposed. The cap on locality pay, however, should be eliminated, ensuring that executives receive full locality pay adjustments. Eliminating a cap on locality pay is consistent with the Volcker Commission Report and would prevent further pay compression based on the new locality pay cap.
2. The language at 5 U.S.C. section 5307 (concerning the cap for overall compensation that includes bonuses and awards) introduced as part of the Homeland Security Act and calling for certified performance appraisal systems should be reformed so that: (1) only OPM –and not OMB–promulgates the implementing regulations; (2) once certified, the certification cannot be removed for a four year certification period; and (3) the certified system cannot use a forced distribution. OMB should be excluded from participating in the process for

certifying a performance system for career executives based on danger of partisan politicization of the system.

While the current statutory language proposed in the President's budget does not contain an explicit provision requiring a certified performance appraisal system before implementing a salary increase based on the new pay caps, as stated above, OPM has announced an intention to impose these types of requirements before an agency could pay higher salaries. SEA will support certified performance appraisal systems as a condition for implementing an increase in salary caps so long as: (1) all bonuses and awards for executives are included in the pay computation for computing retirement annuities (this would institute a true pay for performance compensation system); (2) the regulations implementing the process come only from OPM and not OMB; (3) forced distributions are prohibited; (4) once certified, the certification cannot be revoked until the end of the 4 year certification period; and (5) upon certification, no executive experiences a reduction in salary. If an agency loses its certification, pay that was set while its system was certified will not be reduced.

3. Senior Executives and all equivalent executives (including SL, ST, and BCAJ) should automatically receive the same annual increase to base pay that the General Schedule receives each year, regardless of the base pay cap (e.g., the 3.1% or 4.1% for this year and the 2% plus schedule for next year). Such annual increases should not be at the discretion of supervisors.
4. The pay cap for base pay should be raised each year by the amount of the annual comparability increases (projected in the President's budget at 2% in 2004). This would be without regard to what Congress does for its own pay or the pay of the Executive Schedule.

5. The wide range of $102,000 to $154,700 proposed by the Administration for SES pay should be abandoned and replaced it with three overlapping pay bands. The lowest base pay within pay band 1 (the lowest level) would be at the current minimum rate for ES-1, $116,500, an amount that is at least sufficient to give a reasonable pay raise to a GS-15/10 who is promoted into the SES.

   Senior executives would receive promotions to pay bands 2 and 3 based on standards in OPM regulations that reward executives for demonstrated capabilities, attained executive experience, and level of assumed responsibility. The ranges of pay for band 2 would overlap band 1 at the bottom and band 3 at the top. Pay band three would be set so that its highest base salary is Executive Schedule Level III. Executives would receive full locality pay on top of base pay. Upon implementation, current executives will go into a pay band that is the highest of (1) the lowest band that has a salary range that would allow the payment of their current salary OR (2) Band 1 for ES 1s and 2s, Band 2 for ES 3s and 4s, and Band 3 for ES 5s and 6s.

6. The following safeguards on SES pay should be implemented:

   a. A minimum pay increase would be established for each executive promoted from the General Schedule or equivalent personnel systems of at least a 5% raise upon entry into the SES. This then becomes the executive's salary floor and his or her salary cannot be reduced to an amount less than that salary floor as adjusted by future comparability increases.

   b. An executive who is denied a salary increase for performance reasons in any calendar year will have the opportunity to appeal to the agency's Performance Review Board under the same process that is used for appealing performance

appraisals. The Performance Review Board would continue to be required to have a majority of career SES members.

c. Any reduction in pay within a pay band will be only for reasons related to conduct or performance and will be limited to an amount of not more than 3% of base pay in any calendar year. If pay is to be reduced for performance, the executive will have the opportunity to appeal to the agency's Performance Review Board under the process that is used for appealing performance appraisals. If it is for conduct, the executive will have full MSPB appeal rights.

d. An executive who is demoted to a lower pay band shall have a right to an MSPB appeal with a final decision issued by MSPB based upon a substantial evidence standard of review. If the reduction is based on conduct, the executive may appeal to the MSPB under the normal criteria currently in place.

Over the next several months we hope to work with the Subcommittee and the Administration to implement these amendments so that pay compression will end. SEA surveyed its members about the Administration's proposal and we provide the Subcommittee with a compilation of those comments (see Attachment II). We believe these observations from the Federal government's highest ranking career employees support an end to pay compression, and express substantial concerns with regard to the Administration's proposal, concerns which can be addressed with the reasonable changes we recommend.

Thank you for the opportunity to testify this afternoon.

Attachment I

2003 LOCALITY RATES OF PAY FOR MEMBERS OF THE SENIOR EXECUTIVE SERVICE
EFFECTIVE JANUARY 2003

SALARY TABLE 2003-ES (LOC)

LOCALITY PAY AREA	ES-1	ES-2	ES-3	ES-4	ES-5	ES-6
Atlanta, GA	$ 127,847	$ 133,883	$ 139,919	$ 142,500 *	$ 142,500 *	$ 142,500 *
Boston-Worcester-Lawrence, MA-NH-ME-CT-RI	132,309	138,555	142,500 *	142,500 *	142,500 *	142,500 *
Chicago-Gary-Kenosha, IL-IN-WI	133,486	139,788	142,500 *	142,500 *	142,500 *	142,500 *
Cincinnati-Hamilton, OH-KY-IN	130,585	136,750	142,500 *	142,500 *	142,500 *	142,500 *
Cleveland-Akron, OH	128,534	134,603	140,671	142,500 *	142,500 *	142,500 *
Columbus, OH	128,966	135,054	141,143	142,500 *	142,500 *	142,500 *
Dallas-Fort Worth, TX	129,199	135,298	141,398	142,500 *	142,500 *	142,500 *
Dayton-Springfield, OH	127,707	133,736	139,766	142,500 *	142,500 *	142,500 *
Denver-Boulder-Greeley, CO	132,041	138,275	142,500 *	142,500 *	142,500 *	142,500 *
Detroit-Ann Arbor-Flint, MI	133,637	139,946	142,500 *	142,500 *	142,500 *	142,500 *
Hartford, CT	132,938	139,214	142,500 *	142,500 *	142,500 *	142,500 *
Houston-Galveston-Brazoria, TX	138,181	142,500 *	142,500 *	142,500 *	142,500 *	142,500 *
Huntsville, AL	127,078	133,078	139,077	142,500 *	142,500 *	142,500 *
Indianapolis, IN	126,810	132,797	138,784	142,500 *	142,500 *	142,500 *
Kansas City, MO-KS	127,311	133,322	139,332	142,500 *	142,500 *	142,500 *
Los Angeles-Riverside-Orange County, CA	135,198	141,581	142,500 *	142,500 *	142,500 *	142,500 *
Miami-Fort Lauderdale, FL	131,004	137,189	142,500 *	142,500 *	142,500 *	142,500 *
Milwaukee-Racine, WI	128,208	134,261	140,314	142,500 *	142,500 *	142,500 *
Minneapolis-St. Paul, MN-WI	129,967	136,103	142,239	142,500 *	142,500 *	142,500 *
New York-N. New Jersey-Long Island, NY-NJ-CT-PA	134,243	140,581	142,500 *	142,500 *	142,500 *	142,500 *
Orlando, FL	126,601	132,577	138,554	142,500 *	142,500 *	142,500 *
Philadelphia-Wilmington-Atlantic City, PA-NJ-DE-MD	130,608	136,774	142,500 *	142,500 *	142,500 *	142,500 *
Pittsburgh, PA	127,591	133,614	139,638	142,500 *	142,500 *	142,500 *
Portland-Salem, OR-WA	130,061	136,201	142,341	142,500 *	142,500 *	142,500 *
Richmond-Petersburg, VA	127,766	133,797	139,829	142,500 *	142,500 *	142,500 *
Sacramento-Yolo, CA	130,468	136,628	142,500 *	142,500 *	142,500 *	142,500 *
St. Louis, MO-IL	126,962	132,956	138,950	142,500 *	142,500 *	142,500 *
San Diego, CA	131,296	137,494	142,500 *	142,500 *	142,500 *	142,500 *
San Francisco-Oakland-San Jose, CA	138,682	142,500 *	142,500 *	142,500 *	142,500 *	142,500 *
Seattle-Tacoma-Bremerton, WA	130,212	136,359	142,500 *	142,500 *	142,500 *	142,500 *
Washington-Baltimore, DC-MD-VA-WV	129,874	136,006	142,137	142,500 *	142,500 *	142,500 *
Rest of U.S	126,566	132,541	138,516	142,500 *	142,500 *	142,500 *

* Rate limited to the rate for level III of the Executive Schedule (5 U.S.C. 5304(g)(2)).

NOTE: Law enforcement officers in the Boston and New York CMSAs are entitled to the rates on salary table 2003-ES (LEO). Locality rates of pay are basic pay only for certain purposes--see "2003 Salary Tables for Members of the Senior Executive Service, Employees in Senior-Level and Scientific or Professional Positions, Administrative Law Judges, and Members of Boards of Contract Appeals" cover sheet.

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Attachment II

SENIOR EXECUTIVES ASSOCIATION
MEMBER SURVEY
REGARDING THE ADMINISTRATION'S
2004 BUDGET PROPOSAL FOR EXECUTIVE PAY

INDEX

I. Unanswered Questions 2
A. Would there be minimum and/or maximum amount by which pay could be increased or decreased? 2
B. Would the current regulations requiring written notice for pay decreases remain in place? 2
C. Would bonuses, in addition to pay adjustments, also be granted for high performance? 2
D. How will this proposal affect SES-equivalent executives, such as Boards of Contract Appeals Judges? 3
(1) BCAJ 3
(2) SLs and STs 3
(3) FAA 3
(4) ALJs 4
II. Core principles set forth by SEA Board 4
A. Setting a cap high enough to enable receipt of the full locality pay adjustment 4
B. Requiring that any basic cost of living adjustment received by GS employees be received by executives 5
C. Prohibiting forced distributions (quotas) of executives' performance ratings by agencies 5
E. Defining the bottom of the pay band to prevent any overlap with GS-15) 7
F. Determining whether establishing pay bands within the SES rank system might not accomplish the same objective 7

Additional Comments

III. Likes SEA's Approach. No Further Comments 7
IV. Likes Administration's Proposals 7
V. Not Enough Information to Assess 9
VI. Possible Politicization of the Rating Process 9
VII. Pay for Performance is a Slippery Slope 11
VIII. Keep SES Ranks 13
IX. Insufficient Funding will be a Problem Under Pay for Performance 14
X. Expressions of Outrage 15
XI. Miscellaneous Comments 17

I. Unanswered Questions

A. Would there be minimum and/or maximum amount by which pay could be increased or decreased?

1. … A limit on the dollar decrease in salary for alleged poor performance per rating cycle would be an appropriate safeguard.

2. It might be useful **to consider not only the maximum that pay may be decreased at any one time, but also to define a path so that significant reductions can only take place over an extended period.**

B. Would the current regulations requiring written notice for pay decreases remain in place?

1. Currently, a reduction in SES grade is a rare act, and must be justified by substantial appraisal documentation. Most SES jobs are pegged at one or two SES levels and there is some security in the absence of substantial pay flexibility. **That security will evaporate if there is no burden to be met in order to reduce compensation**, and the floor in that eventuality is unacceptably low.... Under the new proposal, if you cannot justify removal, because performance is clearly satisfactory, the Agency can reduce pay. Budgetary concerns, or other problems related to political concerns, could easily result in a substantial salary reduction. Moreover, **SES applicants should know what they can expect to earn, rather than accept an initial salary that may change substantially. An SES promotion should not resemble a lottery ticket, and you take your chances after the first year.**

2. … Decreases in pay should require written documentation. A safeguard here would be to have any decrease reviewed and approved by an ERB [sic: PRB?].

C. Would bonuses, in addition to pay adjustments, also be granted for high performance?

1. … why can't pay for performance be measured by bonuses instead of base pay? Fewer but substantially bigger bonuses should produce the same results the Administration seeks without the problems inherent in their current proposal

2. I'm in favor of retaining both bonuses (one-time) and salary adjustments. This too should be at the Agency's discretion.

D. How will this proposal affect SES-equivalent executives, such as Boards of Contract Appeals Judges?

(1) BCAJ

1. As a board of contract appeals judge who was directly involved in the negotiation and establishment of the "CA" pay system, I hope we will not be left behind. Our system was designed to take into consideration the **inappropriateness of bonuses for judges**....As you know, chairmen are CA I (exec. level 4), vice chairmen are CA II (97% of exec. level 4) and judges are CA III (94% of exec. level 4**). If that changes to the above percentages of exec. level III, I think most BCA judges would be happy**.

2. **In my view, the CDA should be amended to tie BCA Judges' salaries to Level III of the Executive Schedule in lieu of the present Level IV, with the overall cap at Level II of the Executive Schedule in lieu of the present Level III cap**. This proposal should ensure that BCA Judges' salaries are on par with the proposed new SES pay structure. Thank you for the opportunity to comment.

3. The CDA should be amended to **tie the BCA Judges salaries to level III of the executive schedule (in place of level IV in the existing legislation) with an overall cap at level II of the executive schedule (in place of the current level III).** Such a change will assure that the BCA Judges salaries keep pace with the SES salaries as proposed by the administration.

(2) SLs and STs

(No comments received.)

(3) FAA

1. In the FAA, pay disparity for SES is a bigger problem than anything else especially in the Air Traffic organization. Currently my deputy makes $21,000 a year more than I do. I'm an SES ; he's not. This year he received a 5.8% pay raise and I received 3.1%. The gap widens. **I'm not sure that this proposal matters to FAA SES'ers since DOT and FAA appear to be able to do whatever they want.** We've not received promised bonuses in two years and are not eligible for Presidential awards. I guess all of the above is to ask **how do the proposed rules apply to FAA?????**

2. Pay for performance is desirable, but being an executive at FAA leaves the advantages of that in doubt. We have been asked to commit to higher performance standards here, but **the payoffs don't materialize if we reach our stretch goals and successfully support strategic initiatives. Given my choice, I would relinquish my executive status and drop down to the L band, if I could do so at my current pay and keep my current position**. I intend to explore this possibility. I believe I have more pay, retirement, and credit time advantages as

a non-executive in FAA than I have currently. Thanks for all your hard work. The Association does a great job.

3. ... **taking away the "annual" increase and making it more of a "reward/bonus" approach has had the downside in FAA of holding it (in a similar current issue) hostage to budget reductions**. I know they talked about a government wide set-aside to fund this (I am still unclear on how that would work) - but those of us in FAA have already experienced the perception in tight budget times that even a performance based award system has the appearance of being "too much to fund" - even while employee annual increases and employee awards remain funded. I also think **there should be some grandfathering clause on existing pay** if they transition into this approach.

(4) ALJs

1. Some of my judges were told by OPM representatives at an ALJ summit on capitol hill this week that the new pay bands will apply to AlJs, i.e, the proposed $102,000 to $154,700 figures. However, I am concerned about the fact that ALJs ... are exempt from the performance appraisal system established by Title 5, USC Sec 4301 (2)(D). There are currently no performance standards of any kind for ALJs. Perhaps there should be some. **Do you have any idea how the proposal could be applied to ALJs?**

II. Core principles set forth by SEA Board

A. Setting a cap high enough to enable receipt of the full locality pay adjustment

1. Several executives in Hawaii, Alaska, etc. asked that a provision be added to SEA's agenda proposing that overseas COLA's be included in high-three retirement calculations, as are locality payments for others.]

2. Any SES pay for performance plan must take into account the fact that federal **salaries are much less competitive in many urban areas than in other parts of the country**. Executives who work in these areas receive disproportionately less pay (the pay comparability act never was fully implemented) and generally have a much weaker and inexperienced workforce. To compare the performance of executives who manage these offices with others in lower cost areas is unfair and will make it even more difficult to attract executives for the toughest assignments in government. Hence, **any pay for performance plan has to take these inherent difficulties into account when paying senior executives.**

3. **The locality pay issue should be exempt from a salary cap**. Our senior executives working in San Francisco make the same as the senior executives in Vicksburg, Mississippi. ...this is grossly unfair.

B. Requiring that any basic cost of living adjustment received by GS employees be received by executives

1. "Cost of living is cost of living ..."

2. **Suggests holding COLAs in abeyance until cap is raised.**

3. ... the absence of a provision for annual raises, based upon cost of living, creates another nonappealable avenue for political other irrelevant considerations to result in a pay freeze, perhaps for many years, which quickly, because of inflation, **becomes a de facto pay cut**. Employees at the GS 1-15 level are virtually assured of annual pay increases, more or less pegged to inflation, (mostly less) and SES members who perform satisfactorily should be entitled to no less assurance.

4. ...**It is bad enough that in many years GS employees receive wage increases in greater percentages than those received by SES'ers. To deprive SES of any regular wage increases is an insult**.

5. **Why have to give up COLAs to enter SES?**

Contra

1. I'm not sure we have to insist that every year SES'ers must as a minimum receive the same COLA as the GS ranks.

C. Prohibiting forced distributions (quotas) of executives' performance ratings by agencies

1. My basic reaction to your email below is one of great concern. Already **at Interior, there is a 45% cap on the proportion of SESers who can be nominated for and receive awards.**

2. It is certainly possible, and perhaps even likely that a very substantial number of SES members, each performing in their respective areas of responsibility, are all performing very commendably or outstandingly. If an Agency has, for example, 10 law offices or litigation centers, each headed by an SES attorney, and they are all successful in winning 95 percent or more of their cases, **why is in necessary to curve their performance.** It should only happen again next year!. And the same can be said of other areas of responsibility led by other SESers. **We should rejoice in the success of SES members rather than find ways to make irrelevant distinctions**. Stated otherwise, I am not comfortable being rated outstanding if I know that my colleagues, who have performed very similarly, given their challenges, are rated lower in order to justify an OPM requirement. The proposal will force Agency evaluators to make teensy weensy distinctions among very similar performers in order to present a satisfactory grid. **Admittedly, there are distinctions among performers, and that should be recognized at the upper end by rank awards and on the lower end by**

lower appraisal ratings, but the vast middle are performing very well and should be recognized rather than penalized for it.

