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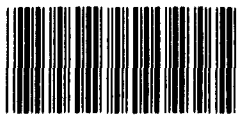
GAO Testimony



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H.R. 4716, "Federal Pay Reform Act of 1990"

Statement of
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for General Government Programs

For the
Subcommittee on Compensation and Employee Benefits
Committee on Post Office and Civil Service
House of Representatives

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H.R. 4716, "FEDERAL PAY REFORM ACT OF 1990

Summary of Statement by
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Assistant Comptroller General for General Government Programs

GAO believes it is essential that federal pay setting principles and processes be changed. The large pay gap that has developed between federal and nonfederal salary rates is causing recruitment and retention difficulties. Thus, GAO evaluated the bill from the standpoint of the extent to which it would restore competitive salary rates and assure that, once restored, they are maintained.

In GAO's opinion, certain elements of H.R. 4716 can help lead to meaningful pay reform.

-- It moves federal pay setting away from the current practice of paying the same salary rates nationwide by calling for locality-based schedules for clerical and technical employees and geographic differentials for professional and administrative employees who would continue to be paid on a national schedule. GAO agrees that federal salaries must be competitive by locality to attract and retain high-quality employees, but points out several inequities and difficulties that could result from using different approaches for the two employee groups.

-- It adds state and local governments to the surveys of prevailing nonfederal salaries as GAO has long urged be done.

-- It incorporates a form of performance-based pay adjustments for individual employees. GAO believes the concept of pay-for-performance is sound, and, in particular, believes the proposal that employees whose job performance is not fully satisfactory would not receive pay increases when salary schedules are adjusted deserves serious consideration.

Although GAO supports the overall objective of pay reform as embodied in H.R. 4716, it remains concerned that the unlimited Presidential prerogatives over salary schedule adjustments, which would be continued under the bill, will not provide adequate assurance that federal salary rates will be set and kept at competitive levels.

Mr. Chairman and Members of the Subcommittee:

We welcome the opportunity to provide our analysis of H.R. 4716, the proposed "Federal Pay Reform Act of 1990," as prepared by the Office of Personnel Management (OPM).

As you will recall from our appearance before the subcommittee on March 14, 1990, GAO strongly endorses actions to reform federal pay setting principles and processes. Noncompetitive salary rates are a major cause of federal employee recruitment and retention difficulties. We are convinced that the currently significant pay disparities can no longer be tolerated as they seriously jeopardize the government's ability to compete for and hire the quality employees needed to deliver services to the American people.

We fully understand that current budget realities prevent paying federal employees salary levels comparable to those their nonfederal counterparts receive for similar work. Nevertheless, we believe the idea of paying federal employees at rates that are at least competitive with the nonfederal sector must be a basic tenet of the government's compensation philosophy. Thus, in our opinion, H.R. 4716, like any other pay reform proposal, must be judged on the extent to which it will restore competitive salary rates and assure that, once restored, they are maintained.

We support several elements of H.R. 4716. It reflects our position that the practice of paying the same salary rates nationwide regardless of local economic conditions is inappropriate. It also incorporates a form of performance-based pay adjustments for individual employees. We believe the concept of pay-for-performance is sound and in line with what we understand typical private sector practice to be.

We are concerned, however, with several of the bill's specific approaches to accomplishing these objectives. For example, in our opinion, the bill does not provide adequate assurance that federal salary rates will be set and kept at competitive levels or that the adjustment processess will be understood and accepted by federal employees.

The bill proposes numerous changes to the government's pay system. Following are our comments focusing on those aspects of the bill that we consider to be the most important.

Salary Schedule Adjustments

H.R. 4716 calls for somewhat similar procedures for adjusting annually the salary schedules for professional and administrative employees paid under the proposed National Pay System (NS) and clerical and technical employees paid under the proposed Locality Pay System (LS). The current "Pay Agent" concept would be retained with certain additional responsibilities assigned to the Director of OPM. The Pay Agent would determine, based on Bureau of Labor Statistics (BLS) salary surveys, the prevailing nonfederal rates for jobs comparable to those in government. This part of the process appears to be the same as the current method of comparing federal and nonfederal salaries, except that state and local governments would be included in the salary surveys. We agree with this change, having long advocated expanding the surveys to include other governments' salaries.

However, the proposed pay adjustment determination processes would vary considerably from current procedures. The Pay Agent would recommend to the President, at its sole discretion, salary schedule adjustments that would put basic pay rates anywhere within a range of plus or minus 10 percent of nonfederal comparability amounts. The bill gives the Pay Agent discretion

to consider several factors in making the recommendation, including federal turnover and vacancy rates, unemployment rates and trends for nonfederal workers, trends in the quality of federal employees, and the "need to provide Government services economically." Recommendations within a range are not allowed under the current statute.

