

**STATEMENT BY**  
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**BEFORE**

**THE SENATE GOVERNMENTAL AFFAIRS COMMITTEE**

**REGARDING**

**THE DEPARTMENT OF DEFENSE PERSONNEL SYSTEM**

**ON**

**JUNE 4, 2003**

Madam Chairman and Committee Members:

On behalf of the more than 600,000 federal employees represented by the American Federation of Government Employees, AFL-CIO (AFGE) including 200,000 in the Department of Defense (DoD), I thank you for the opportunity to testify today on several aspects of legislation to give the Secretary of Defense discretion over whether to abide by numerous chapters of Title 5.

At the outset of my testimony, let me thank you, Madam Chairman, as well as Senators Levin and Voinovich, for the numerous changes you have made to the House-passed version of the Department's personnel system proposal. While we remain profoundly concerned about the fairness of and the economic impact on federal employees from the establishment of a pay-for-performance system as well as other issues which we will discuss in greater detail, we are grateful for your willingness to study this matter closely. By taking the time to do so, you have managed to write legislation which substantially restrains the Department's desire for a blank check to create a new personnel system.

The authorities sought by the Pentagon are broad and have profound implications for not only the reality of the merit-principle based civil service system, but also for the very idea of a merit-principle based civil service system. AFGE believes that the passage of the Defense Department's legislative proposal would result in an abandonment of the principles that undermine the merit system precisely because it leaves so many aspects of that system unenforceable. No one will be able to hold the Secretary of Defense accountable for upholding the merit system principles if the legislation is passed; one must only hope and trust.

Support for the Pentagon's request amounts to a willingness to exchange a civil service both based upon and held accountable to the merit system principles for systems to be designed, implemented, and adjudicated by a political appointee – the Secretary of Defense. The risk that this system will be politicized, and characterized by cronyism in hiring, firing, pay, promotion, and discipline are immense. And the ability to mitigate that risk will be miniscule.

AFGE strongly opposes the Pentagon's proposal as passed by the House of Representatives on the grounds that it erases decades of social progress in employment standards, punishes a workforce that has just made a crucial and extraordinary contribution to our victory in Operation Enduring Freedom, and takes away from Congress and affected employees the opportunity they now possess to have a voice in crafting and approving the personnel and other systems of the Department of Defense. Today, no one owns the Department of Defense – it is a public institution, supported by U.S. taxpayers and administered by a Secretary of Defense appointed by an elected President, and overseen and regulated by the U.S. Congress. If the House bill is enacted, each individual Secretary of Defense, in cooperation with each President, will effectively own the

Department of Defense as if it were a private concern. If the House version becomes law, Congress will have relinquished its oversight and legislative role with regard to approximately 700,000 government personnel.

AFGE finds it entirely implausible that Pentagon officials honestly believe that the Defense Department needs sweeping new authorities for every Secretary of Defense in order to be successful in the future. The civilian employees of DoD represented by AFGE have been working around the clock for months supporting and maintaining both troops and weapons, loading materials and combat forces onto ships, aircraft, and tanks; or in many cases serving on active duty as well as caring for the military families who have been waiting at home for their loved ones to return. They are justly proud of their contribution, and are devastated to learn that Pentagon leaders intend to respond to their effort with Operation Erode the Civil Service.

The fact is that there is no serious or true rationale for this legislation. Over the past 12 years, DoD has achieved BRAC, services realignment, the creation of several agencies, including:

- Defense Logistics Agency (DLA),
- Defense Finance and Administration Service (DFAS)
- Defense Commissary Agency (DeCA)
- Defense Printing Agency (DPA)
- Defense Contract Audit Agency (DCAA)
- Defense Contract Management Agency (DCMA)
- National Imagery and Mapping Agency (NIMA)
- Defense Information Systems Agency (DISA),

and the elimination and consolidation of several agencies, widespread privatization, and downsizing of more than 200,000 federal positions. DoD has been granted tremendous flexibility, and it has exercised its authorities to the maximum extent. They have engaged in numerous successful combat missions, including two wars in the Gulf and in Europe. They have done a tremendous job advancing and protecting our nation's security interests. What did they need to do to protect our nation's security that the laws and regulation they seek the authority to waive prevent? What is the problem they are trying to solve?