3. … the proposal could have extremely divisive consequences. For example, in my Agency, there are well defined goals in each SES performance plan that are used to measure and rate our individual performances. They're not easy goals. What if, as one would presume is desirable from a public service point of view, most of us meet the goals and thereby effectuate public policy? Does than mean that the system does not make "meaningful distinctions"? If the system does not make "meaningful distinctions" because most executives are good at what they do, does this mean minimal or no pay raises**? Does someone have to fail so than someone else can get a pay raise?**

4. The "meaningful distinctions" standard, to be judged by OPM alone, can act only to deprive deserving executives of pay raises or recognition. Few, if any, SES'ers obtain their positions unless they truly are the cream of the crop. This provision alone is reason to reject OPM's proposal out of hand.

5. The proposal can only be read (particularly the aspect of the appraisal system needing to be "certified") to mean that there will be <u>forced</u> lower ratings (quotas) and that would result in gross unfairness to the many who perform at the highest levels of performance but who would not get the commensurate pay. Clearly the proposal would force those persons to unfairly get lower pay. As a result**, including language in the proposal that the Agency would have "total flexibility" appears disingenuous when in the full context, the Agencies would have to force varied ratings regardless of real performance in order to be certified.** Undoubtedly that would result in forced pay scale determinations.

D. Providing appeal rights to Performance Review Boards for executives denied an annual pay adjustment

1. One potential system for preventing abuse, which I agree could be a problem, is to require reviews by the Executive Resources Board (ERB). [sic: PRBs?] I've lost touch with the requirements for ERBs, but the composition might be regulated.

2. At the Railway Retirement Board, **political appointees don't pay any attention to PRB recommendations.**

3. **Should be reviewed by <u>outside</u> board.** (Also 186)

4. …to a "board." A single manager should not have sole authority.

<u>Contra</u>

1. Leave PRB appeals off the table.

E. Defining the bottom of the pay band to prevent any overlap with GS-15

Note: Virtually every executive responding made this point.

1. I cannot understand the rationale for pegging the bottom of the SES scale to a little more than the beginning of the GS-15 pay range, except to provide an avenue to reduce SES members in order to force them to resign by paying them less than their GS 15 subordinates. Most SES members entered the service from at least the middle of the GS-15 pay range, and probably higher, so the new floor would constitute a substantial pay cut for any SES member reduced to that level.

2. ... Under no circumstances should the LOWEST level of SES pay be less than $10,000 greater than the HIGHEST level of GS-15 pay. The idea of any SES executive earning less than a GS-15 is unacceptable.

3. Your position about keeping a distinction between pay for the top of the GS-15 level and entry level SES is also good, ...

F. Determining whether establishing pay bands within the SES rank system might not accomplish the same objective

1. Go with 5 or 10-year renewable contracts. If there will be pay bands, these should be set government-wide, so stingy CEOs couldn't make his mark by showing his "toughness."

[See also **VIII**, below]

III. Likes SEA's Approach. No Further Comments

Of the 186 comments received, many express agreement with the questions raised by SEA and the Board, with little or no further comment. Almost all thanked SEA profusely for continuing to look after their interests.

IV. Likes Administration's Proposals

1. ..."While it's not the greatest approach, **it's the only one that has a possibility of approval...."**

2. [W-P A.F.] says "I think this sounds like a pretty good proposal."

3. [Corp. for National & Community Service] I support this new direction for pay for senior executives. Six 'levels' of senior management simply don't make a lot of sense. **Agencies need more authority to manage, and this is one vehicle for doing it.**

4. [Ag – Reg. Forester] …thanks for the heads-up and request for feedback on the Administration's new pay proposal for SES'ers. **I strongly support it and urge our association to be as cooperative as we can** be with the Administration and do everything we can to quickly get it enacted. I was troubled to see us so confrontational with the Administration over the Dept of Homeland Security personnel issues. I disagreed with our stand on that one.

   On this **proposal I encourage you to graciously acknowledge thanks to the Administration for finally moving forward positively to address executive pay compression, work proactively and quickly with them to finalize their proposals, and then help support the congressional sponsors**.. I strongly support pay for performance and making meaningful distinctions between SES performance. Departments and agencies which refuse to make meaningful distinctions between SES performance should not be supported. Your position about keeping a distinction between pay for the top of the GS-15 level and entry level SES is also good, although I'm not sure we have to insist that every year SESers must as a minimum receive the same COLA as the GS ranks.

   So in summary, do everything you can to make this happen quickly**, don't pick fights with the Administration**, and continue to do the good job that you are in keeping us informed. Resolution of the pay compression problem and the recognition we need significant extra financial help with locality pay in high-cost locations like the San Francisco area where I work, are the primary drivers in keeping me serving our government. I am retirement eligible, but have no interest in quitting working. The pay compression problem was weighing heavily on me.

5. Though agreeing with most of the issues raised in CAB's e-mail, suggests "**I would be careful about fighting it too hard**. …On the positive side it would eliminate the rank vs. position problem, … would also get the pay cap up, which is something I did not think I would work long enough to see."

6. **Must be basically supportive to remain a player** ... while raising only those few, key issues that are important to members.

7. Though agreeing that the e-mail "asks some very good questions," "am generally not opposed to the Administration's proposal …"

8. [OMB] I believe **this is the best shot we have at lifting the cap** and the SEA should endorse the Pay Proposal.

   More significantly, **the image and reputation of the Federal workforce will not be improved until pay is more closely tied to performance** and pay banding is an integral part

of that. Pay banding is also desirable to enable us as managers to manage our workforces better. We should embrace it for ourselves as well.

The exact rules and conditions for implementation are important **but we should avoid getting into** protracted negotiations over every detail as this makes us look more like a labor union and is precisely the kind of problem that plagues agency relationships with Federal employee unions. We should be supportive of efforts to give management greater flexibility. In return, we can rightly justify higher pay. **Opposition to forced distributions of performance ratings contributes to the "management versus labor" image. In any event, requirements for such forced distributions are unlikely once a true pay for performance system is in place.**

9. (Assuming bonus money will not be folded into the new pay band) ... I have no objection to the concept outlined below.

V. Not Enough Information to Assess

Several responders said they did not have enough information to assess the situation.

VI. Possible Politicization of the Rating Process

1. Having worked as a career SES in several agencies for the past 22 years and witnessed the games that some politicals play with the SES, **I would insist upon sufficient safeguards.** For example, agency head A wants to free up some SES slots for his or her "supporters" by encouraging current career SES staff to retire. An arbitrary salary cut of lets say $20,000 per year in salary for alleged poor performance, impacting the person's high-3 retirement annuity calculation, would drive many retirement-eligible SES out the door.

2. I see this as another trap. **I have not had an assignment since January 2002,** which lasted until April 1st. Since then my shop was abolished, my S&E budget taken away and I am awaiting reassignment to be a senior advisor to a division director, with no supervisory or money management authority. I received a pass rating in June. **Nothing since in the way of work. I am a Charter member SES 6 with three presidential rank awards since 1981. You cannot receive a performance award when there is nothing to perform.** What protection do those of us have, who served whomever was in charge over the years, to continue to serve with dignity and integrity? It makes one suspicious of intent, I don't want anything done for me, but it does provide **an example of how the lowering or raising of an executive's pay becomes a political ploy**.

3. Many SES people have their performance evaluated by political appointees. This proposal by the Administration **seems to present a new way for such appointees to downgrade,** and ultimately force out, people whose political loyalty is questioned. It might be useful to consider not only the maximum that pay may be decreased at any one time, but also to define a path so that significant reductions can only take place over an extended period.

4. … **allowing such flexibility over the pay range allows politicals a much greater leverage over SESers by allow pay increases to be potentially more greatly influenced by political considerations**. Why is this important? The current administration has taken many folks who became SESers under the Clinton Administration, myself included, and **dumped us into dead end positions, no staff, no responsibilities even remotely approaching our previous positions. Under these circumstances, many of us have no chance at all to succeed under such a new pay regime and all the talent and experience we represent, … are now at risk**. In the most strenuous way, I strongly, strongly urge you to look into this abusive situation and to consider that this pay plan may just be another method the current administration will use to weed out "incorrectly thinking" individuals from the past administration. Please consider this point in any position you take on pay regimen changes for SESers. **There are a lot of us that have been unfairly treated and this new pay scheme may just be a case of the screwing we get for the screwing we just got.**

5. I'm reminded of the late Claude Pepper's comments about proposals to reform Social Security: **"When your boss calls you into his office and tells you he's going to 'reform' your salary, do you think you're getting a raise?"** I've worked directly for a large number (and variety) of **political appointees, more than a few of whom responded to career executives on a purely visceral level. If they liked you, your errors were a reflection of desirable risk-taking. If they didn't like you your less than total successes were a reflection of your lack of initiative.** In other words, I find pay compression under the current system to be more desirable than **a wild card system**, which is what the proposal looks like to me.

6. **Having the agency set the basic pay would always be "political" whether stated or not.** Those on the "right side" or politically connected will be the ones to benefit and those on the "other side" (depending on what party is running the Administration) will not benefit regardless of performance.

7. **none of the four politicals that I have reported to in the last six years have had any relevant industry or even management experience** required for the job, while my entry into the SES ranks, even with over 20 years of industry management experience, required 7 interviews and a lengthy 14 page essay outlining my qualifications for certification.

8. … a politicization of the SES appraisal process, or its distortion, will do far more harm than the increased compensation will do good.... A related issue concerns the identity of the performance rater and reviewer, who have been, up until now, career SES members. Although I do not trust every SES careerist, just because they have that status, the system has worked fairly well. I would want to be sure that the appraisal power does not shift to political appointees or their appointees. The power to appraise is the power to destroy, or to at least inflict substantial harm. We should oppose any delegation or transfer of the appraisal power to the political arena, for the good of the SES and the nation. [A number of NLRB Regional Directors expressed their agreement with all of these comments (See, e.g., 77)

9. ...**Giving agency heads -- political appointees -- authority to set basic pay is a dangerous step away from the fundamental concept of SES -- having a core group of unbiased, non-partisan career executives.**

10. I know human nature and have many years of experience in this political system and know that such expectations, clearly laid out, are an exception and not the rule. My fear is that **this new approach would reward those who blow with the political winds** regardless of what is in the best interests of the people of the U.S. and punish those who might disagree or object to ill-considered decisions.

Contra

1. I support pay for performance. We already have it in OSD via the SES bonus process. Although subject to review by a career performance board, **OSD political appointees pretty much decide** which SES members get bonuses and how much of a bonus they get. As far as I can tell, **this system has been fairly implemented over the years and the bonuses reflect merit and pay for performance.**

VII. Pay for Performance is a Slippery Slope

1. The statement that the agencies have total flexibility sounds like we've regressed to the 'spoils' system!!! It will be interesting as to what is actually presented as an acceptable performance system that makes "distinctions" among ratings. I read the GAO report on this and it had an example of stratifying bonuses – it was rather flaky and still involved a **great deal of subjectivity, arbitrary boundaries and 'point' assigning – it appears objective, but it's a facade.**

2. Regarding "pay for performance," I concur as long as standards for excellence can be defined in definitive terms and those benchmarks can be a part of the evaluation/measurement process. **Caution must be exercised to ensure expectations can be accommodated in a public sector environment**. While some may be quick to say federal agencies must become more business-like in achieving efficiencies, and I agree, I also offer **that public sector leaders and managers are much more constrained in their ability to operate with the same degree of latitude exercised by private sector entrepreneurs.** Accordingly, a pay for performance ethos must be complemented with modifications in operational procedures that permit an entrepreneurial spirit to prevail. Establishing the former without the latter ends the race before it begins.

3. With regard to basing increases on performance, the sound of the concept is nice, however, the demon is in the details, which I believe explains why **this scorecard approach is unheard of in private industry. Without even a revenue basis to depend on, the public sector searches aimlessly for a performance indicator. It is very hard, if not impossible, to construct reliable, sufficiently concrete and objectively measurable performance measures for executives, whose work is abstract, complex, and multi-factoral. In addition, particularly in public service, accomplishments are dependent largely on**

external forces, such as appropriations, abrupt changes in political leadership and agendas, and socioeconomic conditions. The SES corps is the first cadre of employees to come under scrutiny every time there is a change in Administrations, and to that end, we serve as the buffer for the GS employees from political manipulation. We know that, as laudable as "mobility" sounds, that is one strong mechanism for political leadership to use in order to remove incumbents and put in place either cronies or toadies. If we add "pay" to that toolbox, the picture will be bleak indeed for our most accomplished civil servants, as demonstrated over time, the SES corps. The fact remains that in order for a civil servant to achieve career SES status, he or she must have risen through the ranks over many years, and likely, across parties. The person must have demonstrated a strong work ethic and many achievements over many years, across supervisors, across programs, and usually across party lines. **To have basic SES pay affected now by performance measures that would be inherently highly subjective and vulnerable to manipulation would be devastating to career professionals** who, by and large, have as their overriding interest not partisanship, but good government. I am highly suspect of this proposal as summarized below, and I am pessimistic about the end result. **With the pay compression that has occurred over the years, Levels 1 through VI are effectively already just one pay band. Widening the "band" by a mere $12k at the top end, as the proposal indicates, is very revealing of little interest in basing salaries on performance.** By measure of central tendency alone, salaries of "average" high achievers would start to drop immediately, and the very best performers, could only look forward to an after tax increase of $8k at most.

4. While pay-for-performance is an admirable concept, making it reality can be a challenge. The key is a objective set of relative measures. The USPTO has a great set of performance measures for certain executives (those in the Patent organization), others have less rigorous measures (those in some of the support organizations). Without some level objective measures, evaluations become too subjective to qualify as true "pay-for-performance".

5. ... In VA I've seen quite a few performance measures not fully developed yet put into place. I've also seen perf. measures dropped out and dropped in mid way through cycles causing some confusion. I'm **also concerned lest so many measures are put into place that achievement across the board becomes impossible.**

6. A great deal of **subjectivity**

7. Problem is coming up with measures that are usable and appropriate.

8. Pay for performance is an illusive concept... Need prior agreement on performance appraisal system.

9. Most organizations have no real cost accounting functionality to accurately measure performance.

10. **Scorecard approach is unheard of in private industry.**

Contra

1. I strongly support pay for performance and making meaningful distinctions between SES performance. Departments and agencies which refuse to make meaningful distinctions between SES performance should not be supported.

VIII. Keep SES Ranks

1. **Abandoning all SES ranks is nonsensical. The level of responsibility of the director of my agency, NOAA Fisheries, is certainly an order of magnitude greater than my own as one of his field directors.** That this difference in scope and magnitude of responsibilities exists ought to be recognized in an SES performance-based system. It certainly was in the general workforce system that NOAA adopted which collapsed the 15 GS levels into 4 bands. **An SES performance-based system might reasonably be collapsed into 2 or 3 bands, but not one.**

2. SES ranks would be abolished, and a pay range established in its place. **Ranks don't seem to make much financial difference now, so I suspect this is something we could 'give up' if we get something in return.** The only problem is compensation for SESers will be solely monetary. There is something in Maslo's hierarchy that says things like **prestige, ego, etc.. become very meaningful once the pay is adequate.** I suspect one of the things that keeps the ES-5 and ES-6's going (since we all get the same pay) is the **psychic award of rank. I would not give it up without some way to provide non monetary recognition for those in the very difficult and most senior levels.**

3. I have no problem with pay banding, particularly within the "band" of ES-1 thru ES-4. Combine them if you want. However, I believe that there is great meaning in **retaining ES-5 and ES-6 as distinct "grades."** Pay band within them if you want, but these "grades," particularly within the career service, are important. I won't waste your time with all of the arguments I am sure you are familiar with, but I believe **the "grade" system of the SES has caused many of the senior political appointees to have second thoughts about appointing/promoting their non career folks to the highest pay levels. I don't hear of any move to eliminate the "grade" structure of the military.** Some years ago China did away with its "structure" by having every officer wear the same uniform. As I recall, it didn't work out very well.

4. The FBI has a very limited performance appraisal system. In fact, it's abysmal. There are only 3 rating levels: Fully Successful; Minimally Satisfactory; and, Unsatisfactory. Virtually everyone is Fully Successful. It will take years for the FBI to reconfigure its performance appraisal system. **How about a compromise position, say, the agency could use the new pay levels, but retain the existing 6 SES Levels for not more than 3 years. At the end of the three years, they had to have a new performance plan in place and be conducting meaningful appraisals.**

5. Establishing a payband alone won't work. Even tying movement to performance won't necessarily work. As long as agencies can use other factors such as protocol code, some semi-classification system, or organizational alignment, agencies will simply administratively institutionalize the current set up. See what OSD did to the ST/SL pay band for example. **OSD policy mirrors the SES policy including quota-controlling the pay equivalent to ES-5 and ES-6**. Look at how Army actually controlled ES-5 and ES-6's. So much for person-in-the-job concept of SES. OSD and the Services continued to quota-control them even though the OPM guidance on distributing pay levels had been cancelled years ago. While I was at AMC, we proposed that in lieu of quotas, the top pay levels (ES-5 and ES-6 which were quota-controlled for career execs) be automatically received by those awarded Presidential Rank Awards, ES-5 for Meritorious, ES-6 for Distinguished. **SES's in HQ positions wanted most of the ES-5 and ES-6 quotas tied to their positions, irrespective of performance record. They felt it was necessary in order to attract individuals to their jobs**.

