



**Statement of Curtis W. Copeland
Specialist in American National Government
Congressional Research Service**

Before

**The Committee on Oversight and Government Reform
Subcommittee on Federal Workforce, Postal Service, and the District of Columbia
House of Representatives**

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on

“Federal Pay Policies and Administration”

Chairman Davis and Members of the Subcommittee:

I am pleased to be here today to discuss certain issues related to federal pay policies and their administration. In preparing the testimony, I closely collaborated with my CRS colleague, Barbara Schwemle.

Federal pay and compensation is a significant, perennial issue facing Congress for a variety of reasons. First, as one might expect, changes to federal rates of pay and the manner in which those rates are determined are of interest to the nearly 2 million members of the federal workforce, and are therefore of interest to many Members of Congress who represent those employees. Also, federal pay is always a major budgetary item. According to the President’s FY2008 budget request, actual federal civilian compensation costs in FY2006 were nearly \$100 billion, and those costs are expected to approach \$110 billion by FY2008.¹ Total civilian and military compensation and benefits were estimated to be more than \$370 billion in FY2008. Finally, federal pay is a key component in allowing agencies to attract and retain the workforce they need to accomplish their missions.

¹ Office of Management and Budget, *Object Class Analysis: Budget of the U.S. Government, Fiscal Year 2008*, p. 11, available at [<http://www.whitehouse.gov/omb/budget/fy2008/pdf/objclass.pdf>].

There are literally dozens of government-wide and agency, institution, or occupation-specific federal pay systems currently in effect, including schedules for the federal judiciary, Congress, blue-collar workers, health care workers in the Department of Veterans Affairs, administrative law judges, and the military. My testimony will focus on the major federal white-collar pay schedules, and will discuss some of the current issues related to those schedules. In brief, those issues are (1) the annual pay adjustment process pursuant to (or, perhaps more accurately, in spite of) the Federal Employees Pay Comparability Act of 1990; (2) pay compression within and between the different pay schedules; and (3) various reform efforts in recent years, including performance-based pay, market-based pay, and proposals to change the pay system for employees living in what are known as “non-foreign” areas of the United States.

Major Federal White-Collar Pay Schedules

First, however, I would like to provide a brief overview of the major white-collar federal pay schedules — the General Schedule (GS), the schedule for Senior Level (SL) and Scientific or Professional (ST) positions, the Senior Executive Service (SES) schedule, and the Executive Schedule (EX). **Appendix I** of my testimony provides summary information on each of these four schedules.

Created by the Classification Act of 1949, the GS pay system is by far the largest, with more than 1.3 million of the federal government’s 1.8 million employees in the GS or GS-related pay systems as of March 2007. The GS is divided into 15 grades of difficulty and responsibility of work, with 10 steps within each grade that employees progress across through longevity and at least an acceptable level of performance. The salaries associated with each GS grade and step currently vary by locality; in Washington, DC they range from a low of \$19,722 to a high of \$143,471. By statute (5 U.S.C. §5303), base GS pay (i.e., without the locality differential) cannot exceed Level V of the Executive Schedule (currently \$136,200). Base pay and locality pay combined cannot exceed Level IV of the Executive Schedule (5 U.S.C. §5304(g)(1), currently \$145,400).

The Executive Schedule (EX), established by Section 303 of P.L. 88-426 in August 1964, consists of five pay levels. Generally, Level I of EX (hereinafter, EX-I) includes cabinet-level officials; Level II includes deputy secretaries of departments, secretaries of military departments, and heads of major agencies; Level III includes under secretaries of departments and heads of middle-level agencies; Level IV includes assistant secretaries and general counsels of departments, heads of smaller agencies, and members of certain boards and commissions; and Level V includes administrators, commissioners, directors, and members of boards, commissions, or units of agencies. EX-I through EX-V positions are specified in statute at 5 U.S.C. §§5312-5316. As of March 2007, the Executive Schedule covered 475 employees in the highest levels of federal agencies. Of these, 280 were in cabinet departments, including 36 in the Department of Defense (DOD), 31 in the State Department, 25 in the Department of Justice (DOJ), and 21 each in the Departments of Commerce, Energy, and the Treasury.

The Senior-Level (SL) and Scientific or Professional (ST) pay schedules cover positions above GS-15 and in scientific or professional positions. Section 102 of P.L. 101-509, the Federal Employees Pay Comparability Act of 1990, enacted on November 5, 1990, established the SL and ST schedules by combining the positions at grades GS-16, GS-17, and GS-18. As of March 2007, the SL and ST schedules covered 928 employees, including 152

in DOD, 116 in the Smithsonian Institution, 86 in DOJ, and 73 in the Department of the Interior.

The Senior Executive Service (SES) was established by the Civil Service Reform Act of 1978 (P.L. 95-454), and, as of March 2007, covered more than 7,300 federal executives — more than 6,400 of whom are career employees selected for the SES by meeting executive core qualifications. Noncareer SES appointees do not have to meet the same competitive selection requirements, but they also do not receive the same entitlements as career senior executives. As of March 2007, nearly 75% of the SES were in Washington, DC, Virginia, or Maryland, and the agencies with the largest number of SES employees were DOD (1,215) and DOJ (678). A new pay system for the SES was established in 2004 by Section 1125 of the FY2004 National Defense Authorization Act (P.L. 108-136). Key features of the new pay system, which took effect in January 2004, include the elimination of locality pay and annual pay adjustments (which were provided in conjunction with annual adjustments for General Schedule and Executive Schedule employees); the replacement of six pay rates (ES-1 through ES-6) with one broad pay range (\$111,676 to \$154,600 as of January 2007); an increase in the cap on base pay from EX-IV to EX-III; and the addition of a second, higher cap, EX-II, for SES appraisal systems that have been certified by OPM as making “meaningful distinctions” among employees based on relative performance.