I am not here to tell you that everything is fine at DoD from the perspective of DoD's rank and file civilian workforce. They have been asked to do more with less throughout the past decades deficit reduction and simultaneous and repeated reorganizations, transformations and policy shifts. Thousands live under the constant threat that DoD will contract out their jobs without giving them an opportunity to compete in a fair public-private competition. Because the downsizing of the 1990's was undertaken without regard to mission or workload, DoD's acquisition workforce was cut in half at the same time that the number and dollar value of service contracts exploded, making the job of oversight and

administration of contracts ever more difficult. The promise that federal salaries would rise gradually in order to become comparable to private sector rates, as provided by the bipartisan Federal Employees Pay Comparability Act of 1990 (FEPCA) has not been realized, and DoD's blue collar employees have likewise been denied the prevailing wage rates that their pay system promises to them.

But nothing in the House bill would begin to solve any of those problems; instead, the House bill would take away from Congress not only the opportunity, but also the responsibility for addressing them, and likely result in making each of those problems worse. This is in stark contrast to the approach taken by you, Madam Chairman, and Senators Levin and Voinovich, in your proposal and AFGE deeply appreciates the difference. In particular, your bill demonstrates not only a willingness, but a determination to reign in some of the most egregious and outrageous of the Pentagon's demands that the House refused to address.

### **Description of the House-Passed Bill**

What does DoD's legislative proposal as passed by the House do to civilian DoD employees? It would amend title 5, United States Code, by adding chapter 99 establishing a new Department of Defense National Security Personnel System. Although many have described these provisions as analogous to the Homeland Security Act, there are notable exceptions.

Secretaries of Defense would be given authority to establish, by regulations prescribed jointly with the Office of Personnel Management (OPM), human resources management systems for some or all of the organizational units of DoD. In addition, they would be authorized to waive the requirement that regulatory changes be issued jointly, "subject to the direction of the President." It is not clear what "subject to the direction of" means, i.e., whether it implies that the authority may be exercised "subject to the approval of" or whether the Secretaries may undertake such unilateral action only when told to do so by the President.

In addition to the above, the legislation gives to Secretaries of Defense powers that go far beyond the unprecedented authorities given to the Secretaries of the Department of Homeland Security. The following is nonwaivable for DHS employees but would be waivable for DoD employees under the proposed legislation:

Subchapter V of Ch. 55: Premium Pay

In addition, the following chapters of title 5 would not technically be waivable:

Ch. 31: Authority for Employment (hiring)

Ch. 33: Examination, Selection, and Placement, and  
Ch. 35: Retention Preference, Restoration, and Reemployment

The bill specifically allows the Secretary to exercise authorities that would otherwise be available to him under paragraphs

- (1) methods of establishing qualification requirements for, recruitment for, and appointment to positions;
- (2) methods of assigning, reassigning, or promoting employees; and
- (8) methods of reducing overall agency staff and grade levels.

of section 4703 (a) of title 5. It thus appears that what the Department was unable to get through the front door; i.e. with a broad waiver of Chapters 31, 33, and 35, in order to eliminate current employee and taxpayer protections on hiring, assignment, promotion, and the conduct of reductions-in-force, they have achieved through the back door of demonstration project authority. DoD's House-backed legislation could eliminate the requirement that reductions in force (RIF) be conducted according to procedures set out in chapter 35. These procedures assure that RIFs are conducted on the basis of employment status and length of service as well as efficiency or performance ratings. On what basis would supervisors select individuals for RIFs without the constraints described in chapter 35's procedures? No one knows, and no one will know since each Secretary of Defense would apparently have authority to write and rewrite RIF rules if the House-backed bill is enacted. Indeed, every time DoD conducts a RIF, the rules could change. The bill would allow supervisors to decide who will be the victim of a RIF on the basis of subjective factors, rather than performance, seniority, and employment status.