6. Second, eliminating the ES pay ranges seems to mean de facto that every job is the SES is potentially as important as any other job. Does SEA agree with that? Clearly, **some SES positions have more authority and responsibility than others.**

7. All senior execs are not equal in terms of responsibility, duties, authority, or comparative market worth. The ES steps should be retained. (Also (181: Performance is just one factor. **Level of responsibility and authority play a part in the pay level of any other position in Federal government**. Pay levels within bands will become de facto pay [ranks.]

8. ... what is the purpose of abolishing ranks? Currently a lower rank SES can be promoted to a higher rank with a little effort on the part of the ranking officer, **so ranks constitute a means of establishing a distribution**. With no ranks an agency, or more likely a subunit within an agency, could happily assign the top salary to all members of the unit and thereby do away with the troublesome business of trying to fairly assess relative performance. The idea of no ranks is on the face of it good, but as a basis for improving evaluation it is not likely to be successful when the ranking officer is either lazy or embarrassed to pass judgment on junior colleagues. Some element of competition between individuals is often helpful.

Contra

1. I support this new direction for pay for senior executives. Six 'levels' of senior management simply don't make a lot of sense. Agencies need more authority to manage, and this is one vehicle for doing it. [There are many more important ones, but that is another subject.]

IX. Insufficient Funding will be a Problem Under Pay for Performance

1. Present plan just underfunded.

2. Fourth, I am concerned **that if Agencies have "total flexibility to set basic pay,, pay rates would inevitably be influenced by budgetary considerations** i.e. insufficient funds to fund appropriate raises.

3. Budgetary concerns, or other problems related to political concerns, could easily result in a substantial salary reduction.

4. ... those of us in FAA have already experienced the perception in tight budget times that even a performance based award system has the appearance of being "too much to fund" - even while employee annual increases and employee awards remain funded.

X. Expressions of Outrage

1. Since other agencies have been given authority to pay SES up to $175,000, and the military can now have their retired pay excluded and get full SES pay, their proposal is blatantly unfair to us now, and for the work we have and are doing. Being from the private sector has little meaning to me other than they these "seemingly" great performers do not know what they need to know to start performing their jobs, yet they get more money because they haven't learned our profession, nor have the requisite knowledge of public service!! **Who's trying to fool whom?**

2. There are a lot of us that have been unfairly treated **and this new pay scheme may just be a case of the screwing we get for the screwing we just got**.

3. **I think this package is pathetic**. It offers tiny relief at a time when major relief is indicated. This package's only up side is a slight increase in pay with a major downside of being dependent upon what a political appointee thinks you are worth. I wonder if my pay can be decreased because of some arbitrary performance measurement system. This proposal will engender major objections for a less then significant pay increase. I support the questions raised by SEA. **I would push for a larger increase and more certainty on who will get the increase and how one goes about getting such an increase.**

4. The timing seems really bad, the economy is bad with no relief in sight, the country is running a deficit that is in a growth mode, The President is about to declare war and made commitments in his state of the nation address last night to send billions to Africa to fight the aids epidemic, fund prescription drugs for seniors, beef up medicare, activate a tax break for the wealthy who have large stock dividends, continue the battle against worldwide terrorism, expand the war in Afghanistan, initiate additional tax reductions in an effort to revitalize the stock market, etc. With all of these things already on his plate, what kind of a prioriity can SEA hope to get from the President and Congress? Other than removing the pay cap, I do not like anything about the OPM proposal. From where I stand, **It looks, talks and walks like a Trojan Horse whose mission is to kill SEA.**

5. In sum, this proposal appeared to do little to resolve the financial and morale issue associated with pay compressions. **Frankly, I feel like we're being offered a used car without a warranty.**

6. **This proposal is ridiculous**, and sounds like an attempt by this Administration to "encourage" SES members to leave the government as soon as possible.

7. I have been one of your many silent members, until now. **I am, frankly, shocked that SEA would even think of responding to OPM's trial balloon** with other than outrage.... A new pay system is window dressing. What is needed, first and foremost, is raising the pay cap and decoupling it from political expediency. The latter point in particular is key -- that Congress lacks the political moxie to defend relatively modest and well-deserved pay raises should not affect senior execs. ...**In sum, SEA should immediately turn its entire resources into fighting OPM's proposal**. I, and many of my colleagues, fully expect nothing less.

8. "Let's be real. **The proposal is an Edsal** ... Fight it tooth and nail."

9. "Fight it."

10. "**Deep –six it**." SES gives up lots and gets a little.

11. "**Arrogant at best, insulting at worst ...**"

12. "Do not screw up what we have ..."

13. Pay increases in Administration program are "paltry" and "insulting." SEA should communicate to the Administration that its program is completely unacceptable to its members ... Source of future abuse.

14. "Odious and insulting attempt to demean the SES's contributions to public service."

15. "Overall, must be viewed as an effort to entice us with a carrot of a cap raise while placing us in a system that is far less advantageous for us..."

16. Just oppose it.

17. "I see the proposal as throwing to us a small bone and carrying a potentially big stick..."

18. To give potentially less than 10% in total ceiling for the 60% at the max is unacceptable with the downside salary adjustment risk ...

19. ...**I would much prefer to pass on the possibility of raising the salary cap than suffer the rest of the proposal. It simply isn't worth it!**

20. Little or nothing ... to be of net benefit to the average SES member or the SES as a whole.

XI. Miscellaneous Comments

1. Former PMRS System proved to be inadequate.

2. Is there any sign the administration intends to put some more money in the pot to **get salaries raised initially on a one-time basis for people who have been in the SES for a while**?

3. I have arrived at the following conclusion. **Reinstate "supergrades"** (16, 17, 18), treat executives at least as "fairly" as the General Schedule, and forget about the SES. If we were on the General Schedule, we would get cost of living raises when everyone else did. We could compete for performance awards the same way GS's can, and those awards would come from a Departmental pool set aside for everyone. I really believe that **the SES is a failed** experiment.

4. I wrote because I wanted to to understand how strongly I feel about the way we have been treated. In fact, one might argue that we're better off as we are than we would be under what is proposed. I thought that there was a crisis in SES staffing**. Do they really think this will keep anyone from retiring? ... what we ought to be talking about is recapturing the amount of money we lost to pay compression over the last 10 years or so** without any conditions before we talk about a new system to measure performance prospectively. In other words, raise the cap to $154,700 first. Pay compression does not exist because of executive incompetence. It exists for political reasons completely unrelated to our performance, good or bad, over the past ten years.

5. **This may also be the time to talk about including bonuses in the computation for retirement**.

6. ... I'm also not sure of the impact of this proposal on salaries for new appointments to the SES. I would opt for Agency discretion, but I would have the results reviewed on a periodic basis.

7. When I entered the SES pay compression was at its worst. Therefore, I entered as an ES-3, and was promoted to ES-4 in 1988 or 89. Since there are only 2 or 3 ES-5 positions in my organization (all in our Headquarters office in Washington), I have remained an ES-4. My performance has been regarded highly. I have received bonuses every year since 1992 and in 2002 received a Presidential Rank (Meritorious) award.

   Your message indicated that if this new system were adopted that our placement within the band would be based upon performance. While I have performed very well, because I have chosen not to move to Washington, and stayed in the hinterlands of Philadelphia my position is among the lowest of the SES positions in my organization in terms of the organizational pyramid. (Those who have reached my position in recent years have been "capped" at ES-3.) Therefore**, do you know if this proposal contemplates "pegging" salaries based SOLELY upon performance (in which case I would do fine), or whether the "importance" of the job would also be a factor (in which case I would likely not fare any better than I do now while the non-career executives who come in to our**

Washington Headquarters for several years primarily (?) to improve their resumes would reap the benefits)??

[Ed] This member Is asking whether new system would be "pay for performance" or "rank in person."]

8. **Should be time limit for OPM to certify.**

9. How will existing differences in **post-employment restrictions** be handled [if ranks are abolished]?

10. **Big agencies will get more ...Just give $154,000 to those who meet presidential rank qualifications.**

11. My overall concern is **the increased time we will have to take to document our performance**, the creation of additional performance review boards – all the non productive administrative things that will most likely occur to implement the system. Speaking for myself, I do not want to take the time to do this in lieu of meeting mission requirements.

Mrs. DAVIS OF VIRGINIA. Thank you, Mr. Bransford.

Ms. Heiser.

Ms. HEISER. Madam Chair and Congressman Davis, my name is Karen Heiser. On behalf of the 200,000 managers and supervisors in the Federal Government whose interests are represented by the Federal Managers Association, I would like to thank you for inviting us to present our views before this committee regarding the important subject of compensation for Federal employees.

I am currently the organizational development manager at Watervliet Arsenal in New York with the U.S. Department of the Army. My statements are my own and in my capacity as a member of FMA and do not represent the official views of the Department of the Army or Watervliet Arsenal.

Established in 1913, the FMA is the largest and oldest association of managers and supervisors in the Federal Government. As those who are responsible for the daily management and supervision of government programs and personnel, our members possess a wide breadth of experience and expertise we hope will be helpful as we collectively seek to address the human capital crisis our Civil Service has been burdened with.

While retaining our status as a world class manufacturer, Watervliet Arsenal has struggled for over a decade with decreasing workload and downsizing of personnel. To help offset attrition and related loss of skills, anticipated hiring of new engineers and manufacturing apprentices will rejuvenate the nucleus of our work force. Now is the time for us to revive development of essential skills for the future through initiatives such as a reactivated apprentice program at Watervliet Arsenal where program graduates since the 1800's have provided our critical manufacturing skills and grown into many of our supervisory positions from firstline to directorate level.

At Watervliet Arsenal and beyond, this type of in-house training and mentoring is what our government must do more of as we continue to lose valuable expertise by way of retirements and mid-career departures.

Compounding the myriad of problems associated with the recruitment and retention of Federal employees is the significant pay gap that we have discussed between public and private sectors. According to a 2001 survey of college graduates, current Federal and non-Federal workers conducted by the Partnership for Public Service, nearly 90 percent said that offering salaries more competitive with those paid by the private sector would be an effective way to improve Federal recruitment. Eighty-one percent of college graduates that same year said higher pay would be very effective in getting people to seek Federal employment.

The public sector simply has not been able to compete with private companies to secure the talents of top notch workers because of cash strapped agency budgets and an unwillingness to address pay comparability issues.

We have discussed FEPCA a bit today. The act was intended to close the gap between Federal employee salaries and those of their private sector counterparts. However, FEPCA has never been implemented as it was originally intended. Since the bill was enacted, administrations led by both political parties have used the capping

feature designed to reduce pay increases in times of economic distress. This executive authority has been utilized despite record budget surpluses.

More than a decade since the enactment of FEPCA, the Bureau of Labor Statistics shows the pay gap between Federal civilian employees and their private sector counterparts has grown to 33 percent. If FEPCA is never to be adhered to, we must at a minimum reexamine the language and the intent of the act and determine how best to bring public sector salaries more in line with those of their private sector counterparts. For the time being, however, we must uphold the longstanding principle of linking annual pay increases between Federal civilian employees and military personnel.

Since 1987 and 19 of the past 22 years, civilian and military personnel have received the same annual raises. President Bush recently proposed a 2 percent across the board average pay raise for Federal employees in 2004, while military personnel are slated to receive a 4.1 percent average pay raise next year. For the third straight year, the White House has attempted to delink civilian and military pay increases.

In light of the well documented human capital concerns facing our Federal Government, we must maintain the tradition of providing equitable pay increases to Federal civilian employees and members of the uniformed services, all of whom work each day to ensure our Nation's security and make significant contributions to the general welfare of the United States.

Legislation has been recently introduced in the Senate by Senator George Voinovich that would allow managers to use a variety of compensation tools such as recruitment, relocation and retention bonuses and give agencies streamlined critical pay authority to fill key positions. These are sensible reforms that would begin to address the work force problems that will only worsen with the forthcoming retirement wave of Federal employees.

Beyond the normal retirement wave of a large portion of the aging Federal work force, there is a distinct retention problem in the Federal Government. The notion of the career civil servant is becoming more and more obsolete because there are few incentives for advancement in the Federal Government. When combined with better salary and benefit packages in the private sector, it is no wonder that many Federal employees are leaving the public sector after only a few years of service.

In fact, there are oftentimes disincentives for moving up the career ladder. A perfect illustration is the current statute that caps overtime pay for Federal managers and supervisors. Between 1994 and 2001, the non-postal executive branch civilian work force was reduced by more than 452,000 positions. As one of the effects of this downsizing, overtime is becoming increasingly common. Under current law, overtime pay for Federal managers, supervisors and FSLA exempt employees is limited to that of a General Schedule Level 10, Step 1 employee. The first grade based overtime cap enacted in 1954 set the base at GS–9, Step 1. Twelve years later in 1966, it was increased to GS–10, Step 1. In the 37 years since then, however, nothing has been done to keep pace with changing work force realities.

We have discussed how the work force in the Federal Government has changed from a clerical work force to one of more professional or information knowledge related services. In 1966, the average GS grade was 7.3 and in 2001, the average GS grade was 9.7, nearly three full grades higher since the implementation of the current pay cap.

Overtime pay is premium pay and therefore does not count toward increasing an employee's future retirement benefit. That means that increasing overtime pay does not affect mandatory spending. The overtime cap causes two problems for Federal managers and supervisors. Managers and supervisors above a GS–12, Step 6 can actually earn less on overtime than they do for work performed during the work week. Second, managers and supervisors may earn substantially less for overtime work than the employees they supervise.

Raising the overtime cap would present an opportunity and provide an important move toward addressing overtime problems that serve as disincentives to hardworking civil servants contemplating accepting promotions to the ranks of management when they consider the various benefits of moving to those levels of higher responsibility.

The Federal Wage System as we have only touched on briefly, is one of the most maligned and adversely affected sectors of the Federal Government. FMA is concerned about securing adequate pay raises for the 225,000 hardworking men and women covered by the FWS. This number represents a reduction of 53 percent of the Federal wage system work force size in 1984 due to downsizing and significant pay disparities with similar positions in private industry.

A major concern is the disparity in how pay raises are determined in the present system of wage grade surveying. In examining the pay setting features used for wage grade pay, a significant improvement would be the utilization of like industries in establishing pay scales, providing a standard wage grade survey and pay scale setting with appropriate locality adjustments would be a step in the right direction to resolve this longstanding inequity.

We have talked much about pay for performance and performance management in general today. Currently, pay is based on internal equity that revolves around seniority, not performance. We certainly agree that pay for performance is as valid as pay for seniority.

As a start, for agencies to perform at optimum levels, employees must have clearly defined performance standards on which to be appraised. These standards should be directly linked to the agency's mission, customer service goals and their annual performance plan or strategic plan. We at FMA support implementing a more comprehensive governmentwide appraisal system that includes a pay for performance component.

We recommend an awards system for managers that adequately reflects the manager's level of responsibility, span of control and level of achievement. Of course any such system requires sufficient appropriations funds. We have too often seen over time new pay authorities without the necessary dollars to utilize these tools. The Bush administration has proposed a $500 million Human Capital

Performance Fund for fiscal year 2004 to allow managers to increase pay beyond annual raises for high performing employees and address other critical personnel needs. Although this is a step in the right direction, questions must still be answered in terms of the disbursement of funds. Who will decide which employees receive increases and who will determine the amount of such increases? Is $500 million significant and sufficient for a work force of some 1.8 million Federal employees? How much will be lost to administrative costs as the money filters down through various chains of command? Will this fund be renewed every year and appropriated accordingly?

Furthermore, FMA does not believe any new performance fund should be used to undercut fair and appropriate annual pay adjustments for Federal employees. The question of an effective, consistent performance measurement system throughout the Government must be addressed.

Our conclusion is, as we collectively grapple with the complex issue of compensation reform in the Federal Government, we must find where models such as the ones being used at the IRS and the FAA have succeeded and where they have failed. There have also been numerous instances where demonstration projects in the area of expanding personnel authority have brought success to some Federal agencies but rarely are these initiatives allowed to cross agency lines.

The approach the Government takes to correct pay systems for civilian workers will decide how this Nation survives the human capital crisis before us. More importantly, Congress and the administration must shift the habitual focus from cutting the size of the Federal workforce to that of recruiting and retaining top talent.

Some of the challenges facing the Federal work force will be difficult to overcome should a continued priority be placed on the conversion of critical Federal sector jobs to private sector activity. The loss of valuable and experienced employees and the institution of wisdom they provide is already taking place. No real succession planning, including managerial development and training, has been funded or implemented to ease the strain the system is facing as retirement eligible employees leave the public sector.

At FMA we would like to propose several recommendations. One important priority is to work with both the administration and Congress to alter the image and perception of the Civil Service. Far too often civil servants have unfairly taken the brunt of the blame for ill-advised policies they have no control over. The public must recognize the important duties our Federal employees perform each and every day on their behalf.

We would also like to see review of FEPCA to examine what adjustments need to be made to enable the legislation to work as intended. Any constructive dialog is better than the hollow act of preemptive designated pay increases each and every year.

We also support ways to improve the hiring process for Federal employment and bring about policies that attract the best and brightest of our society to serve in public service. Correspondingly, managers should be afforded the means to continuously enhance their skills. Agencies and departments should increase opportunities for managers to receive training in their respective fields while

on duty by specifically allocating funds for this training. Thus FMA supports establishing management succession programs to ensure we have the strongest possible pool of managers to lead tomorrow's Civil Service.