Annual Pay Adjustments

A perennial issue of concern to federal employees (and to many Members of Congress) is the size and timing of the annual pay adjustment for GS employees. Although commonly referred to as a “cost of living adjustment” or “COLA,” the pay adjustment is actually two adjustments, and has little to do with cost of living. Rather, it is driven by (1) changes in the cost of labor nationwide and (2) comparisons of non-federal and federal pay within particular localities.

Annual adjustments for federal employees under the GS and certain other systems are governed by Section 529 of Public Law 101-509, the Federal Employees Pay Comparability Act of 1990 (FEPCA), which generally requires that covered employees receive an annual basic pay adjustment and a locality-based comparability payment. The same amount of basic pay adjustment is provided to all covered employees, and is based on the Bureau of Labor Statistics (BLS) Employment Cost Index (ECI), which measures changes in private sector wages and salaries. Federal pay rates are generally required to be increased by an amount that is 0.5% less than the percentage change in the ECI from one year to the next, but the law stipulates a 15-month lag at the time of each adjustment. For example, the pay increase for January 2008 will be based on the percentage change in the ECI from the quarter ending on September 30, 2005, to the quarter ending on September 30, 2006. The ECI change for this period was 3.0%, so this formula indicates that the basic pay adjustment (i.e., without the locality differential) for January 2008 would be 2.5%. However, FEPCA also authorizes the President to issue an alternative pay plan (by September 1 of the year prior to the scheduled effective date) in the event of a national emergency or serious economic conditions affecting the general welfare. For the January 2008 adjustment, therefore, an alternative pay plan would need to be authorized by September 1, 2007.

The locality portion of the annual adjustment for GS and other employees is based on a comparison of federal pay rates for particular positions to non-federal rates of pay (as measured by BLS surveys) within designated local pay areas. In January 2008, there will be

32 such local pay areas (including one called “Rest of the United States”). FEPCA provides that payments are to be made within each locality in which federal pay rates lag behind non-federal rates by more than 5%. However, as was the case for the basic adjustment, FEPCA also permits the President to establish an alternative level of locality-based comparability payments because of a national emergency or serious economic conditions affecting the general welfare. To do so, the President must transmit a report to Congress at least one month before the comparability payments would be payable that describes the alternative level of payments and why the alternative level is necessary.

This complicated formula for calculating basic and locality payments notwithstanding, FEPCA has never been implemented without presidential or congressional intervention. No annual basic pay adjustment was made in 1994, and the adjustment was reduced in 1995, 1996, and 1998. Reduced amounts of locality payments were provided in 1995 through 2007. **Table 1** below shows the annual and locality pay adjustments made under FEPCA for the years 1991 through 2007.

Table 1. Annual and Locality Pay Adjustments Under FEPCA, 1991 to 2007

Year	ECI-Based Annual Adjustment Required by FEPCA	Annual Adjustment Authorized	Locality Payments Required by FEPCA (National Average)	Locality Payments Authorized (National Average)	Net Increase, Annual and Locality Pay (National Average, Weighted)
1991	—	4.1%	—	—	4.1%
1992	4.2%	4.2%	—	—	4.2%
1993	3.7%	3.7%	—	—	3.7%
1994	2.2%	0	3.95%	3.95%	3.95%
1995	2.6%	2.0%	6.44%	5.05%	3.08%
1996	2.4%	2.0%	8.58%	5.56%	2.49%
1997	2.3%	2.3%	11.29%	6.37%	3.09%
1998	2.8%	2.3%	14.30%	6.93%	2.84%
1999	3.1%	3.1%	16.95%	7.50%	3.65%
2000	3.8%	3.8%	20.62%	8.62%	4.89%
2001	2.7%	2.7%	23.12%	9.77%	3.76%
2002	3.6%	3.6%	25.92%	10.95%	4.72%
2003	3.1%	3.1%	27.59%	12.12%	4.21%
2004	2.7%	2.7%	25.71%	13.81%	4.24%
2005	2.5%	2.5%	25.51%	15.01%	3.54%
2006	2.1%	2.1%	25.85%	16.22%	3.19%
2007	1.7%	1.7%	24.15%	16.80%	2.24%

Sources: For the ECI-required annual adjustment, see U.S. Department of Labor, Bureau of Labor Statistics, *Employment Cost Index*, Sept. of each year. For the locality payments required by FEPCA, see *Report on Locality-Based Comparability Payments for the General Schedule, Annual Report of the President's Pay Agent*, Dec. of each year. For the annual and locality pay adjustments authorized, see E.O. 12736, Dec. 12, 1990; E.O. 12786, Dec. 26, 1991; E.O. 12826, Dec. 30, 1992; presidential memorandum of Dec. 1, 1993; E.O. 12944, Dec. 28, 1994; E.O. 12984, Dec. 28, 1995; E.O. 13033, Dec. 27, 1996; E.O. 13071, Dec. 29, 1997; E.O. 13106, Dec. 7, 1998; E.O. 13144, Dec. 21, 1999; E.O. 13182, Dec. 23, 2000; E.O. 13249, Dec. 28, 2001; E.O.s 13282, Dec. 31, 2002, and 13291, Mar. 21, 2003; E.O.s 13322, Dec. 30, 2003, and 13332, Mar. 3, 2004; E.O. 13368, Dec. 30, 2004; E.O. 13393, Dec. 22, 2005; and E.O. 13420, Dec. 21, 2006.