The bill grants the President authority to put the salary adjustments recommended by the Pay Agent into effect or make lesser adjustments if he believes such action is appropriate because of a "national emergency" or "serious economic conditions affecting the general welfare." If a lesser adjustment is made, the President would be required to report to Congress his reasoning for the smaller amount, including an assessment of the impact of the decision on the government's ability to recruit and retain well qualified employees.

In effect, the bill would continue to allow the President complete discretion in determining salary schedule adjustments. As such, we are concerned that the bill does not constitute meaningful pay reform and gives little assurance that adjustments related to the survey results will actually occur. Pursuant to the current statute, Presidents have consistently attributed less than comparability adjustments to the existence of a national emergency or economic conditions affecting the general welfare every year since 1978. These alternative adjustments are the reason for the large gap that now exists between federal and nonfederal salary levels.

A rigid "formula-based" adjustment process may be too restrictive and some latitude in determining adjustment amounts is warranted. But, the unlimited latitude allowed under H.R. 4716 is too broad. A middle ground allowing a degree of limited flexibility appears to be in order. One possible compromise could be to limit the President's authority to grant alternative adjustments to a

maximum amount, such as 5 or 10 percent below comparability rates. Another possibility is to prescribe that, in any given year, the President must make pay adjustments at least equal to the percentage increase in nonfederal salaries during the previous year. Other workable approaches also undoubtedly exist.

The reasoning is unclear behind one aspect of the proposed process for adjusting LS pay schedules. Under the LS approach, OPM would make the "plus or minus 10 percent" determinations for each pay area and report its determinations to the Pay Agent. The Pay Agent would then convert the OPM determinations to an overall average percentage for all LS pay areas and recommend to the President the overall percentage adjustment that should be granted. Once the President had decided what overall percentage to grant, using the approach previously discussed, OPM would then, at its discretion, decide how to allocate the approved adjustment to each pay area. We do not see what purpose is served by limiting the President's decisionmaking to an overall average if the objective is to make salary rates more competitive with nonfederal rates in each locality where clerical and technical employees work. Our analyses of nonfederal pay rates for such employees indicate that wide variances exist among geographic locations, and we see no reason why pay adjustment decisions should not be made on a locality-by-locality basis. Localized pay adjustment decisions could also permit consideration of cost-of-living differences throughout the country, which we believe should be a factor, along with nonfederal salary rates, in making salary decisions for specific localities.

Locality Pay

H.R. 4716 calls for professional and administrative employees to continue to be paid under a national salary schedule known as the NS and clerical and technical employees to be paid under local

salary schedules known as LS. According to the bill, the NS schedule would cover classes of positions for which the government recruits nationally and whose incumbents are usually college graduates. The bill describes LS positions as typically those for which the government recruits locally and whose incumbents are not usually expected to be college graduates. OPM would be responsible for determining which positions would be placed under each schedule.

The bill provides for locality-based pay for each of the two groups, albeit in considerably different manners. The LS schedules would be based, in large part, on prevailing nonfederal salaries in each pay area. To recognize local variations in nonfederal salaries for professional and administrative occupations under the NS schedule, the bill allows the Pay Agent to authorize geographic differentials of up to 25 percent in any geographic areas or localities where the national NS rate would be so low as to cause the government serious difficulties in recuriting or retaining employees.

While we agree that salary rates for all employees should be based on local economic factors, including prevailing salaries, we are not convinced that the proposed differences in locality pay approaches for the two groups are appropriate. Under the proposal, for example, local salaries under the LS schedules would all be basic pay for retirement benefit calculations and other purposes, but the geographic differentials for employees under the NS schedule would not be basic pay. We see no justification for this difference.

Based on data developed by OPM in its pay study, as well as our own work, we also believe a 25 percent geographic differential may be insufficient to restore federal professional and administrative salaries to competitive levels in many locations. An August 1989 OPM report showed that nonfederal rates for

professional and administrative occupations varied virtually as much by locality as did rates for clerical and technical employees. For example, OPM found nonfederal pay rates for jobs equivalent to GS-7 accountants ranged from $19,912 in the lowest paying locality, to a high of $30,432 in the highest paying locality--a 52.83 percent spread. The average GS-7 salary (step 5) at the time was $21,222. Rates for contract specialists equivalent to the GS-11 level ranged from $28,148 to $49,711 by locality, a difference of 76.61 percent. The GS-11 step 5 rate was $31,412. We suggest the 25 percent limitation on NS geographic differentials should be removed, particularly since the bill does not limit LS salary levels in any locality.