Finally, we encourage a real and sincere look at Federal pay systems while encouraging structures that attract, retain and maintain the Federal workforce we need and desire. You asked if everyone was satisfied with pay, should we still look at the grade structure. I would put to you that the current grade structure not only determines pay but also is a determining factor in recruitment and internal movement of employees. Often a person's grade is more determining of their ability to be promoted than their resume. That is not good. That is not right.

We would propose that any new system be fair and realistic in offering career ladder incentives and progressions.

I would like to thank you again, Madam Chair, for allowing me to go beyond my 5 minutes and for providing FMA an opportunity to present our views. We look forward to working with you and other Members of Congress to deal with the human capital crisis. I would be delighted to answer any questions you have.

[The prepared statement of Ms. Heiser follows:]

FMA

Federal Managers Association

Testimony
Before the Committee on Government Reform
Subcommittee on Civil Service and Agency Organization
United States House of Representatives

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Compensation Reform in the Federal Government

Statement of
Ms. Karen Heiser
Federal Managers Association



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Chairwoman Davis, Ranking Member Davis, and Members of the Subcommittee:

My name is Karen Heiser. On behalf of the 200,000 managers and supervisors in the Federal government whose interests are represented by the Federal Managers Association (FMA), I would like to thank you for inviting us to present our views before the House Government Reform Subcommittee on Civil Service and Agency Organization regarding the important subject of compensation for Federal employees.

I am currently the Organization Development Manager at Watervliet Arsenal in New York, U.S. Department of the Army. My statements are my own in my capacity as a member of FMA and do not represent the official views of the Department of Defense or the Army.

Established in 1913, FMA is the largest and oldest Association of managers and supervisors in the Federal government. Our Association has representation in more than 25 Federal departments and agencies. We are a non-profit advocacy organization dedicated to promoting excellence in government through effective management. As those who are responsible for the daily management and supervision of government programs and personnel, our members possess a wide breadth of experience and expertise that we hope will be helpful as we collectively seek to address the human capital crisis that our civil service has been saddled with.

This hearing comes on the heels of recently released survey results from the Office of Personnel Management (OPM)[1]. OPM sent a 100-question survey to over 208,000 Federal workers between May and August 2002, to which more than 106,000 employees responded, representing 189 units in 24 of the largest Federal agencies. The data confirms that in addition to the impending mass exodus of Federal workers due to retirement, we are facing difficulties in the

[1] U.S. Office of Personnel Management: 2002 Federal Human Capital Survey, March 2003.

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area of retention, as more than one-third of those surveyed said they were considering leaving their jobs. A little less than half of the 34.6 percent who are considering leaving said they were planning to retire within three years. As it relates to our discussion today, 43.8 percent felt their pay was fair, poor, or very poor. The study also shows that fewer than half of all employees are satisfied with the recognition they get for doing a good job, with only 30 percent believing awards programs provide real incentives for workers to do their best. Only 27 percent said steps have been taken to deal with poor performers.

Watervliet Arsenal has struggled for over a decade with decreasing workload and downsizing of personnel. To help offset attrition and skill loss, anticipated hiring of new engineers and apprentices will rejuvenate the nucleus of the workforce. The infusion of skills is a critical part of a successful transformation. The apprentice program at Watervliet Arsenal has always been the vehicle to recruit and develop these core skills. Although dormant for several years as a result of declining workload, the program is ready and waiting. Now is the time to revive the development of essential skills for the future through initiatives such as a reactivated apprentice program at Watervliet Arsenal, where program graduates have always staffed our critical manufacturing skill needs as well as many of our supervisory positions, from first line to directorate level. This type of in-house training and mentoring is what our government must do more of as we continue to lose valuable expertise by way of retirements mid-career departures.

A critical piece to this puzzle is the issue of compensation. Last April, OPM released a white paper[2] intended to initiate a dialogue on reform of the current Federal pay structure. According to OPM, if the government is to recruit, manage, and retain the human capital it needs, its white-collar pay system should:

- Achieve the principle of providing equal pay for work of equal value;
- Provide agencies the means to offer competitive salary levels on a timely, rational basis;
- Recognize competencies and results, at both the individual and organizational level; and
- Orient employee efforts and pay expenditures toward mission accomplishment.

[2] U.S. Office of Personnel Management: "A Fresh Start for Federal Pay: The Case for Modernization," April 2002.

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Similarly, the second National Commission on the Public Service, a.k.a, the Volcker Commission so named for Commission Chair Paul Volcker, has issued recommendations on pay reform as part of its final report released this past January. More specifically, the Volcker Commission believes that Congress should establish policies that permit agencies to set compensation related to current market comparisons. The Commission is also of the opinion that current personnel systems are: a) out of touch with market reality; and b) immune to performance because managers seek to "spread bonuses around as compensation supplements for large numbers of employees instead of incentives or rewards for top performers."[3] The Commission goes on to state that such a system "discourages potential employees, especially the most talented and promising, who are reluctant to enter a field where there are so few financial rewards for their hard work, where mediocrity and excellence yield the same paycheck."[4]

PAY COMPARABILITY BETWEEN PUBLIC AND PRIVATE SECTORS

Compounding the myriad of problems associated with the recruitment and retention of Federal employees is the significant pay gap between the public and private sectors. According to a survey by the Partnership for Public Service[5], the Federal government is not considered an employer of choice for the majority of graduating college seniors. In the survey, nearly 90 percent said that offering salaries more competitive with those paid by the private sector would be an "effective" way to improve Federal recruitment. Eighty-one percent of college graduates said higher pay would be "very effective" in getting people to seek Federal employment. When Federal employees were asked to rank the effectiveness of 20 proposals for attracting talented people to government, the second-most popular choice was offering more competitive salaries (92 percent). The public sector simply has not been able to compete with private companies to secure the talents of top-notch workers because of cash-strapped agency budgets and an unwillingness to address pay comparability issues.

The Federal Employee Pay Comparability Act (FEPCA) of 1990 was intended to close

[3] Report of the National Commission on the Public Service: "Urgent Business for America: Revitalizing the Federal Government for the 21st Century," January 2003, pp. 9-10.
[4] Ibid
[5] Survey conducted by Hart-Teeter for the Partnership for Public Service and the Council for Excellence in Government, Oct. 23, 2001, p. 1-3.

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the gap between Federal employee salaries and those of their private-sector counterparts.

However, FEPCA has never been implemented as it was originally intended. Since this bill was enacted, administrations led by both political parties have used a capping feature designed to reduce pay increases in times of economic distress. This executive authority was utilized despite record budget surpluses by the government. More than a decade since the enactment of FEPCA, the Bureau of Labor Statistics shows that the pay gap between Federal civilian employees and their private-sector counterparts has grown to 33 percent. If FEPCA is to never be adhered to, we must, at a minimum, re-examine FEPCA to determine how best to bring public-sector salaries more in line with those of their private-sector counterparts. Closing the pay gap between public and private-sector salaries is critical if we are to successfully recruit and retain the "best and brightest."

PAY PARITY BETWEEN CIVILIAN AND MILITARY PERSONNEL

For the time being, however, we must uphold the longstanding principle of linking annual pay increases between Federal civilian employees and military personnel. Since 1987 – and in 19 of the last 22 years – civilian and military personnel have received the same annual raises.

Per the direction of Congress, President Bush recently signed into law a 4.1 percent average pay raise for civilian workers this year that matches the increase for the military – despite originally proposing only a 2.6 percent pay raise for Federal civilians. Nevertheless, the Administration has just proposed a 2 percent across-the-board average pay raise for Federal employees in 2004, while military personnel are slated to receive a 4.1 percent average pay raise next year – marking the third straight year that the White House has attempted to de-link civilian and military pay increases. The 2 percent recommended pay raise also rebuffs the 2.7 percent increase mandated by the formula in FEPCA used to determine annual civil service pay raises.

In light of the well-documented human capital concerns facing our Federal government, we must maintain the tradition of providing equitable pay increases to Federal civilian employees and members of the uniformed services – all of whom are on the frontlines ensuring our nation's security each day and make significant contributions to the general welfare of the United States.

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RECRUITMENT AND RETENTION TOOLS

Compensation is an integral piece of the human capital crisis we are presently facing. Legislation has been introduced in the Senate by Sen. George Voinovich (R-OH), S. 129, that would allow managers to use a variety of compensation tools such as recruitment, relocation, and retention bonuses, and give agencies streamlined critical pay authority to fill key positions. These are sensible reforms that would begin to address the workforce problems that will only worsen with the forthcoming retirement wave.

Retention bonuses do not always have to take the form of financial incentives. In exit interviews of Federal workers, other issues have been raised such as a lack of recognition and the absence of a long-term sense of purpose. It is also a widespread belief of those leaving government that insufficient opportunities exist for growth in the public sector, which brings us to the problem of proper succession planning. In a recent poll conducted by the Partnership for Public Service, when Federal employees were asked to rank the effectiveness of 20 proposals for attracting talented people to government, the most popular choice was providing more opportunities for career advancement.

OVERTIME PAY FOR MANAGERS

There is a distinct retention problem in the Federal government. The notion of the career civil servant is becoming more and more obsolete because there are few incentives for advancement in the Federal government. When combined with higher salaries and benefits packages in the private sector, it is no wonder that many Federal employees are leaving the public sector after only a few years of service. In fact, there are often times disincentives for moving up the career ladder. A perfect illustration is the current statute which caps overtime pay for Federal managers and supervisors.

Between 1994 and 2001, the non-postal executive branch civilian workforce was reduced by more than 452,000 positions.[6] One of the side-effects of this downsizing is that overtime is

[6] U.S. Office of Personnel Management, "The Fact Book 2002 Edition: Federal Civilian Workforce Statistics," p. 8.

becoming increasingly common. According to OPM, "the percentage of public-sector supervisors and other FLSA-exempt employees who receive overtime pay is increasing."[7]

Federal managers, supervisors, and other Fair Labor Standards Act-exempt employees, however, face an outdated restriction placed on the payment of overtime that is encouraging some to leave the ranks of management and return to the bargaining unit or move to the private sector so they can earn a higher paycheck.

Under current law, 5 U.S.C. 5542(a)(2), overtime pay for Federal managers, supervisors and FLSA exempt employees (one and a half times the normal rate for work in excess of 40 hours per week) is limited to that given to a General Schedule level 10, step 1 employee. The first grade-based overtime cap, enacted in 1954, set the base at GS 9, step 1 (P.L. 83-763). Twelve years later in 1966, it was increased to GS 10, step 1 (P.L. 89-504). In the thirty-three years since that time, however, nothing has been done to keep pace with changing workforce realities. In 1966 the average GS grade was 7.3; in 2001 the average GS grade was 9.7,[8] nearly three full grade levels higher since the implementation of the current overtime cap.

Overtime pay is premium pay and therefore does not count toward increasing an employee's future retirement benefit. This means that increasing overtime pay does not affect mandatory spending. The overtime cap causes two problems for Federal managers and supervisors:

1. First, managers and supervisors above GS-12, step 6 actually earn less on overtime than they do for work performed during the regular work week.

   Example: Sally Supervisor is a GS-13, step 9.

   Her regular rate of pay is $36.14 per hour.

   For overtime, however, she is paid at a rate of $26.64 per hour.

   If Sally worked on a Saturday she would be paid $9.50 less per hour than for the work she performed on Friday.

[7] April 28, 1999 letter from Office of Personnel Management Director Janice R. LaChance to House Speaker J. Dennis Hastert.
[8] U.S. Office of Personnel Management, "The Fact Book 2002 Edition: Federal Civilian Workforce Statistics," p. 26.

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2. Second, managers and supervisors may earn substantially less for overtime work than the employees they supervise.

   Example: Sally Supervisor is a GS-13, step 9.

   Her regular rate of pay is $36.14 per hour.

   For overtime, however, she is paid at a rate of $26.64 per hour.

   Ed Employee is a GS-12, step 7 and FLSA non-exempt with an overtime rate of $42.09.

Raising the overtime cap would represent an important step toward addressing overtime problems that increasingly serve as disincentives to hard-working civil servants contemplating accepting promotions into the ranks of management. It would also go a long way toward removing significant obstacles to our government's ability to recruit and retain a highly motivated cadre of managers and supervisors.

WAGE-GRADE DISPARITIES

The Federal Wage System (FWS) has been one of the most maligned and adversely affected sectors of the Federal government. FMA is concerned about securing adequate pay raises for the 225,000 hardworking men and women covered by the FWS.[9] This number represents only 47 percent of the FWS workforce size in 1984[10], due to downsizing and significant pay disparities with similar positions offered in private industry. Multiple regions across the nation are presently in place to determine the wage of the particular trades and skills that are set in the wage grade pay-setting.

There are several concerns regarding wage-grade pay that demand serious attention in order to make these Federal jobs more competitive and desirable for the younger job seekers leaving our colleges and high schools today. The first concern is the disparity in how pay raises are determined in the present system of wage-grade surveying. The vast difference in locality pay not only occurs from region to region, but also can exist in small pockets within the same

[9] U.S. Office of Personnel Management, "The Fact Book 2002 Edition: Federal Civilian Workforce Statistics," p. 30.
[10] Ibid

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locality. A contributing factor to this disparity lies in the methodology used to select wage-grade survey industries and services. While it is true that the cost of living is different from region to region, there is no correlation when you examine how pay scales are set for various trades in our Federal workforce.

A prime example occurs in the wage-grade trades for the nation's ship repair trades. There is a $4 per hour difference in pay for ship repairers who perform the same skill at the Norfolk Naval Shipyard and those working at the Puget Sound Naval Shipyard. This difference was in large part established by the businesses used in those two areas as part of their wage-grade surveys. In the Puget Sound area a huge aerospace and computer industry base was utilized while at Norfolk more service-oriented businesses were examined. Despite the cost of living for the two areas being very comparable, the wage-grade surveys set vastly different pay rates. This occurrence can be found in many areas across the nation, which creates an unfair system for the skilled artisans and workers in our workforce.

In examining the pay-setting features used for wage-grade pay a major improvement would be the utilization of like industries in establishing pay scales. A more consistent method must be used to establish logical and realistic pay skills for skilled workers. A uniform system to establish the pay scales would be a major step forward in attracting younger workers into our aging Federal workforce. Fair distribution of pay raises is a primary concern of management and workers in the Federal civil service today. As different methods are examined to use in the setting of pay there must be an element of fairness instilled. A specific trade must be paid on a similar scale nationwide with only the consideration of an area's cost of living as an adjustment. Providing a standard wage-grade survey and pay-scale setting with appropriate locality adjustments would be a step in the right direction to resolve this longstanding inequity.

General schedule pay has a huge impact on the present setting of wage-grade pay. The trend has been to cap wage grade raises to the percentage set for GS pay. This has also been a major contributing factor to keeping the pay gap in the double digit levels.

PERFORMANCE MANAGEMENT

For agencies to perform at optimum levels, employees must have clearly defined

performance standards. These standards should be directly linked to the agency's mission, customer service goals, and their annual performance plan and/or strategic plan.

According to a Merit Systems Protection Board survey[11] conducted during fiscal years 1997 through 1999, on average one of every 8.8 Federal workers received a promotion each year during the three-year period that was studied. In other words, 7.8 of 8.8 employees – or 88.6 percent of the Federal workforce – were not promoted in any given year. At GS-12, the rate of promotion fell to about one in 13 a year; at GS-13, the rate was about one in 20, and at GS-14, the rate was about one in 25. Generally speaking, the rate of promotion slows as the General Schedule grade level increases. With such a low rate of promotion, the problem of putting the right people in the right jobs is aggravated.

We at FMA support implementing a more comprehensive, government-wide appraisal system. The current "pass/fail" appraisal system, for example, can serve as a disincentive for excellence. An appraisal system that clearly delineates unacceptable, acceptable and excellent performance is recommended. The appraisal rating should be a key consideration in the promotion and award processes.

The current mechanism in place for addressing unacceptable performance should be revised, for it is far too cumbersome and takes too long to document. As a remedial measure, the employee should be provided tutoring and given a reasonable timeframe in which to attain acceptable performance. We as Federal managers want the process to be fair for both the employee and the agency.

We envision a "contract" between the manager and the employee, i.e., if an employee performs at the acceptable level of performance, he/she will retain the position and receive the scheduled within-grade increases; if an employee performs at the excellent level, he/she will receive proper recognition; if an employee performs at the unacceptable level, he/she will receive a reasonable timeframe in which to improve performance.

We at FMA recommend an awards system for managers that adequately reflects the manager's level of responsibility, span of control, and level of achievement. Of course, any such system requires sufficient appropriations funds. We have too often seen over time new pay

[11] U.S. Merit Systems Protection Board: "The Federal Merit Promotion Program: Process vs. Outcome," Dec. 2001, p. xi.

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authorities without the necessary dollars to utilize these tools. The Bush Administration has proposed a $500 million Human Capital Performance Fund for fiscal 2004 to "allow managers to increase pay beyond annual raises for high-performing employees and address other critical personnel needs."[12] OPM will administer the Fund for the purpose of allowing agencies to deliver additional pay to certain civilian employees based on individual performance or other human capital needs, in accordance with OPM-approved agency plans. Although this is a step in the right direction, questions must still be answered in terms of the disbursement of the funds:

- Who will decide which employees receive increases, and who will determine the amount of such increases?
- Is $500 million sufficient for a workforce of some 1.8 million Federal employees?
- Will this Fund be renewed every year and appropriated accordingly?

Furthermore, FMA does not believe any new Performance Fund should be used to undercut fair and appropriate annual pay adjustments for Federal employees.