Presidential Request and Congressional Appropriation. One of the first indications of the possible size of the combined pay increase (basic pay increase plus average locality increase) for the next year is in the President's annual budget request, where the President indicates how large a federal pay increase he intends to support. Ultimately, though, as part of the appropriations process, Congress may legislate an overall pay adjustment that is different from the one recommended by the President in his budget message or that might be authorized by the President in an alternative pay plan.

In his annual budget request for FY2008, provided to Congress in February 2007, President Bush proposed a 3% total pay increase for federal white-collar workers — the same percentage increase as he requested for members of the uniformed military. The Financial Services and General Government appropriations bill (H.R. 2829), as passed by the House

of Representatives, includes a 3.5% increase for FY2008, and the Senate Appropriations Committee has reported the bill with the same increase. In a statement of Administration policy regarding the House bill, the Bush Administration said it “strongly opposes” the 3.5% pay increase, and characterized it as an “arbitrary across the board increase” that “would cost agencies over \$600 million in FY2008 and would not target any specific recruitment or retention challenges.”²

Civilian-Military Pay Parity. In recent years, one factor consistently raised in determining the size of the GS-pay increase has been the amount provided to uniformed military personnel. The Concurrent Resolution on the Budget, which provides the framework within which Congress subsequently considers spending legislation, has several times in the past included language expressing the sense of Congress on the federal civilian pay adjustment. The FY2008 budget resolution as agreed to by the House (H.Con.Res. 99) on March 29, 2007, includes such a provision at Section 510, which states the Sense of the House that federal civilian pay should be adjusted at the same time and in the same proportion as pay for the uniformed military. The Senate’s version of the budget resolution (S.Con.Res. 21) as agreed to on March 23, 2007, does not include such a provision. On May 3, 2007, Representative Tom Davis, Ranking Member on the House Committee on Oversight and Government Reform, sent a letter to the chairmen and ranking members of the House Committee on Appropriations and its Subcommittee on Financial Services and General Government urging the committee “to ensure parity in pay adjustments for civilian and military personnel” for FY2008. In the letter, Mr. Davis stated his belief that it is critical for civilian and military personnel to receive similar pay adjustments because “Federal civilian employees from DOD, DHS, FBI, CIA, U.S. Customs Service, Secret Service, Department of Justice, Department of State, and many other agencies” support the efforts of the uniformed military and “work to ensure the security of our nation and people.”³

Are Federal Employees Overpaid? Occasionally, articles appear in the press indicating that federal employees are paid more than the non-federal workforce. For example, an article published last month in the *Asbury Park Press* entitled “Across the nation, federal employees making top dollar” concluded that “Federal workers, on average, are paid almost 50 percent more than employees in the private sector.”⁴ The article stated that the area with the largest federal-private sector disparity was Nassau County, Florida, where 577 federal employees, many of them employed at an air traffic control center, were paid an average of more than \$108,000 in 2005, compared with an average of less than \$30,000 for private sector workers, many of whom were in the tourism and hospitality industries. Other publications have picked up on this article, raising doubts about the GS pay setting process and official studies underlying that process showing that federal workers lag behind their non-federal counterparts.⁵

² Office of Management and Budget, “Statement of Administration Policy: H.R. 2829 – Financial Services and General Government Appropriations Act, 2008,” June 26, 2007.

³ Letter from Representative Tom Davis to Representatives David Obey, Jose Serrano, Jerry Lewis, and Ralph Regula, May 3, 2007.

⁴ Jason Method, “Across the nation, federal employees making top dollar,” *Asbury Park Press*, June 24, 2007.

⁵ Stephen Losey, “Is the pay gap real? Only for some,” *Federal Times*, July 9, 2007.

The process by which GS pay rates are compared to pay rates outside the federal government within local pay areas was determined by Congress, and is administered by the Office of Personnel Management (OPM) using data collected by BLS. That process has been examined by top compensation experts in academia and elsewhere, and found to be valid and reliable.⁶ Such reviews have found consistently that federal pay lags behind the private sector by as much as 50% in some localities. Federal-non-federal pay comparisons like the one published in the *Asbury Park Press* are much less precise (there, simply comparing federal and private sector salaries that are published in the BLS Quarterly Census of Employment and Wages, rather than comparing specific types of jobs and job levels). Nevertheless, concerns by Congress and the current and previous Presidents about the validity of the pay comparison process and the budgetary implications of implementing the results of that process have led to the establishment of alternative pay plans in virtually each year since FEPCA was enacted.

