Testimony of

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"In Search of Equity: An Examination of Locality Pay"

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Chairman Davis, Ranking Member Marchant, and members of the Subcommittee, I appreciate the opportunity to appear again before this distinguished subcommittee to discuss the important subjects relating to federal pay. As you know, the National Treasury Employees Union represents more than 150,000 federal employees in over 31 different agencies and departments throughout the government.

Locality pay is a subject I have worked on for some time. I have the privilege of serving on the Federal Salary Council (FSC) which makes recommendations to the President's Pay Agent on a variety of issues relating to federal pay—including locality pay. The calculations are understandably sensitive in some regions of the country. Employees face challenges in making ends meet in view of legitimate economic woes – rising gas prices that affect commuting to work; increased food prices; prices of commodities; and a declining housing market. Regional variations add pressure and weigh heavily in some or all of these areas of the country for federal employees who simply seek a good quality of life for themselves and their families.

Federal Employees Pay Comparability

My number one recommendation to the subcommittee is this: Regional concerns over the differing levels of locality pay and overall fairness of the General Schedule (GS) can best be fixed through **full implementation of the Federal Employees Pay Comparability Act of 1990 (FEPCA)** *(PL 101-509)*. Congress enacted FEPCA to replace the nationwide GS system with a method for setting pay for white-collar employees that uses a combination of across-the-board and locality pay adjustments. The raises are indexed to wage increases in the private-sector, as measured by the Employment Cost Index (ECI). The policy for setting General Schedule pay contained in 5 U.S.C. 5301 is that—

(1) there be equal pay for substantially equal work within each local pay area;

(2) within each local pay area, pay distinctions be maintained in keeping with work and performance distinctions;

(3) Federal pay rates be comparable with non-Federal pay rates for the same levels of work within the same local pay area; and

(4) any existing pay disparities between Federal and non-Federal employees should be completely eliminated.

Before FEPCA, the goal was still comparability with the private sector, but FEPCA introduced locality adjustments to make comparability more sensitive to local labor markets. Before FEPCA, GS employees all received the same annual pay increase, regardless of the cost-of-labor in their locality. While the law has not been fully implemented it does afford additional locality pay to high cost areas including many larger cities. NTEU supports fully implementing the law.

Across-The-Board and Locality Adjustments

Under FEPCA, General Schedule salary adjustments, beginning in January 1994, consist of two components: (1) a general increase linked to the Employment Cost Index and applicable to the General Schedule, Foreign Service pay schedules, and pay schedules established under title 38, United States Code, for Veterans Health Administration employees; and (2) a General Schedule locality adjustment that applies to specific areas of the continental United States where non-Federal pay exceeds Federal pay by more than 5 percent.

The formula for the general increase (defined in section 5303 of title 5, United States Code) provides that the pay rates for each statutory pay system be increased by a percentage equal to the 12-month percentage increase in the ECI, minus one-half of one percentage point. The 12-month reference period ends with the September preceding the effective date of the adjustment by 15 months.

The locality component of the pay adjustment under FEPCA was to be phased in over a 9-year period. In 1994, the minimum comparability increase was two-tenths of the "target" pay disparity (i.e., the amount needed to reduce the pay disparity to 5 percent *according to the methodology required by current law*). For each successive year, the comparability increase was scheduled to be at least an additional one-tenth of the "target" pay disparity. For 2002 and thereafter, the law authorized the full amount necessary to reduce the pay disparity in each locality pay area to 5 percent. However, the schedule under FEPCA has not been followed. This is because in almost every year since 1995, the President has exercised his authority under FEPCA to submit an "alternative pay plan" due to a "national emergency or serious economic conditions affecting the general welfare" (see 5 U.S.C. 5104a), and ultimately separate legislation designating a pay raise has been enacted in Congress providing lower federal pay raises than would have been provided under FEPCA.