PAY BANDING

To help the Internal Revenue Service (IRS) improve tax administration and service to taxpayers, Congress included new requirements affording greater flexibility in handling personnel issues as part of the IRS Restructuring and Reform Act of 1998 (RRA).[13] One of the act's personnel flexibility provisions gave IRS discretionary authority in hiring, paying, and recruiting staff. Section 9509 authorized IRS to implement a broadbanded pay system, also called pay banding, to assist in its reorganization. Pay-banding combines two or more pay grades. Using this provision, IRS combined between 2 and 3 grades per band.

The IRS began its "pay-for-performance," pay-banding effort with conversion of Senior Managers (SM) in March 2001. The following December, Department Managers (DM) were converted to the pay-banding system. There are separate pay bands for each level of IRS management. The SM Band is for all mid-level positions. The DM Band combines grade 11-13

[12] Fiscal Year 2004 Budget Proposal of the U.S. Government, p. 38.
[13] P.L. 105-206 was enacted on July 22, 1998. Title I, Subtitle C, Personnel Flexibilities, sections 1201-05, list the provisions.

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Service Center positions. The Service recently decided that the remaining GS/GM managerial positions in the Service will be converted to the pay-banding system effective in July 2003.

IRS plans to establish two Frontline Manager (FM) pay bands to include remaining managers not currently covered by the SM or DM pay bands. The FM I pay band will cover GS managerial positions at grades 7 through 11, and the FM II pay band will cover GS/GM managerial positions at grades 12 through 14. Frontline grade 15 managerial positions will be converted to the SM pay band.

Managers in the FM pay bands will continue to receive the annual comparability and locality increases. However, once in the pay band, step increases will no longer be automatic; rather, they will be based strictly on performance. Managers covered by an FM pay band will be eligible for their first performance-based step increase in January 2004, based on their FY 2003 performance ratings. Thereafter, salary reviews and any appropriate step increases will occur every 2 years. Annual performance bonuses will be mandatory for those managers earning an "Outstanding" summary rating. Managers in the FM pay band with summary ratings of "Exceeded" will be eligible for performance bonuses every year. The Service has established a bonus pool of 2% of FM salaries to fund FM bonuses.

Some of the IRS pay-band principles include:

- Appraisals will be done every year, but salary determinations are made every 2 years. The determination of whether an employee progresses further in the band is determined by matching 2 consecutive annual ratings and then matching them to pre-determined minimum rating requirements.

- Rating requirements to progress through the band increase the further the employee moves. (Example: In the beginning of the band two "Met" ratings are needed to move forward in the SM Band. One rating of "Outstanding" and the other of at least "Exceeded" are needed to move into the last increment of the band.)

- Pay-banded employees can receive annual bonuses based on the yearly appraisal. The bonus is a one time payment that does not become part of base pay (salary).

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- All employees in IRS pay bands receive the General Schedule comparability increase.
- Employees converted into IRS pay bands are given credit for time spent in current step when converted. (Example: Current Grade 13, step 9 with 2 years under current step; the salary of Grade 13, step 9 increased by 2/3 of the value of the step increase between steps 9 & 10; the new amount is then slotted into the new pay band salary chart. If the employee falls between steps s/he is slotted at the higher step.)
- To ensure ratings consistency, performance review boards were built into the system. The review examines ratings given to ensure consistency of criteria application.

Within FMA, we have conferences divided along agency lines, one of which is the FMA-IRS Conference. Feedback from our IRS Conference shows that pay bands offer the opportunity to provide real recognition to top performers. The General Schedule places its emphasis on longevity. As long as an employee maintains a satisfactory level of performance, s/he will move through the step, and if s/he stays employed long enough, s/he will reach the top of the step.

Pay bands also provide the opportunity to have accelerated salary progression for top performers. Under the IRS pay-band system, managers are eligible for a performance bonus each year. Those managers with "Outstanding" summary ratings will receive a mandatory performance bonus. Managers with "Exceeded" summary ratings are eligible for performance bonuses.

In the area of job classification, determinations are made which place positions in different pay categories where the distinctions that led to the classification are small. Pay-banding provides the opportunity to place greater weight on performance and personal contributions.

Pay bands can also be designed to provide a longer look at performance beyond a one-year snapshot. Many occupations have tasks that take considerable lengths of time. Pay bands can be designed to recognize performance beyond one year. (The IRS system combines two consecutive yearly ratings to determine whether an employee moves forward in the band).

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Arbitrary grade classifications in the GS system inhibit non-competitive reassignments. Broader bands allow non-competitive reassignments. This enhances management flexibility and developmental opportunities.

Of course, there remain challenges with the IRS pay-band system, and any proposed pay-band system for that matter. First, pay-for-performance systems are only as good as the appraisal systems they use. Since performance is the determining factor in pay-band movement, if there is no confidence in the appraisal system, there will be no confidence in the pay system. Moreover, pay-for-performance systems can be problematic where there is an aging workforce. Experienced employees tend to convert towards the top of the pay band. This provides them little room to progress through the band, and only if they achieve higher levels of performance ratings. This is particularly true for those employees whose GS grade is the highest grade in the new band. (Example: Grade 13 employee placed in an 11-13 band. S/he will be towards the top and now will need the higher grades to continue to move ahead. Previously s/he only needed time in grade to progress).

Finally, pay-band performance requirements can discourage non-banded employees from applying for banded positions. If the employee is converted in the upper range of a band s/he may not have confidence s/he can achieve the higher ratings requirements.

For additional guidance, Congress should look to the pay-banding system being implemented at the Federal Aviation Administration (FAA). As a result of legislation in 1995 that granted the agency broad exemptions from laws governing Federal civilian personnel management found in Title 5 of the United States Code, the FAA is managing its personnel in one of the most flexible human capital management settings ever witnessed in the Federal government. In 1996, FAA announced a sweeping reform of its personnel management system. Once exempted from these provisions of title 5, FAA replaced the traditional grade and step pay system with a broadbanded pay structure that provides for a wider range of pay and greater managerial flexibility to attract, retain, and reward employees.

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CONCLUSION

As we collectively grapple with the complex issue of compensation reform in the Federal government, we must find where models such as the ones being used at the IRS and the FAA have succeeded – and failed. There have also been numerous instances of demonstration projects in the area of expanding personnel authority bringing success to some Federal agencies, but rarely are these successful initiatives allowed to cross agency lines. The approach the government takes to correct pay systems for civilian workers will decide how this Nation survives the human capital crisis before us. More importantly, Congress and the Administration must shift the habitual focus from cutting the size of the Federal workforce to that of recruiting and retaining top talent.

Some of the challenges facing the Federal workforce will be difficult to overcome should a continued priority be placed on conversion of critical Federal sector jobs to private sector activity. The loss of valuable and experienced employees – and the institutional wisdom they provide – is already taking place. No real succession planning, including managerial development and training, has been funded or implemented to ease the strain the system is facing as retirement-eligible employees leave the public sector.

We at FMA would like to propose several recommendations. One important priority is to work with both the Administration and Congress to alter the image and perception of the civil service. Far too often, civil servants have unfairly taken the brunt of the blame for ill-advised policies that they had no control over. The public must recognize the important duties our Federal employees perform each and every day on their behalf. Everyday, Federal employees are working tirelessly behind the scenes to ensure that our Nation remains as secure as possible. Everyday, a disaster of some sort is averted through the dedicated efforts of our extremely talented Federal workforce. Yet we often hear stories of blame being assigned to these public servants, rarely about the successes that occur on a daily basis. And while our attention is focused on security, the business of our Nation continues to move forward in an increasingly efficient manner.

All the while, Federal workers at the Departments of Transportation and Justice are providing heightened security of our skies, our shores, and our borders; employees throughout

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the Department of Defense are supporting our warfighters as they continue fighting the war with Iraq as well as the war on terrorism; and the ongoing endeavors of the talented individuals at the Centers for Disease Control are addressing immediate terrorist threats while preparing us for future contingencies. Time and time again, our civil service selflessly responds in a professional manner – all for the greater well-being of the country they serve.

We at FMA would also like to see a review of FEPCA to examine what adjustments need to be made to enable the legislation to work as intended. Any constructive dialogue on FEPCA at this point is better than the hollow act of preempting designated pay increases each and every year, which serves only to exacerbate the low morale that is pervading our civil service.

We also support ways to improve the hiring process for Federal employment, and bring about policies that attract the best and brightest of our society to serve in Public Service. Correspondingly, managers should be afforded the means to continuously enhance their skills. Individual development plans should be devised to maximize each manager's potential. Agencies and departments should increase opportunities for managers to receive training in their respective fields while on-duty by specifically allocating funds for this training. Thus, FMA supports establishing management succession programs to ensure that we have the strongest possible pool of managers to lead tomorrow's civil service.

Finally, we encourage a real and sincere look at Federal pay systems, while encouraging structures that attract, retain, and maintain the Federal workforce we need and desire. The system must be fair and realistic in offering career ladder incentives and progression. Congress must also look at legislation that has been introduced to ensure that Federal retirees and their spouses do not lose benefits they are entitled to receive as being citizens of this great democracy. The time has come to eliminate the penalties and caps placed on a Federal retiree's Social Security benefits. Both Government Pension Offset and the Windfall Elimination Provision must be done away with to allow former civil servants to receive their just rewards for serving their nation and being a citizen of the United States of America.

FMA has long served as a sounding board for the Legislative and Executive branches in an effort to ensure that policy decisions are made rationally and provide the best value for the

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American taxpayer, while recognizing the importance and value of a top-notch civil service for the future. We must keep in mind that even if passed into law, without the necessary funding, no real benefits will be realized – and thus no real progress will be made.

I want to thank you again, Chairwoman Davis, for providing FMA an opportunity to present our views. We at FMA look forward to working with you and other Members of Congress to deal with our government's workforce challenges in our mutual pursuit of excellence in public service. This concludes my prepared remarks. I would be glad to answer any questions you and members of the subcommittee might have.

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Mrs. DAVIS OF VIRGINIA. Thank you, Ms. Heiser.

Once again, I would like to say thank you to all of you for having to wait so long to be able to be our witnesses today.

Ms. Simon, you referred to the survey—and we have all referred to it a lot today—you referred to it and said the questions were in such a way to make it look like pay-for-performance was something that the workers would be interested in. I believe it was only 27 percent who said they felt there was an adequate way to deal with poor performance. Can you speak to poor performers and how the folks in your union feel about the poor performers? It is tough to get rid of them now.

Ms. SIMON. The first thing I would like to say about poor performers is although in the context of today's discussion, we are talking about pay, pay is not the only tool in the toolbox for dealing with poor performance. We really don't think it is appropriate to have a discussion about pay be so focused on how to deal with the problem of poor performers.

Poor performers are a discipline problem. There are certainly procedures on the books that allow managers to deal with poor performers through performance improvement plans, through various forms of discipline including demotion and termination. To suggest that the pay system be radically altered just to use pay as sort of a blunt instrument for punishing people who are judged to be poor performers seems to be inappropriate to us.

Mrs. DAVIS OF VIRGINIA. Has the thought occurred that it might not be to punish the poor performers but to get them to perform better, that rather than punishment, be an incentive to get them to do their work?

Ms. SIMON. I think that is certainly a good idea and I think the procedures for allowing an employee to have an opportunity to improve through a performance improvement plan is already in existence and is not using pay as the exclusive tool for either encouraging someone to improve or punishing them if they haven't.

Mrs. DAVIS OF VIRGINIA. As it stands now, how would an employee doing work over and above, in their opinion, feel that their pay is the same as the poor performer and their increases are the same because everybody's pay increase is the same when they are at the same grade, if I am not mistaken. Is that correct?

Ms. SIMON. If you have a situation like the one you just described, I would say it is really a case of poor management. It is a manager's responsibility to deal with the poor performer. It is a manager's responsibility to sit down with that employee and devise a plan for that employee's improvement and give that person the opportunity, the resources and the assistance he or she may need to improve.

If, in spite of all that, the employee still fails to improve, then it is the manager's responsibility to deal with the poor performer. It is the manager's responsibility if he or she still thinks there is hope, to withhold a step increase when that employee becomes eligible. That is the existing system that does give a manager an opportunity to use the pay system as a performance management tool but then there are hopeless cases, let us face it. When it is the manager's unpleasant duty to either demote or ultimately terminate an employee who isn't pulling his weight.

Mrs. DAVIS OF VIRGINIA. If I am not mistaken on one of the surveys someone reported earlier, 83 percent of the workers had a good performance rating. Yet, how do you justify that with the 27 percent of the folks in the survey who said they did not think the poor performers were being dealt with in a good way. Do you think there are just that few poor performers?

Ms. SIMON. I don't pretend to be an expert on exactly what the questions were in the final survey or the interpretation of the results. As I said in our testimony, we saw draft questions in that poll. We did not see the final poll questions and I haven't had the opportunity to do a really thorough examination of whether or not the way the poll results are being presented is necessarily an accurate way to present that data.

One of the things we know is that this poll was undertaken during a very difficult period for Federal employees. They are facing relentless attacks in many forms but certainly a very aggressive privatization agenda, they are hearing about all kinds of what they consider to be threats to give their managers tremendous discretion over their pay system, and to the extent they express satisfaction with their pay, we believe they are expressing satisfaction with the existing system as compared to some of the alternatives they have heard about that certainly don't make them feel very comfortable given the sort of hostilities they have experienced in the last several months.

Mrs. DAVIS OF VIRGINIA. We have three votes and I want to give my colleague a chance to ask some questions, but I have one quick question for all three of you. Do any of you agree that we need to move to a more market and performance pay based system for the Federal Government to maximize the performance of the Federal people? Do any of you agree with that?

Ms. SIMON. I would say that to the extent we need to move toward a more market based system, the market-based attribute we need to move toward is comparability, that which was promised but never realized through FEPCA.

Mrs. DAVIS OF VIRGINIA. So the dollar figure versus changing the system?

Ms. KELLEY. I agree with the issue of comparability. On the issue of performance, NTEU supports anything that will help the employees to do a better job so they can be successful and so the agencies can be successful. I am not convinced that necessarily means a pay-for-performance as I envision what that means. I truly do believe if everyone in this room were asked to write down what pay-for-performance means on a blank piece of paper, we would have a lot of different definitions of what it is. Therein, I think, lies the problem, but anything to support and to improve the performance and the efficiency of the Federal Government, NTEU and the employees we represent would stand behind that.

Mr. BRANSFORD. SEA supports pay-for-performance. It believes that the SES, the Senior Executive Service has historically been a pay-for-performance system.

When you talk about a market system, I am not sure what that means. If we are talking about the comparability increases and that kind of thing, I agree with my colleagues, but if you are talking about paying executives who do computer work differently from

executives who do program work, I am not sure how you do that. I think that needs more study.

Mrs. DAVIS OF VIRGINIA. Ms. Heiser.

Ms. HEISER. FMA would support a pay-for-performance component without eliminating the annual increases and other types of opportunities available for employees to increase their salary. That aside, on the issue of comparability, we think we need to get away from the old ways of looking at classifications of jobs and how skills are determined to be comparable without regard to the mission of an agency, installation or whatever level those determinations are being made.

Pay-for-performance, we have heard some stories of very negative effects and that does happen because you all made valid issues that managers have to be trained, employees have to buy in, there is no doubt about that. I designed and implemented a very, very successful pay-for-performance system in the private sector before I came into the Federal Government and I can tell you that you are always going to have some subjective component but overall, it was extremely successful. It was a hospital and was based on our mission, our strategic planning, customer service, involved the union and the employees and managers working together.

Mrs. DAVIS OF VIRGINIA. Mr. Davis. I think we probably have another 5 minutes.

Mr. DAVIS OF ILLINOIS. Thank you very much.

I know some of you may have been here when Representative Ruppersberger testified. I don't think you were, Ms. Kelley. If you were, what do you think about gainsharing as a possible way of arriving at pay for performance?

Mr. BRANSFORD. Mr. Davis, I think it is a great idea if it can be quantified. I think that is the problem, quantifying the savings because there are a lot of different ways of counting and if you can figure that out with some level of objectivity so that there really is a taxpayer savings and then reward the employees, I think that is a great incentive.

Ms. SIMON. AFGE had some experience with gainsharing and in general, we support the idea of productivity gainsharing focusing on organizational success and group productivity awards, but there are two things to bear in mind. First of all, we believe even the gainsharing program should be as a supplement to a well funded regular pay system and second, the most successful demonstration project that involved gainsharing, the Pacer Share Program in the Department of Defense, was ended in spite of its success because it cost too much. It did have supplemental funding but the agency decided it was too costly.

Mr. DAVIS OF ILLINOIS. And last, what do you think about privatization? How does privatization relate to what we are trying to accomplish in terms of creating and retaining the work force that we need for the Federal Government?

Ms. HEISER. Privatization is a clear statement that Federal employees are not valued as a starting point.

Ms. KELLEY. I would say the Federal employees see privatization as an intent to move their jobs. It is not about competition and is not about giving them the resources to be able to find the efficiencies and be as successful as everyone talks about on the issue

of privatization. If there were those resources, there is no question the Federal employees could do the job better than anyone else but they are not being given the resources and are expected to deliver on the efficiencies. So there is really no way for them to see the privatization effort other than as a threat to Federal employees doing the work of the Federal Government.

Ms. SIMON. We agree with our colleagues. The privatization quotas that have been imposed by the administration are certainly the worst scourge on the Federal work force right now and I think they, far more than the pay system or any failures of the pay system, explain agencies' difficulties in recruitment and retention.

I think it was very telling that Representative Ruppersberger mentioned the fact that he considered privatization of the grass cutting prior to implementation of the gainsharing program. Unfortunately, with the administration's rewrite of the A–76 process, any kind of strategy or management tool that would try to reorganize or reengineer or do anything to improve productivity is explicitly precluded. The only tool that managers are allowed to use whether or not it saves money is privatization.