Pay Compression

Another major federal pay issue currently facing Congress is the increasing degree of compression between and within the different federal pay schedules. **Appendix 2** at the end of my testimony illustrates this compression by showing the salary relationships between the major schedules. For example:

- In 1991, cabinet secretaries and others at the top of the Executive Schedule (EX-I) were paid 28.2% more than employees at the top of the SES schedule (then ES-6), and ES-6 employees received the same salary as employees in EX-IV (e.g., certain inspectors general, chief financial and information officers). By 2007, however, EX-I salaries were only 11% more than what the highest paid SES employees were paid in agencies with certified performance appraisal systems, and these top SES employees received the same salaries as EX-II (e.g., deputy cabinet secretaries, Senators, and Members of the House of Representatives).⁷ Interestingly, certification of an agency's SES performance appraisal system by OPM *exacerbates* this pay compression problem by raising the cap on SES pay to nearly the top of the Executive Schedule. In agencies without certified SES appraisal systems, the EX-I salaries were nearly 21% more than top SES salaries.

⁶ For example, Charles H. Fay, Chair of the Human Resource Management Department at Rutgers University School of Management and Labor Relations said in testimony before this subcommittee that "BLS uses impeccable methodology in gathering reliable and valid data to price the GS, and applies sophisticated statistical methods to evaluate survey data and apply it to the GS for the Federal Salary Council." Testimony of Charles H. Fay before the House Subcommittee on the Federal Workforce, Postal Service, and the District of Columbia; and the Senate Subcommittee on the Oversight of Government Management, the Federal Workforce, and the District of Columbia, May 22, 2007, p. 13.

⁷ As of March 2007, 2,332 SES employees (32% of all SES employees) were paid between \$160,000 and \$169,999. Of these, the largest number were in the Departments of Justice (266), Agriculture (217), Energy (194), Health and Human Services (189), and Defense (174). In contrast, only 68 EX employees (14% of all EX employees) were paid more than \$160,000.

- In 1991, employees at the top of the SES pay schedule (then ES-6) were paid 11.3% more than GS-18 employees. In 2007, top SES employees in agencies without certified appraisal systems were paid the same as the top SL and ST employees.
- In 1991, a GS-18 employee was paid 21.4% more than an employee at GS-15, step 10. In 2007, SL and ST employees were paid only 7.8% more than GS-15, step 10 in the Washington, DC, pay area, and only 6.3% more in the San Francisco pay area.

Studies have also shown that employees in the EX pay system are losing buying power. For example, in June 2006, using the Gross Domestic Product (GDP) price deflator, the Government Accountability Office (GAO) reported that EX-I positions (e.g., cabinet secretaries) were paid 27% less in constant dollars than they were in 1970.⁸ EX-II through EX-V positions had also experienced losses in inflation-adjusted dollars from 1970 to 2006, although not as much (between 7% and 11%). When using the Consumer Price Index (CPI) to adjust for inflation, GAO found that the buying power losses during this period were even greater, ranging from 25% to 41% for EX-I through EX-V.

Pay compression has begun to affect the upper reaches of the General Schedule. Because of the EX-IV cap on base and locality pay (currently at \$145,400 nationwide), GS-15 employees at steps at steps 7 through 10 in nine locality pay areas are currently unable to receive the full pay increases that they would otherwise receive. Specifically, those affected are GS-15 employees:

- at step 10 in the (1) Boston-Worcester-Manchester, MA-NH, Combined Statistical Area (CSA), plus the Providence-New Bedford-Fall River, RI-MA, Metropolitan Statistical Area (MSA), Barnstable County, MA, and Berwick, Eliot, Kittery, South Berwick, and York towns in York County, ME; (2) Chicago-Naperville-Michigan City, IL-IN-WI, CSA; (3) Detroit-Warren-Flint, MI, CSA, plus Lenawee County, MI; (4) Hartford-West Hartford-Willimantic, CT, CSA, plus the Springfield, MA, MSA and New London County, CT; and (5) San Diego-Carlsbad-San Marcos, CA, MSA;
- at steps 9 and 10 in the (1) Houston-Baytown, Huntsville, TX, CSA; (2) Los Angeles-Long Beach-Riverside, CA, CSA, plus the Santa Barbara-Santa Maria-Goleta, CA, MSA and all of Edwards Air Force Base, CA; and (3) New York-Newark-Bridgeport, NY-NJ-CT-PA, CSA, plus Monroe County, PA, and Warren County, NJ;
- at steps 7, 8, 9, and 10 in the San Jose-San Francisco-Oakland, CA, CSA, plus the Salinas, CA, MSA and San Joaquin County, CA.

Without changes in the EX-IV cap on base and locality pay, more pay areas are expected to be affected, with more GS-15 employees in those areas receiving the same amounts of pay.

⁸ U.S. Government Accountability Office, *Human Capital: Trends in Executive and Judicial Pay*, GAO-06-708 (June 2006).

More generally, pay compression has led to a number of inconsistencies and illogical pay relationships. For example, pay rates (base and locality pay combined) for SL and ST members are capped because of the tie to the EX-III pay rate. Agency SL and ST employees can earn more than the heads of smaller agencies at EX-IV and EX-V. SES members can potentially earn more than all EX schedule members, except for EX-I. Total compensation in one calendar year for SL, ST, and SES can be up to the Vice President's salary of \$215,700, an amount that is greater than what any EX employee can earn, as EX members are not eligible for awards and bonuses.