Based on calculations provided by the Office of Personnel Management (OPM) staff to the Federal Salary Council, in taking a weighted average of the locality pay gaps, the overall gap between base GS average salaries (excluding any add-ons such as special rates and existing locality payments) and non-Federal average salaries surveyed by the Bureau of Labor Statistics (BLS) was 43.73 percent as of March 2007. The amount needed to reduce the pay disparity to FEPCA's target gap of 5 percent averages 36.89 percent.

Pay gaps are calculated excluding existing locality payments because locality pay is paid on top of the base General Schedule rates. The overall average pay gap in 2007, including the average locality of rate of 16.88 percent, is 22.97 percent. If FEPCA were fully implemented, that gap could be nearly reduced to meet the statute's 5 percent target.

If FEPCA were in effect, federal employees in San Francisco would receive a locality adjustment of 17.2 percent for 2008 on top of what the already receive; Los Angeles federal employees would get an additional 10.2 percent in salary for locality pay.

Pay Methodology Improvements

Through our work on the Federal Salary Council, NTEU supported reforming the data used by BLS at the Department of Labor (DOL) in 1996. Prior to that time, BLS collected private sector survey data under its Occupational Compensation Survey Program (OCSP). It was our position that the data gathered for locality pay determinations was flawed. Subsequently BLS changed and phased in a National Compensation Survey Program (NCSP), which used a different improved methodology. NTEU believes the data collected from OCSP will more accurately depict the gaps in pay, particularly in large metropolitan areas. The new survey was, however, phased in incrementally over a five year period, so we are just now beginning to see the results of the new data. Those results are depicting increased pay gaps in our larger metropolitan areas including cities in California.

Mr. Chairman, some have suggested using a different standard for determining locality pay. As I mentioned earlier, the Employment Cost Index (ECI) which essentially measures the cost-of-labor is an underlying component of both base pay and locality pay, the two main elements of FEPCA. Some have argued for a change to a cost-of-living standard, not cost-of-labor, in determining federal pay. I think that would be a mistake and NTEU would oppose it. The GS system has been based on the concept that federal pay should be comparable with private sector pay for almost two decades as have its pay predecessors. And with the new data I just discussed, we are seeing more accurate depictions of widening pay gaps in larger metropolitan areas. Fully implementing FEPCA would address the particular stresses of large metropolitan areas and makes more sense than changing the underlying tenets and theory of federal pay.

While NTEU does not support changing locality pay determinations from the cost-of-labor standard, it does not oppose government agencies use of existing flexibilities such as special pay or recruitment and retention bonuses in an effort to keep talented and high quality employees. These are particularly relevant in high cost communities like those in California. We need to find ways to address the possible loss of talent in government, and we will be happy to work with the subcommittee and with the Office of Personnel Management to seek ways to make better use of flexibilities available under the law.

Pay Compression

NTEU is concerned with an issue that has surfaced in recent years and appears to be growing for some federal employees in high cost areas of the nation. Some federal employees in the GS system did not receive their full federal pay raise this year, and it is likely they will not receive it in its entirety in 2009. These employees' salaries are "capped" because they bump up against the Executive Schedule, the pay system for senior executives in government. By law, (5 USC 5304(g)(1)) base GS pay and locality pay combined cannot exceed Level IV of the Executive Schedule (EX-IV)—which, for 2008, is set at $149,000. According to the *Congressional Research Service* (RL34380) approximately 7,100 GS and other GS-equivalent employees in 12 pay areas did not receive all of the pay increases for their pay areas. Those primarily affected have been GS-15 step 10s, but in some high cost areas, those who are Step 9 and even Step 8 could be capped, or only receive part of their pay raise.

While NTEU does not represent large numbers of employees at the top of the GS scale, we do represent some and they are very deserving of their full raises. We recognize—and support—fixing the problem. We fight hard for fair pay raises in the General Schedule each year, and all federal employees who serve in government should not suffer because they worked hard, got promoted and reached the top of the pay scale. While pay compression was first seen in San Francisco, there are now cases in eleven other cities, including Houston, Boston, Chicago, Detroit, Washington, DC and others. Since federal retirement is calculated on salary, these caps have an adverse effect on an employee's retirement benefits as well. The pay compression issue could drive talented people from government at a time when we want to recruit and retain quality employees.