Mr. DAVIS OF ILLINOIS. I thank you very much, Madam Chairman. I would just conclude that I guess there are people who would expect the Federal workforce to make bricks without any straw. I thank you very much and it has been a pleasure.

Mrs. DAVIS OF VIRGINIA. Thank you, Mr. Davis.

Unfortunately, we have three votes, not just one, and it is going to be 30 to 45 minutes before we could get back, so I want to say thank you all for coming and if it is OK with you, I have some more questions I would like to submit to you for the record. If I could get you to put them in writing, we will make sure they are distributed to the other members of the subcommittee.

Thank you again for coming and I appreciate your time and patience.

The meeting is adjourned.

[Whereupon, at 3:32 p.m., the subcommittee was adjourned, to reconvene at the call of the Chair.]

[Additional information submitted for the hearing record follows:]

**"Compensation Reform:
How Should the Federal Government Pay Its Employees?"
Subcommittee on Civil Service and Agency Organization**

OPM: I understand a large percentage of employees now under the General Schedule are rated on a simple pass/fail basis. How can meaningful distinctions in performance be made under such a system? Would OPM rule out that kind of a system for an agency to participate in the Human Capital Performance Fund? If an agency doesn't participate in the Fund, will its share be distributed to the participating agencies?

A. Approximately 44 percent of General Schedule employees are rated under pass/fail appraisal systems. Pass/fail appraisal systems taken on their own do not make meaningful distinctions in performance. We counsel agencies that use pass/fail appraisals to determine other ways to make such distinctions. This would normally be through their awards programs. Awards criteria can be linked to organizational goals and employees' specific contributions to those goals. Meaningful distinctions can be made in determining who gets awards and the amounts of those awards.

We anticipate that agencies that use pass/fail appraisals and seek to participate in the Human Capital Performance Fund (HCPF) will have to provide very specific documentation showing how they make meaningful distinctions through their awards programs. We will examine their awards criteria and activities very closely before allotting them their share of the Fund.

If an agency doesn't participate in the Fund, OPM may allocate the agency's share of the Fund to agencies with exceptionally high-quality plans. Such agencies may receive HCPF monies in excess of their full pro rata shares. OPM will base its decision on how well performance ratings in the agency overall link with organizational accomplishments, as well as the agency's past performance under the Fund. HCPF monies (include funds reserved for training) will revert to the Treasury if not disbursed by OPM and/or agencies in the fiscal year in which they are appropriated.

"Compensation Reform:
How Should the Federal Government Pay Its Employees?"
Subcommittee on Civil Service and Agency Organization

OPM: During the past couple of decades, a number of Federal agencies have experimented with broad banded pay systems, under which two or more General Schedule grades and pay ranges are grouped for classification and pay purposes. Some of these "experimental" programs are now more than 20 years old. What is your overall view of the success of these programs? Does OPM believe continued experimentation with the concept of broadbanding is necessary? Other than demonstration projects, how much research has the Administration conducted on pay banding?

A. Pay banding (the currently used term for broadbanding) has been fully tested in demonstration projects. In addition, it has been successfully used in various Government organizations, such as the Department of Defense's (DoD's) Non-Appropriated Fund (NAF) activities and the General Accounting Office. The Administration has been closely studying pay banding as part of its pay reform initiative and in support of the establishment of the Department of Homeland Security (DHS). OPM strongly believes that the pay banding concept has been fully and successfully tested and further testing is not necessary.

"Compensation Reform:
How Should the Federal Government Pay Its Employees?"
Subcommittee on Civil Service and Agency Organization

OPM: Would the administration be willing to give Federal agencies discretionary authority to adopt broad banded pay systems under government-wide criteria established by OPM, without the necessity for developing a demonstration project plan or "alternative personnel system" proposal?

A. Governmentwide criteria established by OPM could improve and streamline the process, particularly because there is and should be no one-size-fits-all approach to implementing a pay banding system. In this regard, the authority granted to the Internal Revenue Service in 5 U.S.C. 9509, at least with respect to the design of broad-banded pay systems in accordance with criteria issued by OPM, has worked effectively. Agencies, working in consultation with OPM as appropriate, would be able to develop more effective and efficient pay banding systems that minimize the chance of unintended adverse impact on employees and programs.

Demonstration project plans are not necessary. However, agencies would be encouraged to consider establishing pilot systems and evaluating those pilots, and OPM would maintain general oversight of these pay systems. It could be effective to require that pay-banding systems be published in the Code of Federal Regulations to clarify the system-specific pay administration policies that would be in effect and to facilitate general management and oversight of the systems.

**"Compensation Reform:
How Should the Federal Government Pay Its Employees?"
Subcommittee on Civil Service and Agency Organization**

OPM: If pay and performance management systems are handed over to individual agencies so they can tailor their systems to their particular needs and objectives, what role in compensation policy do you foresee for OPM?

A. Since 1995, agencies have had a great deal of flexibility to design performance management systems best suited to their needs and objectives. OPM's role since then has been to provide extensive policy guidance and assistance to educate agencies on a wide variety of performance management topics, such as developing employee performance plans that align with agencies' strategic plans, information about successful practices among the agencies, and ways in which to use employee awards to support organizational missions. In addition, OPM has aggressively encouraged agencies to take full advantage of human resources flexibilities to attract and retain well-qualified, high-performing employees.

We continue to see our role as advisor, facilitator, and advocate of pay and performance management systems that allow agencies to provide significant rewards for superior performance. OPM will develop necessary regulations, guidance, and tools needed by agencies to develop strategic plans for recruiting, retaining, developing, and rewarding their workforce. In addition, OPM will continue to administer Governmentwide pay systems like the General Schedule until such systems are replaced by more flexible pay systems.

Even then, OPM would still have a role in managing such pay systems by determining market rates and ensuring Governmentwide consistency in the application of such systems, especially when employees move between Federal agencies. Of course, OPM would maintain its general oversight role, particularly with respect to ensuring the agency-specific systems support the Merit System Principles. Further, OPM would manage any interagency compensation councils that might be chartered to ensure coordination across agencies employing similar occupational groups. Finally, OPM would retain its role as a member of the President's Pay Agent and would continue to be a centralized source of information and analysis for the President and the Congress on matters relating to Federal pay.

**"Compensation Reform:
How Should the Federal Government Pay Its Employees?"
Subcommittee on Civil Service and Agency Organization**

OPM/Sistare: The recent OPM survey showed that 64% (nearly 2/3) of federal employees are satisfied or very satisfied with their pay, but also revealed that 35% are considering leaving their jobs. Doesn't this indicate that perhaps pay is not the source of job dissatisfaction for many federal workers and would it imply that the emphasis should not necessarily be on pay reforms?

A. We realize that many factors influence employee retention and performance, such as job satisfaction and work/life balance. Since the question on our survey did not specifically address satisfaction with our pay system, we hesitate to make a correlation at this time. OPM's leadership role with the Human Capital Initiative is to help create personnel systems that are agile, flexible, and geared toward recruiting and retaining a high-performing workforce. This includes working with agencies on alternative personnel systems, including pay.

However, it is true that the recent survey showed that many employees are satisfied with their pay; considering the size of the Federal workforce, the percentage of those not satisfied with their pay number represent hundreds of thousands of employees—and this represents a serious problem.

OPM/Sistare: If "pay for performance" is a suitable goal, what is the effective answer for dealing with poor performers? According to the Federal Management Association, the current mechanism "is far too cumbersome and takes too long to document."

A. An important aspect of an effective strategy to deal with poor performers is to ensure, through pay-for-performance initiatives, that poor performers do not receive unearned and unwarranted pay increases. Another aspect of dealing with poor performers is to take appropriate remedial action. We understand that the current process, which balances the rights of employees with the rights of management to carry out agency missions, may be perceived as cumbersome and lengthy. There is, however, no substitute for decisive management action concerning poor performers, even if it does take time. OPM has developed materials specifically oriented toward helping managers understand their roles in the process and helping them (and encouraging them) to take appropriate action. At the same time, OPM is on record as advocating increased management flexibilities, as with DHS, to help management act more efficiently and effectively on a range of HRM matters, including actions that might be taken under chapter 43 (performance-based actions) of title 5 of the United States Code.

**"Compensation Reform:
How Should the Federal Government Pay Its Employees?"
Subcommittee on Civil Service and Agency Organization**

OPM/Sistare: Do you believe that the current General Schedule system harms the mission accomplishment and recruiting effectiveness of federal agencies by sending the message that seniority is valued more highly than performance?

A. I believe the current system does far too little to enhance mission accomplishment and encourages highly-motivated prospective employees to turn away from Federal employment because pay raises, within-grades, and career ladder promotions are virtually automatic. The reality is that if you put in your time and do an adequate job, you will receive all across-the-board pay increases just the same as everyone else. Highly-motivated hard-working employees can reap greater financial rewards by working for employers where pay advancement and financial rewards are tied closely to performance.

Annual pay raises in the Federal Government are not dependent on performance at all. All employees, including those receiving unacceptable performance evaluations, receive across-the-board pay increases regardless of level of performance. This pay system sends the message that pay will--and should-- increase with inflation and with the passage of time. Federal employees receive more and greater pay increases simply for remaining on the payroll than for meeting or exceeding performance expectations. For most employees, their time-driven increases have much more value than any awards or raises they receive for outstanding performance. In contrast, private sector companies take great pains to avoid creating pay entitlements and focus instead on the strategic leverage that pay delivery tools provide.

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Response by Hannah Sistare, National Commission on the Public Service to Questions Asked following Subcommittee on Civil Service and Agency Organization April 1, 2003 Hearing.

Q: Do you believe that pay banding, without the presence of specific measurable performance standards, will work as a concept? Did the Commission do any work on performance measures?

The Commission did recognize that performance standards would be needed to implement a performance based compensation system, including a pay banding system. The Commission referred to work done by others, such as OPM and GAO in reaching its conclusions in this area.

Q: Is it realistic to believe we can really implement market-driven reforms in government pay? Will pay banding initiatives get bogged down in employee grievances about political favoritism for certain workers? Did the Commission study any past pay banding cases in federal or state government that prompted it to make the recommendation?

The Commission believes that absolutely, the government is capable of instituting market-based pay reforms. Necessary ingredients are mission clarity (which would be greatly enhanced by mission-based reorganization), performance standards, training for those implementing the system and ongoing oversight by Executive Branch leadership and the Congress. The Commission particularly studied the pay banding system instituted at the GAO. Charles Bowsher, a Commission member, served as Comptroller General for 15 years.

Q: Will a government pay banding system create a lot of resentment among private sector employees who might have to forgo bonuses and pay increases in hard times if their government counterparts are raking in bonuses during a recession? Since government workers don't usually suffer salary cuts or layoffs during a recession, should they receive bonuses during a recession, or any other time?

My own impression is that the existing system, under which federal employees receive annual pay increases completely regardless of performance, causes resentment among private

sector employees and contributes to the bureaucrat bashing that hurts all of the public service. The stereotype of the "do-nothing" federal employee is very destructive. I believe the public would support a fair and transparent system if their elected leaders explained it to them.

Q: Does the recent OPM survey indicate that pay is not the source of job dissatisfaction for many federal workers and would it imply that the emphasis should not necessarily be on pay reforms?

Studies done by the Brookings Institution Center for Public Service indicate that "the job" is the most important motivator of those considering a federal job. The key importance of performance based pay, in the mind of the Commission, is that it will in fact improve performance. It will also improve morale among the vast majority who want to do a good job and also want their efforts recognized.

Q: What is the effective answer for dealing with poor performers?

The Commission agrees with the Federal Management Association that the current mechanism is not effective. Experience has shown that when poor performers are denied pay increases, they leave of their own accord.

Q: Does the General Schedule system send the message that seniority is valued more highly than performance?

Yes.

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May 19, 2003

The Honorable Jo Ann Davis
Chairwoman
Subcommittee on Civil Service and Agency Organization
Committee on Government Reform
House of Representatives

Subject: *Posthearing Questions Related to Pay for Performance*

Dear Madam Chairwoman:

On April 1, I testified before your Subcommittee at a hearing on "Compensation Reform: How Should the Federal Government Pay Its Employees?"[1] This letter responds to your request that I provide answers to follow-up questions from the hearing. Your questions, along with my responses, follow.

1. What standards must an agency implement to safeguard against a pay-fo performance system that might be abused by managers playing favorites?

At the request of Representative Danny Davis, we developed an initial list of possib safeguards for Congress to consider to help ensure that pay for performance systen in the government are fair, effective, and credible. We believe that the following could provide a starting point for developing a set of statutory safeguards in connection with any additional efforts to expand pay for performance systems.

- Assure that the agency's performance management systems (1) link to the agency's strategic plan, related goals, and desired outcomes and (2) result in meaningful distinctions in individual employee performance. This should inclu consideration of critical competencies and achievement of concrete results.

- Involve employees, their representatives, and other stakeholders in the design o the system, including having employees directly involved in validating any relat competencies, as appropriate.

- Assure that certain predecisional internal safeguards exist to help achieve the consistency, equity, nondiscrimination, and nonpoliticization of the performanc management process (e.g., independent reasonableness reviews by Human

[1]U.S. General Accounting Office, *Results-Oriented Cultures: Modern Performance Management Systems Are Needed to Effectively Support Pay for Performance*, GAO-03-612T (Washington, D.C.: Apr. 1, 2003).

Capital Offices and/or Offices of Opportunity and Inclusiveness or their equivalent in connection with the establishment and implementation of a performance appraisal system, as well as reviews of performance rating decisions, pay determinations, and promotion actions before they are finalized to ensure that they are merit-based; internal grievance processes to address employee complaints; and pay panels whose membership is predominately made up of career officials who would consider the results of the performance appraisal process and other information in connection with final pay decisions).

- Assure reasonable transparency and appropriate accountability mechanisms in connection with the results of the performance management process (e.g., publish overall results of performance management and pay decisions while protecting individual confidentiality, and report periodically on internal assessments and employee survey results).

2. I understand a large percentage of employees now under the General Schedule are rated on a simple pass/fail basis. How can meaningful distinctions in performance be made under such a system? Should the Administration rule out that kind of a system for an agency to participate in the Human Capital Performance Fund?

A pass/fail system does not provide enough meaningful information and dispersion in ratings to recognize and reward top performance, help everyone attain their maximum potential, and deal with poor performers. At your request, and at the request of Senator Voinovich, we identified the key practices leading public sector organizations both here and abroad have used for effective performance management.[2] Among these practices is to make meaningful distinctions in performance. We believe that this set of practices can serve as the basis for an agency to demonstrate that it has a performance management system in place that can support pay and other personnel decisions before it would be eligible to participate in the Human Capital Performance Fund.

3. If pay and performance management systems are handed over to individual agencies so they can tailor their systems to their particular needs and objectives, what role in setting compensation policy would you foresee for the Office of Personnel Management (OPM) and the Office of Management and Budget (OMB)?

We have reported that OPM leadership is critical to accomplish its mission in a decentralized human capital environment in which direct accountability for strategic human capital management continues to shift to agencies.[3] In particular, as noted above, OPM should certify that an agency has in place an effective performance management system before the agency is granted the authority to better link pay to performance for broad-based employee groups. In addition, OPM should gather, assess, and disseminate leading practices from federal organizations on a full range of

[2]U.S. General Accounting Office, *Results-Oriented Cultures: Creating a Clear Linkage between Individual Performance and Organizational Success*, GAO-03-488 (Washington, D.C.: Mar. 14, 2003).
[3]U.S. General Accounting Office, *Major Management Challenges and Program Risks: Office of Personnel Management*, GAO-03-115 (Washington, D.C.: January 2003).

innovative human capital policies and procedures, such as pay for performance. Further, OPM should build on its White Paper to design and lead a broad research agenda to develop a more market-based approach to federal pay.

First and foremost, OMB can help to obtain funding for agencies to make the targeted investments that often are needed to develop and implement performance management and related human capital systems. OMB also can continue to help sustain attention on human capital management. For example, in October 2001, OMB notified agencies that they would be assessed against standards for success for each part of the President's Management Agenda, including the strategic management of human capital. The first agency assessment was made public in February 2002 as part of the President's proposed fiscal year 2003 budget. Subsequent assessments were later released on both the status and progress of agency efforts. In October 2002, OMB and OPM approved revised standards for success in the human capital area of the President's Management Agenda, reflecting language that was developed in collaboration with GAO.

4. The General Accounting Office (GAO) report discusses "line of sight" as the overarching principle for effective performance management. What is it and why is it important? Can you highlight the practices that public sector organizations used in their performance management systems to drive internal change and achieve results?

Leading public sector organizations used the key practices I referenced above to create a clear linkage—"line of sight"—between individual performance and organizational success.[4] These organizations have found that to successfully transform themselves, they must often fundamentally change their cultures so that they are more results-oriented, customer-focused, and collaborative in nature. To transform their cultures, high-performing organizations have recognized that an effective performance management system can be a strategic tool to drive internal change and achieve desired results.

5. Things seem to move awfully slowly in the government sometimes. I understand the China Lake pay system experiment is over 20 years old and other experimental systems have also been used for years now. How many tests of pay-for-performance do we need before we decide to go for it across the entire government?

Additional testing of the concept of pay for performance at the federal level is not what is needed at this point. Our experience at GAO and the experiences of others have shown that it is possible to better link employee pay to performance. However, experience also has shown that how it is done, when it is done, and the basis on which it is done can make all the difference in whether or not such efforts are successful. In our view, one key need is to modernize performance management systems in executive agencies so that they are capable of adequately supporting more performance-based pay and other personnel decisions. Unfortunately, based on GAO's past work, most existing federal performance appraisal systems are not designed to support a meaningful performance-based pay system.

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[4]GAO-03-488.