The primary drivers behind this cascading set of pay compressions appear to be limits on EX salaries and the linkages between EX and the other pay systems. If EX salaries were to rise, compression between the EX schedule and the other systems would ease. However, EX salaries are, in turn, linked to congressional salaries, with the pay for EX-I the same as that of Members of Congress. Also, under the Ethics Reform Act of 1989, the pay adjustment for the Executive Schedule can be no larger than the GS base pay adjustment, regardless of the amount specified by the relevant ECI data (the December ECI minus 0.5%), cannot be greater than 5%, and cannot be less than zero.

The Ethics Reform Act of 1989 includes two provisions under which pay rates for Members, the Vice President, federal officials paid under the EX, and certain federal justices and judges can be set. The first of these provisions provides for a quadrennial review of the salaries of federal officials by a Citizens' Commission on Public Service and Compensation.⁹ The commission is to make recommendations to the President. The law requires the commission and the President to submit recommendations to Congress providing that the salaries of the

- Speaker of the House of Representatives, the Vice President of the United States, and the Chief Justice of the United States shall be equal;
- Majority and Minority Leaders of the House of Representatives and the Senate, the President pro tempore of the Senate, and Level I of the Executive Schedule (e.g., cabinet secretaries) shall be equal; and
- Senators, Members of the House of Representatives, the Resident Commissioner of Puerto Rico, Delegates to the House, Judges of the U.S. District Courts, Judges of the United States Court of International Trade, and Level II of the Executive Schedule (deputy secretaries of cabinet departments, secretaries of military departments, and heads of major agencies) shall be equal.¹⁰

⁹ Ethics Reform Act of 1989, P.L. 101-194, §701(a), Nov. 30, 1989; 103 Stat. 1716, at 1763; 2 U.S.C. §351.

¹⁰ Ibid., §701(I); 103 Stat. 1716, at 1766; 2 U.S.C. §362.

The commission, however, has never been activated. The commission was initially funded in the 1993 Treasury, Postal Service, and General Government Appropriations Act, but that appropriation was rescinded in the 1994 act.¹¹

Congress has not systematically examined the EX pay system since the passage of the Ethics Reform Act of 1989, and some have called for Congress to do so now to avert even more pay compression problems in the future.¹²

Pay for Performance Reforms

Another major federal pay-related issue of late has been an attempt to move toward pay systems that are more focused on the performance of employees or their organizational units. Efforts to establish performance-based pay have a long history in the federal government. For example, Title V of the Civil Service Reform Act of 1978 created a merit pay system which was subsequently amended by P.L. 98-615, enacted on November 9, 1984. The law established a Performance Management and Recognition System, with pay based on performance for managers and supervisors in GS grades 13 through 15. There were five levels for rating performance with various amounts of pay attached to each level. An individual rated “outstanding” was to receive a full comparability raise, a full merit increase, and a performance award that generally ranged from 2% to 10% of base pay. Cash awards ranging from \$10,000 to \$25,000 were available to reward individuals for superior accomplishment and special service.

A more recent manifestation of this movement has been in the Senior Executive Service, where agencies with SES performance appraisal systems that have been certified by OPM as making “meaningful distinctions” among employees based on relative performance are allowed to pay their senior executives more than agencies without such certified appraisal systems. A number of individual agencies have attempted to move toward performance-based pay for some or all of their employees, including DOD, the Department of Homeland Security, and the Government Accountability Office (GAO). In early 2006, the Bush Administration drafted legislation that proposed to move the entire federal government in the direction of performance-based pay, but the legislation was never introduced.

A number of organizations have examined agencies’ efforts to move toward performance-based pay, and several common lessons appear to be emerging. For example, in 2005, GAO convened a symposium on such pay systems and concluded that agencies attempting such reforms must make sure that they have the institutional infrastructure in place to ensure that the reforms are effective and properly implemented. “At a minimum,” GAO said, “this infrastructure includes a modern, effective, credible, and validated performance management system that provides a clear linkage between institutional, unit, and individual performance-oriented outcomes; results in meaningful distinctions in ratings;

¹¹ Treasury, Postal Service, and General Government Appropriations Act, 1993, P.L. 102-393, Oct. 6, 1992; 106 Stat. 1729, at 1743; and Treasury, Postal Service, and General Government Appropriations Act, 1994, P.L. 103-123, Oct. 28, 1993; 107 Stat. 1226, at 1239. The appropriation of \$250,000 was to remain available until Sept. 30, 1994.

¹² U.S. House, Committee on Government Reform, Subcommittee on the Federal Workforce and Agency Organization, *Executive and Judicial Compensation in the Federal Government* (Quadrennial Commission), hearing, Sept. 20, 2006. Transcript available from the committee.

and incorporates adequate safeguards.”¹³ Similarly, in a January 2006 report to the President and Congress, the Merit Systems Protection Board (MSPB) said that pay for performance “will require more than legislation,” and that the foundation of a pay for performance system is an evaluation system that is sound in both its design and its application.¹⁴ MSPB also concluded that agencies must tailor pay for performance systems to their missions and environments, and that agencies must be prepared to make a substantial investment of time, money, and effort before linking pay to performance.