Using separate salary schedules could also result in employees with equivalent jobs in a locality being paid different salaries. Under the current General Schedule system, they are paid the same amounts. For example, employees now classified at GS-7 would become either LS-7s or NS-12s under the proposed new salary system, while retaining their equivalent job responsibilities.

Another difficulty that could arise in many localities from the different locality pay approaches is the "pay inversions" that could occur if supervisors on national NS rates are paid less than their subordinates on local LS rates. The bill recognizes the potential pay inversions by providing a supervisory differential of up to 3 percent of pay if necessary for supervisors to make more than their subordinates under a different pay system. However, the supervisory differential would not be part of basic pay for retirement calculations and other purposes. Payment of the supervisory differential could also result in other supervisors, at the same level, being paid less simply because they do not have subordinates under a different pay system.

In our opinion, the two different locality pay approaches present such potential inequities that serious consideration should be given to using one approach for all employee groups. Of the two, we favor the NS approach. We believe there is considerable justification for being able to tell prospective employees as well as transferring employees that basic pay rates are consistent across government with geographic differentials paid in areas where local economic conditions so dictate. As a possible compromise to maintain some relationship between income levels during employment and retirement, perhaps one-half of the geographic differential could be counted as basic pay for retirement and other benefit determination purposes.

Other Proposed Salary Differentials for the NS and LS Systems

H.R. 4716 contains a number of differentials that could be added to NS and LS salary rates in specified circumstances. None of the differentials would be basic pay. They include:

1. Staffing differentials of up to 60 percent of basic pay for particular occupations or grades when federal salary rates are insufficient to recruit and retain employees. The staffing differential would replace the "special rate" program currently authorized by law to counter recruitment and retention difficulties caused by higher private sector pay for particular occupational groups. Special rates are now part of basic pay and are limited to a maximum additional amount of 30 percent. Under the bill, staffing differentials would be continuing payments, but they could be adjusted or eliminated at any time.

2. Recruitment and relocation bonuses of up to 25 percent of basic pay that may be paid when a newly appointed or current employee must relocate to accept a position and OPM

determines that the agency would be likely to encounter difficulty in filling the position without the bonus. The bonus would be a one-time, lump-sum payment, and the employee would be required to serve a specific period of employment with the agency or repay a pro rata amount of the bonus.

3. Retention allowances of up to 25 percent of basic pay that OPM may authorize agencies to pay to employees whose services are essential to an agency, but are likely to leave the agency if the retention allowance is not paid. The allowance would apparently be a continuing payment, but it could be reduced or eliminated at the agency's discretion.

In general, there should be limited need for these extra payments if federal salaries were reasonable and competitive with prevailing nonfederal salaries in any given locality. Therefore, to the extent that they are intended to be a "stop gap" measure to accommodate inadequate salary rates, we believe they are an inappropriate approach to salary reform.

We are also concerned about the potential unevenness of application of the recruitment and relocation bonus and the retention allowance. Considerable judgment could apparently be exercised in deciding when and to whom such payments could be made, and the opportunity for inequities to result could certainly exist.

We agree that a mechanism such as the proposed staffing differential, or the current special rates program, is needed for those cases where nonfederal salaries for particular occupations are greater than the federal rates being paid to employees in all occupations at any given grade level. Because of the averaging process used in establishing federal salary levels, occupations with nonfederal rates higher than the overall average may need to

be paid more for the government to be competitive. However, significant opportunities for inequities to occur exist here too. Under the current special rates program, OPM will not approve an agency's special rate request unless the agency will certify that it has sufficient resources to pay the higher amounts within its existing budget. Thus, an agency's budget situation, rather than a demonstrated need for more competitive salary levels, is often the chief determinant of whether special rates will be paid. The same shortcoming could exist with staffing differentials. Also, since the higher amounts paid under the staffing differential are primarily intended to make federal salary levels competitive with salaries paid to nonfederal employees in the applicable occupations and localities, we believe at least some portion of the differential should be counted as federal basic pay as well.

Pay for Performance

GAO adopted a pay-for-performance system last year that contains some provisions similar to those in H.R. 4716. We believe that a pay-for-performance system, if properly designed and implemented, can work in the government. Also, as we reported to you in our appearance on March 14, 1990, our survey of private sector company practices indicates that few companies give automatic pay increases to all employees when salary schedules are adjusted.