We believe that Congress should consider granting governmentwide pay banding authority in a manner that assures that appropriate performance management systems and safeguards are in place before the new authorities are implemented in any respective agency. This approach would accelerate needed human capital reform throughout the government in a manner that assures reasonable consistency on key principles within the overall civilian workforce. It also would provide agencies with reasonable flexibility while incorporating key safeguards to help maximize the chances of success and minimize the chances of abuse and failure. This approach would also help to maintain a level playing field among federal agencies in competing for talent.

6. GAO's internal pay for performance system is relatively new. How long do you think it will take before we can tell whether it is a success? How did GAO develop its competency-based performance management system? What lessons learned did GAO experience in developing, implementing, and using its new performance management system?

The most prominent change in human capital management that we implemented as a result of the GAO Personnel Act of 1980 was a broadbanded pay for performance system. It should be noted that we had over a decade of experience in the use of pay banding before we undertook our recent changes, so much of the needed organizational infrastructure was already in place. In January 2002, we implemented a new competency-based performance management system that is intended to create a clear linkage between employee performance and our strategic plan and core values.

In designing the new system, GAO involved employees at key points through a variety of channels. Senior management and a diverse cross section of staff selected from across all employee populations reviewed a preliminary competency model. Once developed, all analyst and analyst-related staff across GAO validated the model to ensure the activities and associated behaviors were indeed relevant and important for analyst work. The new policies were put on the GAO intranet for employee comments and appropriate changes were made. We see early results of GAO's implementation of its new competency-based performance management system and other changes to key human capital programs. For example, GAO has achieved greater dispersion in its performance appraisals and merit pay decisions, thus making meaningful distinctions in performance that were not always made in the past.

We realize our approach is not perfect and never will be. High-performing organizations continually review and revise their performance management systems to support their strategic goals. In that spirit, we expect to modify our banded system in the future based on our experience to date.

7. Has GAO found pay for performance efforts that failed?

Yes. Experience from the U.S. and abroad shows pay for performance does not work when modern, effective, credible, and validated performance management systems, with appropriate safeguards, are not in place to support pay decisions and

consequently, employees and managers lose confidence in the fairness of the decisions that are made. At your request, and the request of Senator Voinovich, we are reviewing OPM's personnel demonstration projects where pay for performance systems have been established to identify lessons learned from their experiences. These demonstration projects are required to prepare project designs, conduct employee feedback, and complete evaluations of their results. Of the 17 demonstration projects that have been implemented, 12 have implemented a pay for performance system. The projects have taken a variety of approaches to linking pay to performance and have also made determinations about how much of an employee's pay increase should be "at risk"—that is, the amount of the pay increase that is tied to performance as opposed to provided as an entitlement.

8. When the GAO undertook an assessment of the Federal Aviation Administration's (FAA) pay for performance policy, what was the percentage of employees interviewed by the GAO that stated that the pay system was unfair? What did the employees think was unfair about it?

In February 2003, we reported that FAA's human capital reform efforts were still in progress.[5] Many of the FAA managers and employees we interviewed were critical of the new compensation system. Nearly two-thirds of those responding to our structured interview (110 of 176) disagreed or strongly disagreed that the new pay system is fair to all employees. While we did not attempt to evaluate the concerns raised during the interviews, we did find some evidence that helps explain these perceptions of unfairness. For example, concerns about air traffic controller pay disparities were supported by a Department of Transportation Inspector General report. FAA has since corrected its air traffic control pay policies to clarify differences in pay scales between those controllers in air traffic control facilities and those in regional or headquarters offices. In addition, according to both FAA and external stakeholders, a general perception of unfairness regarding FAA's new compensation system has led to increased unionization among both air traffic service employees as well as those in other FAA business lines.

9. In your research, what performance management system do you find more effective—an individually based reward system or a group based reward system? If rewards are given to individuals as opposed to groups, couldn't this create teamwork problems in situations where collaboration and information sharing are essential to good performance? How do you protect against that kind of behavior? Conversely, if rewards are group-based rather than individual-based, couldn't there be problems in which individuals slack off and hope to benefit from the efforts of others? How do you protect against that kind of behavior?

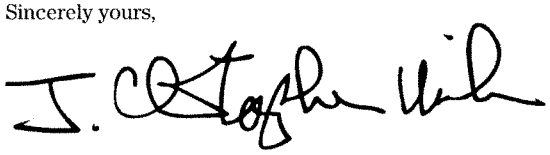
Leading organizations reward individuals based on their contribution to team, unit, and organizational goals. Among the key practices I referenced above is the practice to connect performance expectations to crosscutting organizational goals.[6] That is, if individuals are to be successful in achieving results, they must work collaboratively

[5]U.S. General Accounting Office, *Human Capital Management: FAA's Reform Effort Requires a More Strategic Approach*, GAO-03-156 (Washington, D.C.: Feb. 3, 2003).
[6]GAO-03-488.

with colleagues in other organizational units. To further underscore the importance of teamwork, leading organizations also set individual performance expectations for collaboration, interaction, and teamwork. Finally, leading organizations recognize and celebrate successful teamwork. In our own case at GAO, we are implementing a new awards program to recognize high-impact work that is produced by matrixed teams formed across the organization.

For additional information on our work on federal agency transformation efforts and strategic human capital management, please contact me on 512-6806 or at mihmj@gao.gov.

Sincerely yours,



J. Christopher Mihm
Director, Strategic Issues

(450221)

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"Federal Employee Compensation Reform: How Should the Federal Government Pay Its Employees?"

Subcommittee on Civil Service and Agency Organization, House Committee on Government Reform
April 1, 2003

Questions for the Partnership for Public Service:

1. **You mentioned in your testimony that effective managers are key to both performance management and employee engagement. And in your oral testimony you acknowledged that favoritism or cronyism has been a concern mentioned in moving to a more performance based system with increased manager discretion – can you provide more specifics about how Agencies can address this concern as they implement new systems?**

   Answer: There are several ways to combat favoritism or cronyism starting with the selection and training of managers who exhibit the necessary "people skills" to manage effectively and who are held accountable for results in this regard. Beyond that starting point, however, one also needs a credible performance management system with employee involvement and buy-in from the early planning stages and throughout implementation. That system should be transparent in that it is clear to employees how their performance will be rated and the performance measures are clear, credible, and aligned with clear goals and work outcomes. The performance management system itself should be evaluated at the end of each cycle to determine if adjustments or improvements are needed.

   Additional safeguards against cronyism might include supervisory "peer review" panels that review proposed employee performance ratings and payouts prior to finalization to ensure that there is consistent application of the performance measures across work units. Finally, an annual and anonymous employee survey that solicits employee feedback on their perceptions of the fairness of the performance management system and its application can also yield valuable information that might highlight emerging problems with perceived favoritism. Monitoring the survey trends over time can be especially useful. The results of the employee surveys should be public information and should be provided in as much detail as possible without violating employee privacy and confidentiality.

2. **Are pay-for-performance management systems widely used in the private sector? How effective are such systems?**

   Answer: Pay for performance systems in a multitude of forms are used across the private sector with widely varied results. Those practices range from executive bonus systems, stock programs, sales commissions, production bonuses and targets,

gainsharing, broad based employee bonus/awards practices, etc. If you polled private sector organizations, you would find very few, if any, who would contend that their system is perfect – many would list this as the one feature of their total human capital program that is least effective. Most would report that they are constantly working on refining their systems. All of the elements of human nature that make performance management challenging make pay for performance in any form difficult to perfect.

But, if you look at the studies of high performing organizations, you will note a strong correlation between regular and effective performance feedback – coupled with differentiated pay tied to performance – and strong financial results. (See Becker and Huselid's study of High Performing Work Systems)

3. **How can we shift from an entitlement mentality to an environment that measures and rewards performance? Certainly, there would need to be an intense education, promotion and partnership with employees and their representatives. How long would or could this process take?**

   Answer: As the question correctly implies, a pay for performance approach may well require a basic organizational culture shift. The degree of difficulty associated with making that shift will vary depending on the degree to which each organization's current performance system made meaningful distinctions among employees or employee groups based on their actual accomplishments and contribution, among other factors. It's safe to say that the education, promotion, periodic evaluation and fine-tuning, and partnership with employees or their representatives in the design and implementation of the system could easily take three to seven years. With perseverance and top management support and buy-in, however, eventual benefits in terms of improved employee satisfaction with the system and improved organizational performance should become evident.

4. **How does the federal government become an "employer of choice" in order to attract and retain the "best and the brightest."**

   Answer: This is a multi-tiered issue that will require a multi-tiered response in order to achieve the very desirable objective of having the federal government become an "employer of choice." Since the goal of the federal government is to attract and retain high performing employees, the federal work environment itself should be characterized by:

   -- a clear mission and goals that employees can support and rally around
   -- quality leadership within each organization
   -- a culture of performance which values and rewards employees or employee groups who achieve results that contribute to organizational performance
   -- employees who are empowered to use their skills and abilities to good effect
   -- an emphasis on training and development

-- a high performing work environment that also allows employees to maintain a "quality of life" balance between their work and their personal lives.

However, in addition to these internal conditions, the general public perception of federal employment and federal employees needs attention. Any vestiges of mindless "bureaucrat bashing," should be rooted out and replaced with a celebration of the value of public service and the many contributions federal employees make.

Federal recruitment needs to be improved in many places and doing so will require a combination of executive and legislative branch activities. Within the executive branch, agencies need to devote time and resources to improving the recruitment and applicant assessment process to make it timely, credible, and user-friendly. Federal managers need to be involved and they need to have a sense of ownership of the recruitment and selection process. Agencies need to write attractive, plain-English, and informative vacancy announcements. The revamping of the federal government's main on-line job information website, www.opm.USAJobs.gov, is a step in the right direction. There should also be a revisiting of the sometimes decades old regulatory provisions which place restrictions on the federal hiring process that may no longer be necessary or productive.

Legislatively, unnecessary legal and regulatory requirements that have outlived their usefulness need to be revamped or abolished. A number these requirements have been identified and changes are being proposed or made. This needs to be continued. For example, well-deserved attention is being given to revamping the inflexible federal compensation system to make it both more performance-sensitive and market-sensitive.

5. **What is the feasibility and effectiveness of collapsing our pay grades into broader bands and creating a system which includes: 1) base pay that reflects the level of responsibility and market value of the job, and 2) variable pay that rewards eligible employees for strong contributions to the organization?**

Answer: We know from the documented experiences of over 30 federal organizations operating under demonstration project authority or other special authorities that pay-banding can be an effective alternative to the current General Schedule pay system. More specifically, it is feasible to fashion a pay-banding or broad-banding approach to federal compensation that allows federal employee base pay to be more market-sensitive and which also allows a stronger positive correlation between strong employee contributions to the organization and base pay. Having said that, however, it is also important to note that pay-banding is not a "magic bullet" that can be put into place as a system and expected to automatically improve an organization's human capital management. There is a lot of hard work, collaboration, and commitment that goes into a successful pay-banding system and—as the General Accounting Office has noted—an effective performance management system is a vital base for any pay-banding approach. Finally, any attempts to design a

government-wide, "one-size-fits-all" approach should be avoided. One of the lessons learned from the experiments that have taken place is that an effective pay-banding system must be tailored to the unique mission, culture, and employee demographics of each organization.

6. **How do we measure the success of the system proposed?**

Answer: The success of any pay for performance system will ultimately be determined by the outcomes achieved both in terms of improved organizational performance and relative employee satisfaction and buy-in. Better achievement of GPRA goals and objectives and the results of employee surveys should provide two types of measures. Any pay for performance system should also undergo periodic program evaluation to document its effectiveness and to identify any needed mid-course corrections. The evolution of the system may well take several years to achieve the type of results desired. The first one or two years under a new pay system may well cause some temporary increases in employee dissatisfaction as they adjust to a new way of doing business and the true value of the new approach may only be evident after that period of adjustment.

7. **How does the federal government stack up against the companies featured in Fortune Magazine's "100 Best Companies to Work For" and Working Mother Magazine's "100 Best Companies for Working Mothers."**

Answer: While neither Fortune Magazine or Working Mother Magazine include federal agencies in their employer rating systems, an examination of the basic criteria used suggest that many—but not all—federal agencies compare very favorably to the "Best Places to Work." The recently released results from OPM's "2002 Federal Human Capital Survey," for example, have a number of very positive findings. The Partnership for Public Service, in collaboration with American University's Institute for the Study of Public Policy Implementation plans to conduct some secondary analyses of the OPM data set to better determine the degree of variance among the 189 identified organizational units. Overall, however, even though federal pay might lag behind some private sector employers—particularly for high-performing employees—other factors such as work-life balance and the ability to make a difference—are very positive satisfiers for many federal employees. In many case, unfortunately, federal agencies do a poor job of "marketing" those aspects of the job when recruiting new employees.

8. **Should the federal government more aggressively implement best practices programs such as flexible work arrangements and paid time off banks (leave banks) in order to be competitive in the marketplace and to better meet the needs of the increasingly diverse workforce?**

Answer: Not only should the federal government more aggressively implement best practices programs such as flexible work arrangements and leave banks, but it should also do a much better job of publicizing their existence during recruitment efforts.

9. **Should we adopt a total compensation philosophy and clearly communicate to employees that their compensation package is salary plus medical benefits, pension, training and development, as well as employee assistance programs, group insurance, investment plans and other "perks" such as paid time off, flexible work arrangements, etc., if these become formalized as part of total a compensation package?**

   Answer: A clearly communicated total compensation philosophy makes sense. The major caveat here is that considerable care needs to be taken when determining the relative value of the various components of the compensation package. This is another area where early involvement of federal employees or their representatives in determining the weight of the different components would be advisable. Involving neutral compensation experts from outside government would also be valuable to ensure that the compensation "package," is one that will actually be competitive in its ability to attract and retain highly-qualified and motivated employees.

10. **Have you benchmarked private sector organizations that have implemented a total compensation system with a pay-for-performance component? What companies are best-in-class in this field? What are the lessons learned?**

    We have not conducted a formal benchmarking study but, as mentioned above have done a review of studies conducted and interviews with a number of high performing organizations to determine best practices and lessons learned. Those practices are as follows.

Critical Success Factors for Effective Performance Management

- Establish strategy, objectives and organizational goals
- Communicate organizational goals consistently and continually to employees
- Cascade goals throughout the organization; align performance expectations at all levels – agency leaders, units, individual employees
- Train and develop employees to enhance their ability to contribute
- Provide ongoing feedback and coaching
- Evaluate employees on their contribution to achieving organizational goals
- Differentiate among performance levels in a meaningful way - reward high performers; deal with poor performers
- Continually assess the performance management system – is it improving performance? If not, fix it.

11. *We are aware that there is a level of discomfort regarding managerial discretion in pay for performance. Employees are familiar and comfortable with the current GS Step system and wary of the unknown. Many are concerned that a new system may dispense with the protections they now have. As we know, the newly formed Department of Homeland Security still retains the section on prohibited personnel practices (title 5 § 2302). Clearly, title 5 included this section because there must have been personnel actions whereby employees were discriminated on the basis of race, color, religion, sex, national origin, age, handicapping condition, marital status, and/or political affiliation.*

    Would you elaborate on the retention of these protections and if and how they would relate to any new system of pay for performance? Do you envision that there would be any changes in these protections?

    Answer: The federal government clearly seems to be moving towards a pay for performance system that will allow both variability among agencies in how it is applied and which will also give federal managers greater ability to make decisions that matter with regard to individual employee compensation. This movement is desirable but it should take place within the government-wide framework of both the merit system principles and prohibitions against specific personnel practices such as discrimination based on non-job related factors. In the context of pay-for-performance, it will be important that any pay determinations be based solely on performance and results achieved. However, care will need to be taken to ensure that any process established to decide employee complaints balances the need for managers to have the freedom to exercise reasonable judgment in the context of established standards and the need for employees to have effective recourse where there has clearly been an abuse of that discretion.

Questions for the Record
April 1, 2003
Subcommittee on Civil Service and Agency Organization
American Federation of Government Employees, AFL-CIO

In your opening statement you indicated that under the current system, whether or not an employee is granted a step increase depends upon performance. Could you please tell me the average annual percentage of federal of federal employees whose performance is found to be below expectations and their step increase withheld?

Answer: We contacted OPM for the data to answer that question, but they did not have it for any agency. It is important to note, however, that federal employees are not eligible for step increases each year – eligibility is staggered throughout a career, with opportunity for mobility faster in the early years and slower in later years until it tops out at the top step in a grade.

Is it appropriate to take away the automatic raises tied to years of public service, including those given to under-performers, and convert them to raises linked to job performance?

Answer: There are no "automatic raises tied to years of public service." The only guaranteed "raises" are those passed by the Congress and while these are often called cost of living increases they are based upon the Employment Cost Index (ECI), a measure of broad changes in private sector wages and salaries. They do, however, have the effect of protecting the purchasing power of federal salaries and are an important element of economic security for working families.

Do you agree that we need to move to a more market and performance based approach to the federal pay system to maximize the performance of the federal government for the benefit of the American people?

Answer: AFGE has advocated moving to a more market based approach to federal pay, and that is why we support full comparability adjustments as specified in the Federal Employees Pay Comparability Act (FEPCA). It is because the government has ignored the recommendations of its own Federal Salary Council and Pay Agent to comply with the market-based criteria that are supposed to govern federal pay that salaries in the federal sector continue to lag behind those in both the public and private sector. We also support performance based approaches that use positive financial incentives as supplements to a fully funded, apolitical regular pay system.

In OPM's recent Federal Human Capital Survey, it was revealed that more than 1/3 of federal employees said that they were considering leaving their jobs. In a 2001 OPM report, OPM reported that demonstration projects that have implemented pay-for performance systems have shown increased retention of high performers. Isn't a new compensation system needed, such as pay for performance, to retain the high quality employees so that the government can provide citizens with the most efficient service possible at the best value for taxpayer dollars?