A similar message was offered in March of this year by several witnesses during a hearing before this subcommittee on the status of federal personnel reform. For example, citing a 2006 study that reviewed approximately 2,600 research studies on the factors that motivate employees to increase their performance, Robert Tobias, Director of Public Sector Executive Education at American University, said the study concluded that “individual financial incentives are ineffective in traditional public sector settings,” and that this failure “is likely due to a lack of adequate funding for merit pay and an absence of the organizational and managerial characteristics that are necessary to make pay for performance work in traditional government settings.”¹⁵ Tobias also said that a recent study of the SES pay system (in which 85% of the respondents reportedly said that the new system had no effect or a negative effect on their motivation) reinforced the basic proposition advanced by the 2006 study that “there must be the successful implementation of a performance management system before the implementation of a pay for performance system.”

Legislation has been introduced in the 110th Congress that would move the entire federal government, or certain pay systems, more in the direction of performance-based pay. For example, S. 1045, introduced by Senator George Voinovich in March 2007, would (among other things) require agencies to establish one or more performance appraisal systems with at least three summary rating levels (unacceptable, fully successful, and above fully successful); and require an employee to receive a summary rating of at least “fully successful” to receive a within-grade increase, an annual basic pay adjustment, a locality pay adjustment, a special rate, or a blue-collar adjustment. Senator Voinovich has also introduced S. 1046, which would change the way SL and ST employees may be evaluated and paid. Under current law, SL and ST employees may receive basic pay up to EX-IV (\$145,400 as of January 2007). S. 1046 would provide that SL and ST employees in agencies with performance appraisal systems certified by OPM as making “meaningful distinctions” in performance could receive basic pay up to EX-II (\$168,000); in agencies without certified appraisal systems, SL and ST employees could receive basic pay up to EX-

¹³ U.S. Government Accountability Office, *Human Capital: Designing and Managing Market-Based and More Performance-Oriented Pay Systems*, GAO-05-1048T, Sept. 27, 2005.

¹⁴ U.S. Merit Systems Protection Board, *Designing an Effective Pay for Performance Compensation System*, Jan. 2006, available at [<http://www.mspb.gov/netsearch/viewdocs.aspx?docnumber=224104&version=224323&application=ACROBAT>].

¹⁵ Testimony of Robert M. Tobias, Director, Public Sector Executive Education, American University, before the House Subcommittee on Federal Workforce, Postal Service, and the District of Columbia, Mar. 8, 2007, citing a study by James L. Perry, Debra Mesch, and Laurie Paarlberg, “Motivating Employees in a New Governance Era: The Performance Paradigm Revisited,” *Public Administration Review*: 66 (July/Aug. 2006), pp. 505-514.

III (\$154,600). Senator Voinovich said the bill would keep SL and ST employees “on equal footing” with members of the SES in terms of pay and performance management.¹⁶

Market-Based Pay Reforms

Another current issue in federal pay is the development of more market-based pay systems. Comparison of federal pay rates to local markets is not new. Special salary rates (higher rates of basic pay) for GS positions may be established by OPM “to address existing or likely significant handicaps in recruiting or retaining well-qualified employees.” The rates may be established by job series, speciality, grade level, and geographic area and are to address staffing problems caused by such factors as non-federal pay rates that are significantly higher than federal pay rates and working conditions or the nature of the work involved that are undesirable. Among the occupations that currently receive special rates are clerical, engineers, and various medical officers. Also, as noted previously, since the passage of FEPCA in 1990, the GS system as a whole has become at least somewhat market based, with federal salaries matched to their private sector counterparts in 32 local pay areas. However, the federal-private sector comparison made through FEPCA is done across the entire set of occupations in each area, not individual jobs. Some agencies are attempting to make their pay systems even more market based by focusing on individual jobs, but sometimes those efforts have met with less than full success.

For example, in July 2004, Congress enacted the GAO Human Capital Reform Act of 2004 (P.L. 108-271), which gave the Comptroller General broad authority to set the pay for employees at the Government Accountability Office (GAO). One of several listed factors that the Comptroller General was required to consider in determining the amount of annual pay adjustments was “the pay rates for the same levels of work for officers and employees of the Office and non-Federal employees in each local pay area.” Shortly after the legislation was enacted, GAO contracted with the Watson Wyatt Worldwide consulting firm to conduct a market-based pay study, which reportedly concluded that certain GAO employees were already paid more than the relevant market. Based on the results of that study, the Comptroller General decided to deny annual basic pay increases to more than 300 GAO employees.

At a May 22, 2007, hearing before this subcommittee, Charles H. Fay, Chair of the Human Resource Management Department at the Rutgers University School of Management and Labor Relations, testified that the Watson Wyatt pay study and how it was used by GAO management were flawed in several respects. Problems cited related to how the GAO jobs were described and matched to jobs in the market pay data, the lack of involvement by GAO employees in the description and matching process, the quality of the “off the shelf” data that Watson Wyatt used in the study, and GAO’s overall strategy of being an average paying employer when it considers itself as one of the top agencies in the federal government and at the center of government decisionmaking. This experience suggests that care must be taken in determining the relevant “market” for an agency and the pay relationship of individual federal occupations to the market.

¹⁶ Statement of Senator George Voinovich, *Congressional Record*, daily edition, vol. 153, Mar. 29, 2007, p. S4180.