Allow me to give you one example of how the agency might abuse such authority. It is an example that is very much on the minds of DoD civilian employees: Reductions-in-force could be run so that all of those who are nearing retirement eligibility, but have not yet reached that point would receive a pink slip. In this example, DoD could not only reduce staffing as might be necessary, but also eliminate their obligation for retirement costs. This example is all too common in the private sector. Title 5 was specifically written in such a way as to prevent such abusive managerial practices during federal employee layoffs, and we must be mindful of these possibilities as the Department's greed for unfettered flexibility is debated in the weeks ahead. While the Senate bill is more restrictive, granting demonstration project authority for hiring, AFGE remains concerned about how this authority will be used.

The House bill, like the Homeland Security Act, authorizes Defense Secretaries to waive the following critical chapters of title 5:

Ch. 43: Performance appraisal system  
Ch. 51: Position Classification

- Ch. 53: Pay rates and systems (GS/WG/grade and pay retention)
- Ch. 71: Collective Bargaining rights
- Ch. 75: Due process
- Ch. 77: Appeal rights/judicial review

### **Pay and Classification**

It is worth elaborating what all this would mean in very practical terms. Allowing each new Secretary of Defense to waive chapters 53 and 51 of Title 5 means that each new Secretary of Defense would be free to create a wholly new pay and position classification system for the Department. It would mean that any Secretary of Defense could eliminate the General Schedule (GS) and the Federal Wage System (FWS) or their successors (whatever they might be) and replace them with new systems of his own design. Annual salary adjustments, nationwide and locality, passed by the Congress to help federal salaries keep pace with private sector wage increases would be gone. Periodic step increases for eligible workers who are performing satisfactorily would be gone. The current Secretary of Defense is said to prefer a pay banding system that allows supervisors to decide whether and by how much an individual employee's pay might be adjusted. Supervisors, not Congress, would decide whether DoD employees get a raise and what the size of that raise would be. No one knows how future Secretaries of Defense might exercise this power.

Chapter 51 describes the current classification system and requires that different pay levels for different jobs be based on the principle of "equal pay for substantially equal work." New systems designed by successive Secretaries of Defense would not have to adhere to that standard. Jobs which are graded similarly today on the basis of that principle might therefore be treated completely differently when various and successive new systems are put into place by each new Secretary of Defense. Granting these authorities to each new Secretary of Defense with regard to classification raises serious concern, as the current standards go a long way toward preventing federal pay discrimination on the basis of race, gender, or ethnicity.

### **Premium Pay**

Another shocking and dangerous waiver authority is sought in the House legislation with regard to subchapter V of chapter 55, which covers Premium Pay. This subchapter addresses numerous issues ranging from overtime and compensatory time calculations, firefighter pay, Sunday and holiday pay, as well as compensatory time off for religious observances. By waiving subchapter V of chapter 55, the current and each new Secretary of Defense would have the power to turn back the clock on the last several decades of progressive legislation on matters crucial to the economic security of federal employees and their families. The Senate bill, by contrast, wisely prevents the waiver of subchapter V of chapter 55.

## **Performance and Appeal Rights**

Allowing waiver of chapter 43 gives over to each Secretary of Defense the power to unilaterally decide a system for taking action against poor performers. In order to make sure that federal employees are not the targets of unwarranted or arbitrary discipline, current law provides employees with an opportunity to undertake a “performance improvement period” before they are disciplined for poor performance. In any new systems created by different administrations, current safeguards and the opportunity to improve **or appeal** may be eliminated.

The House bill allows the Secretary of Defense to waive chapters 75 and 77, which puts in jeopardy DoD employees’ due process and appellate rights. While non-union private sector workers have no legal right to appeal suspensions, demotions, or dismissals from their jobs, federal workers have these legal rights for very important reasons. In addition to being the right thing to do, because their employer is the U.S. government, the guarantor and enforcer of American citizens’ due process rights, the bar is higher than for private firms whose obligations are different. Thus chapter 75 sets up a system for management to suspend, demote, or dismiss employees, but provides employees with the ability to appeal these actions to the Merit Systems Protection Board (MSPB) if there is evidence that the actions were motivated by factors other than performance, including racial or other prejudice, political views, or union status. Under this chapter, DoD employees are eligible for advance written notice of the disciplinary action, a reasonable time to respond, representation by an attorney, and a written decision by DoD listing the specific reasons for the disciplinary action. Any Secretary of Defense could eliminate these protections under the House bill.