Answer: The advocates of pay for performance systems for government usually make a point of saying that they do not advocate career employment, and that one of the things they dislike about the existing system is that it encourages longevity (what we call loyalty and experience). We think pay for performance encourages a "look out for number 1" attitude that is not consistent with dedication to mission, teamwork, and public spirit.

Would you support government wide pay for performance compensation system if you were ensured that sufficient safeguards were in place to prevent cronyism?

Answer: We already have one, it is called FEPCA.

AFGE has opposed NASA's proposals to move most, if not all for its personnel into a demo that waives certain Title 5 provisions on the grounds that it removes the baseline from which the demo can be tested. NASA believes that having employees under 2 personnel systems will create inevitable resentment and tension in the workplace, since some employees will likely believe that they would be better served in the other system. Should NASA have the opportunity to try an agency-wide project and measure the satisfaction of the employees in the aggregate and avoid the impact on morale caused by competing systems?

Answer: We do not believe that NASA's true rationale is the one referred to in the question. We believe that NASA's request should be looked at as a whole package, and the whole package envisions an assemblage of temporary employees moving between contractor and NASA, with no career workforce overseeing the contractor workforce, and in house capacity to protect the interests of the taxpayer.

A 1998 Human Resources Report stated that title 5 exempt organization made the most reforms in the areas of classification, etc. Fewer differences were found in recruitment and staffing, training, and performance. AFGE has criticized China Lake, but I note that an OPM study shows that 70% of China Lake employees expressed support for the alternative personnel system. Do you have any studies to verify the assertion that employees are unsatisfied in Title 5 exempt organizations?

Answer: Our members tell us that in alternatives to Title 5 like China Lake, the reason so many people are satisfied is that the agency puts extra money in so that no one is any worse off, and the majority are better off. The proposals for governmentwide pay for performance do not consider adding resources to make every one satisfied. Instead, it will be "cost neutral" so that one worker's gain will have to be someone else's loss. That will not create universal, or even 70%, satisfaction.

What advice will you have for DHS when it begins consulting with you on a new system for pay and benefits for employees? With the degree of employee consultation required in the law before implementation, and the guarantee of Title 5 merit system principles and the continued protections against prohibited personnel practices, has this law struck the necessary balance between workers' protections and Department needs?

Answer: There is no justification for authority to waive workers' protections, especially those found in chapter 71. That was and continues to be a purely political threat to bust unions. AFGE's advice to DHS is that just because they have the authority to design a new personnel system and new pay system, they should not think that they are required to design one that is inferior to the one it replaces, or to design one that is more anti-worker. We will encourage them to design one that is not only as good as the existing system, but better for our members and the taxpayer.



May 7, 2003

The Honorable Jo Ann Davis
Chairwoman
Civil Service Subcommittee
U. S. House of Representatives
Washington, D. C. 20515

Dear Chairwoman Davis:

Thank you very much for giving NTEU the opportunity to appear before your Committee recently on the subject of compensation reform.

Attached are my responses to the questions you submitted following that hearing. I apologize for the delay in forwarding these answers to you. If I can provide any further information, please let me know.

Sincerely,

Colleen M. Kelley
National President

Attachment

Questions from April 1 Hearing on Compensation Reform

1) Is it appropriate to take away the automatic raises tied to years of public service, including those given to under-performers, and convert them to raises linked to job performance?

No, it is not appropriate. The annual Employment Cost Index (ECI) portion of the federal pay raise is designed to help bring federal jobs more into line with pay rates in the private sector. The locality pay portion of the annual raise is similarly designed to make the annual raise reflect pay rates in those locations with particularly high labor costs. Although the Federal Employees Pay Comparability Act (FEPCA) has been on the books for more than a decade, it has never been fully implemented. NTEU believes FEPCA must be properly implemented before we begin talking about changing the federal pay structure.

In addition, numerous witnesses at the April 1 hearing, including Comptroller General David Walker and NTEU, raised concerns about the federal government's lack of a fair and appropriate performance appraisal system. The performance appraisal system needs to be overhauled before a workable pay for performance system could be implemented.

2) Do you agree that we need to move to a more market and performance based approach to the federal pay system to maximize the performance of the federal government for the benefit of the American people?

See response to Question 1.

3) In OPM's recent Federal Human Capital Survey, it was revealed that more than 1/3 of federal employees said they were considering leaving their jobs. In a 2001 OPM report, OPM reported that demonstration projects that have implemented pay-for-performance systems have shown increased retention of high performers. Isn't a new compensation system needed, such as a pay-for-performance system, to retain the high quality employees so that the government can provide citizens with the most efficient service possible at the best value for taxpayer dollars?

As NTEU pointed out in its testimony, where pay for performance has been implemented, major concerns have been raised. When the GAO interviewed FAA employees concerning their market-based pay for performance system, nearly two-thirds of the employees interviewed "disagreed, or strongly disagreed that the new pay system is fair to all employees." FPMI Communications undertook a poll of federal workers last October on the subject of pay for performance and two-thirds of the respondents believed

that giving managers more authority on pay would lead to too much favoritism. In still other locations, the introduction of pay for performance has led to infighting and divisiveness instead of cooperation

4) Would you support a government-wide pay for performance compensation system if you were ensured that sufficient safeguards were in place to prevent cronyism?

A fair and unbiased performance appraisal system must be an underlying principle in any pay for performance system. In addition, Congress must be prepared to commit adequate resources to make such a system work. Where pay for performance has been implemented, it is clear that it is not cost neutral. Failure to provide agencies with adequate resources to implement a pay for performance system will doom it to failure. Moreover, managers must be trained to appropriately evaluate employee performance. Writing a fair and unbiased performance appraisal requires a level of skill that most federal managers do not currently possess.

5) If you were going to offer specific policy proposals for reforming or abolishing the General Schedule, what would they be? What would be your proposed reforms that would move us away from a pay system that rewards endurance, but not excellence?

At this time, NTEU does not believe the General Schedule should be abolished. Annual pay raises based on the increase in the Employment Cost Index (ECI) as well as locality pay raises must continue to apply to prevent federal salaries from slipping further behind private sector wages.

6) AFGE has opposed NASA's proposals to move most, if not all, of its personnel into a demonstration project plan that waives certain Title 5 provisions on the grounds that it removes the baseline from which the demonstration project can be tested. NASA, however, believes that having employees under two personnel systems will create inevitable resentment and tension in the workplace, since some employees will likely believe they would be better served to be in the other personnel system, whichever that may be. Should NASA have the opportunity to try an agency-wide project and measure the satisfaction of the employees in the aggregate, and avoid the impact on morale caused by competing statutes?

NTEU does not represent NASA employees and is not familiar with the particular proposal.

7) A 1998 OPM Human Resources Report stated that Title 5-exempt organizations made the most reforms in the areas of classification, compensation, benefits and employee protections. Fewer differences were found in recruitment and staffing, training and performance management. AFGE has criticized the Navy's "China Lake" demonstration project, but I note that an OPM study shows that of the 10,000 employees that are part of the "China Lake" Demonstration Project, more

than 70% expressed support for the alternative personnel system (Per the OPM Report: Demonstration Projects and Alternative Personnel Systems). Do you have any studies to verify the assertion that employees are unsatisfied in the Title 5-exempt organizations?

No NTEU-represented employees participated in the China Lake Demonstration Project and because NTEU does not have an in-depth knowledge of that project, or AFGE's concerns, I think it would be inappropriate for me to comment further.

I might add, however, that NTEU believes that demonstration projects work best when all parties are clear that they have a voice in the process. To this end, we believe that the collective bargaining process is invaluable in ensuring that both management and employees understand the nature of the demonstration project and are committed to its success. Efforts to empower and involve employees in the goals of their agencies leads to employees with commitment and a sense of attachment to their workplaces. Involving employees in decisions before changes are made helps make employees feel a sense of commitment to the process, and a desire to make their workplace as efficient as possible.

8) What advice will you have for the Department of Homeland Security when it begins consulting with you on a new system for pay and benefits for employees in the new Department? With the degree of employee consultation required in the law before implementation, and the guarantee of Title Five Merit System principles and the continued protections against prohibited personnel practices (i.e., whistleblower and nepotism protections), has this law struck the necessary balance between workers' protection and Department needs?

No, I do not believe the law has struck the appropriate balance between workers' protection and Department needs. As you know, the legislation allows the OPM Director and the Secretary of Homeland Security to modify key sections of Title 5, including union rights, pay, performance appraisals, the disciplinary and job classification systems and merit system appeals. The OPM Director and the Secretary must "notify" NTEU 30 days prior to any proposed changes and if the union objects, they must notify Congress and pursue mediation for an additional 30 days. Following that, they may simply implement the changes they have proposed over any objections that may remain.

9) Do employee organizations support targeted pay bonuses for positions of high importance that may be seeing high attrition such as law enforcement, customs and immigration officers on our nation's borders?

Several pieces of legislation pending before Congress seek to provide agencies with additional flexibility in the use of bonuses. I must point out that the key reason bonuses are not used more frequently now is that agencies do not have adequate funding for this purpose. Without additional funding, the only way agencies will be able to increase the

use of bonuses is by further gouging their training budgets and placing added stress on their salary and expense accounts.

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April 25, 2003

VIA HAND DELIVERY

The Honorable Jo Ann Davis
Chairwoman
US House of Representatives
Subcommittee on Civil Service and Agency Organization
B-373A Rayburn House Office Building
Washington, DC 20515

Dear Chairwoman Davis:

Thank you for the opportunity to participate in the Subcommittee hearing "Compensatio Reform: How Should the Federal Government Pay Its Employees" held on Tuesday, April 1, 2003 We appreciate the opportunity to contribute the Senior Executives Association's ideas on pay issue facing the Federal government, most importantly pay compression within the Senior Executiv Service.

This letter is in response to your letter of April 11, 2003. We have included our changes to th transcript in the following pages. In response to your question regarding forced distribution o performance appraisal ratings, we are supportive of agencies first reviewing what monies are availabl for raises and bonuses and then drawing conclusions as to how many people will be awarded the to raises and bonuses. SEA recognizes that a line has to be drawn somewhere due to limited resources However, we are opposed to the arbitrary distribution of ratings, where agencies are limited to only certain number of "outstanding" ratings and are required to give a certain number of ratings that ma be less than fully successful. This may require agencies to unfairly mark down some employee simply to meet the arbitrary distribution requirements.

The Senior Executives Association also participated in the April 8, 2003 joint hearing of th Senate Subcommittee on Oversight of Government Management, the Federal Workforce and th District of Columbia and the House Subcommittee on Civil Service and Agency Organization entitle "The Human Capital Challenge: Offering Solutions and Delivering Results." We will be submittin the answers to questions raised as a result of this hearing in a separate letter.

Please contact us if you have any further questions or if we may provide additional information

Sincerely,

William L. Bransford
Counsel
Senior Executives Association

FMA

Federal Managers Association

FMA Response to Additional Questions from Chairwoman Davis

Compensation Reform in the Federal Government
Subcommittee on Civil Service and Agency Organization
House Government Reform Committee
April 1, 2003

Is it appropriate to take away the automatic raises tied to years of public service, including those given to under-performers, and convert them to raises linked to job performance?

We believe that as long as there is employee participation and input into the process that will be used, a pay for performance system could be an acceptable system. The most vocal complaint from managers is that policy is formed and implemented without consultation. In order to create a pay-for-performance system that is successful, it is necessary to have the input of the supervisors and managers who will be responsible for measuring performance. Without participation from the employees who will be responsible for the implementation of the system as well as its success, the system will never achieve its goals.

Pay for performance could be a good tool to reward performers, while serving as a start to solving problems associated with poor performers. It is absolutely crucial, however, that employees participate in the development of this type of pay system, because without the support and trust of the employees, a pay-for-performance system will not succeed.

Do you agree that we need to move to a more market and performance based approach to the federal pay system to maximize the performance of the federal government for the benefit of the American people?

While FMA is supportive of moving to a more market and performance-based approach to the Federal pay system in order to maximize the performance of the Federal government, any such system must have the support of Federal employees. If the current environment of mistrust continues to dominate the Federal sector, a new pay system will not increase the performance of the Federal government. The principles of merit, fairness, and trust must be included in this process in order to achieve the goal of maximizing the performance of the entire government.

In OPM's recent Federal Human Capital Survey, it was revealed that more than 1/3 of federal employees said they were considering leaving their jobs. In a 2001 OPM report, OPM reported that demonstration projects that have implemented pay-for-performance systems have shown increased retention of high performers. Isn't a new compensation system needed, such as a pay-for-performance system, to retain the high quality employees so that the

government can provide citizens with the most efficient service possible at the best value for taxpayer dollars?

There is no doubt that the compensation system should be examined and modified so as to reward high performance as well as to ensure that supervisors receive pay commensurate with their additional accountability and oversight functions.

The primary obstacle is to ensure fairness in the system as well as implement controls to prevent subjective decision-making from being the sole criterion for raises. Additionally, realistic objective standards and performance measurements need to be set that are achievable. These standards and measurements must be set by the employee-employer providing for a win-win arrangement in an objective-based environment. If a new pay-for-performance system is established in this method, efficient service will be a cornerstone.

Would you support a government-wide pay-for-performance compensation system if you were ensured that sufficient safeguards were in place to prevent cronyism?

FMA would fully support a pay-for performance compensation system if there were sufficient safeguards embedded into the system and all stakeholders had an active role in the development and implementation of the new system. The General Accounting Office has already proposed a list of safeguards that should be used as a starting point for further discussion and enhancement. Again, a government-wide pay-for-performance system will not be successful without the support of Federal employees.

If you were going to offer specific policy proposals for reforming or abolishing the General Schedule, what would they be? What would be your proposed reforms that would move us away from a pay system that rewards endurance, but not excellence?

FMA believes that the pay-for-performance experiences at IRS, FAA, and demonstration projects such as China Lake should be examined to see where the strengths and weaknesses of those systems exist. Pay-banding has been the predominant alternative to the current system; however, agencies should establish mechanisms to ensure that a high-performing employee does not "cap out" within the band. The frustration of the present system is that once an employee caps out, there is no way to reward the individual in the pay system.

As an alternative way to reward performance, the Federal government may want to consider modifying the present GS system to expand beyond the 10^{th} step for those employees deserving of receiving additional pay.

AFGE has opposed NASA's proposals to move most, if not all, of its personnel into a demonstration project plan that waives certain Title 5 provisions on the grounds that it removes the baseline from which the demonstration project can be tested. NASA, however,

believes that having employees under two personnel systems will create inevitable resentment and tension in the workplace, since some employees will likely believe they would be better served to be in the other personnel system, whichever that may be. Should NASA have the opportunity to try an agency-wide project and measure the satisfaction of the employees in the aggregate, and avoid the impact on morale caused by competing systems?

NASA should be able to move its entire workforce into a demonstration project if the assurance is made that there would be a return to the former system should the demonstration project be deemed unsatisfactory by the agency's employees. In order to accomplish this, NASA should be given the authority to roll out a two-year project and allow the employees to assess its results toward the end of the project. If the new system is successful, then the agency should adopt the system permanently. If it needs modification, then changes should follow; and if there needs to be a return to the former provisions, then the agency should return to its original system. Partial movement to a demonstration project inserts a barrier to success from the beginning of the project.

A 1998 OPM Human Resources Report stated that Title 5-exempt organizations made the most reforms in the areas of classification, compensation, benefits, and employee protections. Fewer differences were found in recruitment and staffing, training, and performance management. AFGE has criticized the Navy's "China Lake" demonstration project, but I note that an OPM study shows that of the 10,000 employees that are part of the "China Lake" Demonstration Project, more than 70% expressed support for the alternative personnel system (Per the OPM Report: Demonstration Projects and Alternative Personnel Systems). Do you have any studies to verify the assertion that employees are unsatisfied in Title 5-exempt organizations?

FMA does not know of any such studies that verify the assertion that employees are not satisfied in Title 5-exempt organizations.

What advice will you have for the Department of Homeland Security when it begins consulting with you on a new system for pay and benefits for employees in the new Department? With the degree of employee consultation required in the law before implementation, and the guarantee of Title Five Merit System principles and the continued protections against prohibited personnel practices (i.e., whistleblower and nepotism protections), has this law struck the necessary balance between workers' protection and Department needs?

Since the Department of Homeland Security (DHS) began the development of its new personnel system, we at FMA have not been asked to participate in the consultation and development phases. We have formally asked DHS for inclusion on the design team for the new personnel system, but as yet have not received an invitation to participate.

While there has been much talk of DHS consulting with employees and employee organizations, it is still unclear how much employee participation has occurred.

It remains to be seen if a balance has been struck for worker's protections and Department needs. Unfortunately, it will not become clear until the rules are drafted and implemented and the Department is fully operational under the new personnel system – and quite possibly, long thereafter.

Do employee organizations support targeted pay bonuses for positions of high importance that may be seeing high attrition, such as law enforcement, customs, and immigration officers on our nation's borders?

FMA supports pay bonuses and incentives for critical skill needs. The debate stems from what the agency – and the employees – deems critical. In our public depots the hard-working skilled artisans that perform extraordinary tasks every day are aging and as a result having to deal with physical challenges. Investment in replacing these older workers through the expansion of apprenticeship programs and school-to-work initiatives for high school students needs to continue and increase. There must be some foresight in the area of succession planning in order to allow our experienced employees to mentor those new workers we bring on board.

While we understand and fully support the need to retain Federal employees who serve as law enforcement officers, the government must understand that these are not the only critical positions in the civil service.