Other Proposed Reform Efforts

Still other types of federal pay reforms might surface in the near future. In May 2007, the Director of OPM submitted a legislative proposal that would, if enacted, extend locality pay to white-collar federal employees in what are known as “non-foreign” areas (i.e., areas outside the continental United States, such as Alaska, Hawaii, Guam/Northern Mariana Islands, the U.S. Virgin Islands, and Puerto Rico).¹⁷ Since 1948, white-collar employees in these areas have received a tax-free, statutorily based pay supplement (5 U.S.C. §5941) predicated on differences in cost of living as compared to Washington, DC. The purpose of the supplements (which can be as high as 25% of base pay) is to improve recruitment and retention in those non-foreign areas, and they are not counted toward an employee’s “high three” salary for retirement calculations. Therefore, shifting to a cost of labor-based locality pay system where locality payments are taxed and count toward retirement calculations would represent a major transition in how employees in these areas are paid. OPM said this change was needed because of “perceived disparities between the pay and retirement benefits” for employees within and outside the continental United States. OPM also pointed out that the non-foreign COLA program has been “fraught with litigation, and has cost the Federal Government hundreds of millions of dollars in settlement payments and attorney fees.” One recent settlement resulted in a new cost-of-living survey that may cause further litigation. If enacted, the proposed legislation would phase in locality pay (and decrease non-foreign COLA payments) over a seven-year period, and is expected to cost \$109 million over the next 10 years according to OPM’s proposal.

More generally, a recent survey of 55 federal human resource officials revealed that a majority believe the GS pay system is no longer adequate, and that “a more performance-sensitive and market-sensitive pay system should be a long term goal.”¹⁸ Although one-third of the respondents said that the GS system should be eliminated immediately, most of the officials believed that “the process to design and implement a new pay system should be slow and deliberate and that credible performance management systems and appraisals should come first.” The officials’ concerns about those reforms reportedly stemmed from recent experiences at DOD and DHS, and the implementation of changes to SES pay that were perceived as rushed and forced on participants.

Mr. Chairman, that concludes my prepared statement. I would be happy to answer any questions that you or other Members of the subcommittee might have.

¹⁷ Letter from Linda M. Springer, Director, OPM, to the Honorable Richard B. Cheney, President of the Senate, May 30, 2007.

¹⁸ Partnership for Public Service and Grant Thornton, *Federal Human Capital: The Perfect Storm*, July 2007, available at [<http://ourpublicservice.org/OPS/publications/viewcontentdetails.php?id=118>].

Appendix 1: Major Federal White-Collar Pay Schedules

Pay Schedule	Number of Employees (Mar. 2007)	Base Pay Adjustment Mechanism	Availability of Locality Pay	Salary Limitations (Jan. 2007)	Total Compensation Limitations (Jan. 2007)
General Schedule (GS)	1,204,608 (GS only) 1,329,684 (GS and related)	Employment Cost Index (ECI) Sept. data minus 0.5%	Yes	<p>Base Pay: GS-1, step 1 (\$16,630) to GS-15, step 10 (\$120,981) ----- Locality Pay - Wash. DC pay area: GS-1, step 1 (\$19,722) to GS-15, step 10 (\$143,471) ----- Base pay cannot exceed Executive Schedule Level V (EX-V) (\$136,200) (5 U.S.C. §5303(f)). ----- Base pay and locality pay combined cannot exceed EX-IV (\$145,400) (5 U.S.C. §5304(g)(1)).</p>	Total compensation (salary plus bonuses) cannot exceed EX-I (\$186,600) (5 U.S.C. §5307(a)(1)).

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Pay Schedule	Number of Employees (Mar. 2007)	Base Pay Adjustment Mechanism	Availability of Locality Pay	Salary Limitations (Jan. 2007)	Total Compensation Limitations (Jan. 2007)
Senior Level (SL) and Scientific or Professional (ST)	928	ECI (Sept. data) minus 0.5%. Annual adjustment may be provided at the discretion of agency heads.	Yes. The Pay Agent may extend locality pay to SL and ST and has done so each year since 1994.	<p>Base pay: \$111,676-\$145,400 -----</p> <p>Locality pay - Wash. DC pay area: \$132,437-\$154,600 -----</p> <p>Base pay ranges from 120% of the minimum base pay for GS-15 to EX-IV (5 U.S.C. §5376). -----</p> <p>Base pay and locality pay combined cannot exceed EX-III (\$154,600) (5 U.S.C. §5304(g)(2)).</p>	<p>Total compensation in agencies whose performance appraisal systems have been certified by the Office of Personnel Management (OPM) may be up to the Vice President's salary (\$215,700) (5 U.S.C. §5307(d)). -----</p> <p>In agencies whose performance appraisal systems have not been so certified, total compensation may be up to EX-I (\$186,600) (5 U.S.C. §5307(a)(1)).</p>