I urge the subcommittee to fix this pay compression problem for those federal civil servants who worked hard, got promoted and are now being penalized.

Non-Foreign COLAs

Mr. Chairman, as you know, we have a different pay system that predates the admission of Alaska and Hawaii into the United States and covers nearly 50,000 federal employees there and in U.S. territories. After World War II, in 1948, a pay system was established when it became clear that federal employees hired or transferred to these then-called outlying territories bore costs that mainlanders did not. At the time, the pay system was a very sensible and necessary action. Rather than being compensated at the then uniform pay rate across the United States, civilian workers in the outlying territories were given an additional payment based on a measure of the increased cost of living in these territories. This cost-of-living adjustment (COLA) was in addition to the employee's base pay. Non-taxable for federal income tax or FICA purposes, it was also not counted towards federal retirement. This was termed the "non-foreign COLA," distinct from pay systems for federal employees living outside the jurisdiction of the United States. This system remained in place following the admission of Alaska and Hawaii into the union and continues as well in U.S. territories and the Commonwealth of Puerto Rico today.

Given that FEPCA was a significant departure from the previous geographically uniform pay rates on the mainland, it was not surprising that Congress exempted the areas under the non-foreign COLA, in essence "grandfathering" this program. But it has become increasingly clear that the non-foreign COLA is dated and in need of reform. With 18 years of experience with locality pay, it is now time to extend locality pay and retirement credit to the outlying areas. Such an initiative must be done in a way that is fair to employees and does not make sudden, unplanned and adverse changes in their pay and compensation.

The Administration has asked for legislation that would phase in a conversion from COLA to locality pay over seven years. This proposal has many positive features. It would substantially improve retirement benefits for impacted employees. At the end of the seven year period, if the locality pay rate is less than the amount of non-foreign COLA for a particular area, employees would continue to receive the difference in non-foreign COLA and locality pay until the locality rate reaches the COLA amount. However, the Administration's proposal has several significant shortcomings that need to be corrected. Instead, we believe the Congress should use

as a starting point S. 3013, the Non-Foreign Area Retirement Equity Assurance Act of 2008 introduced by Senators Akaka, Stevens, Inouye, and Murkowski.

S. 3013 is a much fairer and more sensible proposal than the Administration's. Rather than the lengthy seven year phase in period, S. 3013 calls for a three year phase in period. For employees concerned as to the retirement disadvantage under COLA, it allows for a speedier transition. And for federal workers who feel the transition does not benefit them, the bill also allows for a one-time, irrevocable opt-out. The Akaka bill also allows for a retirement credit buy-back for the period of January 1, 2009 to December 31, 2011. The proposed legislation also includes provisions to guarantee that no employee would see an unfair reduction in his or her paycheck by implementing a fairer offset formula than the Administration's proposal, and protect the pay standards of those employees under special rates.

Without the features of S. 3013 that are lacking in the Administration's proposal, some federal employees could actually see their compensation decreased. Cutting the pay of federal workers because they live in these states or territories is unfair and would cause grave harm to employee morale.

Conclusion

In summary, I would like to emphasize that NTEU's continued recommendation is full implementation of FEPCA. NTEU also supports FEPCA's continued utilization of the cost-of-labor standard since it reflects the basic tenet of pay comparability with the private sector in a way that cost-of-living comparisons do not. The reason employees are not receiving adequate pay in high cost areas is because FEPCA is not being implemented, not because of the relatively minor differences between cost-of-labor and cost-of-living indexes. Finally, NTEU supports removing inequities caused by pay compression for GS employees and reforming the non-foreign COLA for Alaska, Hawaii and affected U.S. territories.