In general, the bill calls for the current 10-step within-grade advancement system, with its 30-percent salary range at each grade, to be replaced with a 40-percent range at each grade and no steps. When overall schedule adjustments are made, employees whose performance is rated at the fully satisfactory level or higher would receive the general increases. Under current law, all employees, regardless of performance level, receive general increases. We believe this approach deserves serious consideration as it seems reasonable to us that employees who are

not doing satisfactory work should not get the same pay increases as satisfactory employees.

However, we noted that the bill (sections 5304 and 5334) calls for the general increases paid to individual employees not to be percentage increases as is now the case, i.e., all employees received raises equal to 3.6 percent of their actual salaries in January 1990. Rather, each eligible employee would receive the same dollar amount by which the minimum rate of the employee's grade is increased, meaning that employees at higher steps in each grade would receive successively smaller percentage increases. It is not apparent to us why this change in general adjustment practices was proposed, particularly since the overall schedule adjustment percentages are based, in large part, on comparisons of actual salary levels being paid in the federal and nonfederal sectors. Again using the January 1990 adjustment of 3.6 percent as an illustration, employees at step 4 of each grade would have received a 3.3 percent raise if the proposed adjustment process had been in effect, and employees at step 10 would have received 2.8 percent. To us, this proposed change appears unwarranted and inequitable to employees at salary levels above the minimum rates of their grades.

H.R. 4716 presents few specifics on how employees would progress through the pay ranges based on their performance, i.e., merit increases, in lieu of the current within-grade increases that are paid to all employees whose work is rated as fully satisfactory or higher. It provides that agency heads would make this determination subject to such regulations and criteria as OPM would prescribe. Therefore, without knowing how the merit increase process might work, it is difficult for us to evaluate this aspect of the proposal.

The bill does indicate, however, that the merit increase process for employees under the NS salary schedule could differ

considerably from the process for employees under the LS schedules. The proposal calls for merit increases for LS employees to be no less than 3 percent of basic pay each year for employees in the lower one-third of the pay range in each grade and no less than 3 percent each two years for employees between the lower one-third and the mid-point of the pay range. No such minimums would be guaranteed for NS employees. We know of no reason why the merit increase processes for the two groups should differ.

Other Provisions

H.R. 4716 contains a number of other provisions, for most of which we have no comments to offer. We do have some observations, however, on the changes proposed for the Federal Wage System for blue-collar employees.

The bill calls for changes to the Federal Wage System that, among other things, would allow the President to limit wage rate adjustments in any wage area if he believes such limitations are needed to provide equity with the NS and LS salary systems. Under current law, the President has no authority to limit adjustment amounts under the system, and annual adjustments necessary to maintain comparability with the private sector are required to be given. However, appropriations limitations imposed by Congress in recent years have restricted blue-collar wage adjustments to amounts no greater than the percentage adjustments granted to white-collar employees under the General Schedule. As a result, large pay gaps with the private sector now exist in many wage areas. While we believe equitable pay rates are needed for all federal employees, we would agree that pay adjustment determinations for all pay systems, including any pay limitation decisions, should be consistently applied. Accordingly, we believe the proposed expansion of Presidential

prerogative to include Federal Wage System adjustments is appropriate.

The bill also calls for changing the method by which general adjustments to the Federal Wage System are determined. Each grade in the system includes five steps, and step 2 is considered to be the "pay line," that is, the rate comparable to average private sector wage rates at each grade. Step 1 is set at 96 percent of the pay line; step 3 at 104 percent; step 4 at 108 percent; and step 5 at 112 percent. Under the bill, the pay line would be set at step 3 and the percentages for the other steps would be reduced accordingly, i.e., step 1 would be set at 92 percent and step 5 would be set at 108 percent. We agree that the pay line determination procedures for the system should be changed. Most employees under the system are at step 4 or 5, meaning that, had the appropriations limitations not been imposed, they would be paid more than their private sector counterparts, since the pay line is set at step 2. However, we believe raising the pay line to step 3 is insufficient since most employees are above that step as well. Some years ago, at our recommendation, the General Schedule pay line determination procedure was changed to provide for comparing the overall average salary at each grade with the private sector average rather than using a specific step of the grade as the pay line. Until that time, step 4 of each General Schedule grade had been used as the pay line. We believe the same average-to-average comparison approach should be used for the Federal Wage System, which would result in the pay line being established at about step 4 of the 5-step system.

We trust that our comments on the bill will be helpful to the subcommittee.