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Pay Schedule	Number of Employees (Mar. 2007)	Base Pay Adjustment Mechanism	Availability of Locality Pay	Salary Limitations (Jan. 2007)	Total Compensation Limitations (Jan. 2007)
Senior Executive Service (SES)	7,323 (6,421 Career)	Automatic pay increases no longer occur; an agency may increase a senior executive's pay, as long as his or her performance or contributions warrant an increase, in order to maintain the individual's relative position within the SES pay rate range. (5 CFR 534.404(b)(3))	No	Base pay: \$111,676- \$154,600 or \$168,000 ----- Base pay in agencies whose performance appraisal systems have been certified by OPM may be up to EX-II (\$168,000). ----- In agencies whose appraisal systems have not been certified, base pay may be up to EX-III (\$154,600).	Total compensation in agencies whose performance appraisal systems have been certified by OPM may be up to the Vice President's salary (\$215,700) (5 U.S.C. §5307(d)). ----- In agencies whose appraisal systems have not been certified, total compensation may be up to EX-I (\$186,600) (5 U.S.C. §5307(a)(1)).
Executive Schedule (EX)	475	ECI (Dec. data) minus 0.5%, but cannot be (1) more than the GS pay increase, (2) greater than 5%, or (3) less than zero.	No	EX-I: \$186,600 EX-II: \$168,000 EX-III: \$154,600 EX-IV: \$145,400 EX-V: \$136,200	EX employees are not eligible for locality pay. Presidentially appointed and Senate confirmed EX members are not eligible for awards and bonuses.

Sources: Data on the number of employees in each pay system are from OPM's FedScope database, accessible at [<http://www.fedscope.opm.gov/employment.asp>].

Appendix 2: Salary Relationships Between Major Federal White-Collar Pay Schedules

Pay Schedule	Maximum Base Pay January 1991*	1991 Relationship to Other Schedules	Maximum Base Pay (EX and SES) and Maximum Base and Locality Pay (SL, ST, GS) January 2007**	2007 Relationship to Other Schedules
EX	EX-I - \$138,900 EX-II - \$125,100 EX-III - \$115,300 EX-IV - \$108,300 EX-V - \$101,300	EX-I was paid 28.2% more than ES-6; EX-IV and ES-6 received the same salary	EX-I - \$186,600 EX-II - \$168,000 EX-III - \$154,600 EX-IV - \$145,400 EX-V - \$136,200	EX-I was paid 11.1% more than SES with certified performance appraisal system and 20.7% more than without certified system; EX-II and SES with certification salaries match; EX-III and SES without certification salaries match
SES	ES-6 - \$108,300 ES-5 - \$104,600 ES-4 - \$100,500 ES-3 - \$95,300 ES-2 - \$91,200 ES-1 - \$87,000	ES-6 received 11.3% more than GS-18; GS-18 salary was between ES-3 and ES-4	\$154,600 (without certified performance appraisal system); \$168,000 (with certified system)	SES salary without certified performance appraisal system is same as SL and ST

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Pay Schedule	Maximum Base Pay January 1991*	1991 Relationship to Other Schedules	Maximum Base Pay (EX and SES) and Maximum Base and Locality Pay (SL, ST, GS) January 2007**	2007 Relationship to Other Schedules
<p>GS-16 to GS-18 (1991)</p> <p>SL and ST (2007)</p>	<p>GS-16, step 9 - \$89,787</p> <p>GS-17, step 5 - \$94,104</p> <p>GS-18 - \$97,317</p>	<p>GS-18 pay was 21.4% more than GS-15, step 10</p> <p>GS-16, step 1 was 11% less than GS-15, step 10</p>	<p>SL and ST - \$154,600</p>	<p>SL and ST - 7.8% more than GS-15, step 10 (Washington, DC, pay area)</p> <p>SL and ST - 6.3% more than GS-15, step 10 (San Francisco pay area)</p> <p>Minimum base and locality pay for SL and ST of \$132,437 (Washington, DC, pay area) - 8.3% less than GS-15, step 10 (Washington, DC, pay area)</p> <p>Minimum base and locality pay for SL and ST of \$145,547 (San Francisco pay area) - 0.10% more than GS-15, step 10 (San Francisco pay area)</p>

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Pay Schedule	Maximum Base Pay January 1991*	1991 Relationship to Other Schedules	Maximum Base Pay (EX and SES) and Maximum Base and Locality Pay (SL, ST, GS) January 2007**	2007 Relationship to Other Schedules
GS-15, step 10	\$80,138	GS-15, step 10 was paid 17.6% more than GS-14, step 10	\$143,471 (Washington, DC, pay area); \$145,400 (San Francisco pay area); steps 7-10 are all at this salary	GS-15, step 10 (Washington, DC, pay area) is paid 17.6% more than GS-14, step 10 (Washington, DC, pay area) GS-15, step 10 (San Francisco pay area) is paid 8.5% more than GS-14, step 10 (San Francisco pay area)
GS-14, step 10	\$68,129	See above	\$121,967 (Washington, DC, pay area); \$134,042 (San Francisco pay area)	See above

*Maximum base pay for EX, SES, and GS grades.

**Maximum base pay for EX and SES. Maximum base and locality pay for SL and ST, and GS. (EX and SES are not eligible for locality pay.)

Notes: P.L. 101-509, the Federal Employees Pay Comparability Act of 1990, combined grades GS-16, GS-17, and GS-18 into the senior-level (SL) pay schedule. Prior to that change, GS-16 had nine steps; GS-17 had five steps, and GS-18 had one step. Locality-based comparability payments began in January 1994. The gap between private and public sector pay is largest in the San Francisco pay area. The 1991 salary data are from U.S. Office of Personnel Management, *Pay Structure of the Civil Service*, Mar. 31, 1991.