Chapter 77 establishes the procedures for appealing to not only the MSPB, but also describes procedures for appealing decisions that are alleged to involve discrimination either to the MSPB or the Equal Employment Opportunity Commission (EEOC), and for accountability, establishes judicial review of MSPB decisions. Giving each Secretary of Defense the power to do away with the rights and procedures described in chapters 75 and 77 means that DoD workers could lose and regain these rights according to the political preferences of any Administration. In the House-passed bill, one Secretary of Defense may decide that employees of DoD should have little or no right to information about why they are being disciplined, and little or no right to appeal decisions against them. Another Secretary of Defense may reinstate procedures for the period of his tenure, but they may disappear again after the next election.

In contrast, the Senate bill effectively maintains the rights described in chapters 75 and 77, and AFGE greatly appreciates the tremendous effort that has been made to address our concerns in these areas. Regarding the language on Employee Grievances and Appeals, the Senate bill is a substantial improvement over the House bill, which virtually parrots DoD’s original proposal. Maintaining

an employee's Merit Systems Protection Board (MSPB) appeal rights and judicial review over adverse actions, discrimination cases, and whistle-blower protection issues is crucial. While we question the constitutionality of the House Bill, which provides for only an internal DoD review of these cases, I must emphasize how unlikely it will be for any whistleblower to ever come forward with documented instances of fraud and abuse if his/her case is to be heard by an internal DoD Board selected by the Secretary with no avenue of a hearing before a neutral third party followed by judicial review. Perhaps, this part of the House Bill should be called "The Maintenance of the \$800 Hammer Provision" since employees will be well-advised to remain silent and look the other way when confronting fraud, waste, or abuse in DoD.

DoD should be quite satisfied with the appeals provisions contained in the Senate Bill. Currently, employees may be fired for cause where the Agency meets its burden of proof by a "preponderance" of the evidence (50.1%) if the Agency follows Chapter 75 procedures. If an Agency fires an employee based on poor performance under Chapter 43, only the lower "substantial" evidence standard is necessary (any evidence in the record that a reasonable person might accept as adequate even though reasonable persons (or the Board itself) might disagree with the Agency's conclusion). Agencies currently win about 85% of these cases now, which is a clear indication that the current legal standards are in no way "tilted" towards employees.

### **Collective Bargaining**

Current law, as set forth in chapter 71 of title 5, allows DoD employees to organize into labor unions and pursue union representation through the process of collective bargaining with management over some conditions of employment. Giving each Secretary of Defense the authority to waive some or all of chapter 71 eliminates a very important part of the system of checks and balances that hold managers and political appointees accountable. It eliminates the process by which disputes between employee representatives and management are resolved. Today, labor-management impasses are sent to the Federal Services Impasses Panel (FSIP), a seven-member board appointed by the President, which acts as a binding arbitrator on all disputes. The legislation as passed by the House would prohibit any national bargaining or negotiability impasses, no matter how routine or unrelated to national security, from going to the FSIP, the Federal Labor Relations Authority, or any third party outside DoD. This is unprecedented and any Secretary of Defense who might exercise this authority would render the entire collective bargaining process a sham.

The House-passed version capitulates to the Pentagon's baseless contention that this authority is necessary for military "agility." In effect, waiving chapter 71, as the House bill provides, would allow any Secretary of Defense to create new personnel systems without any formal give- and-take with the affected employees' **elected** representatives.



AFGE strongly supports the Senate bill's retention of chapter 71, which assures DoD employees that when they exercise their basic democratic right to vote to elect union representation, the Secretary of Defense will not have the authority to negate their vote and deprive them of the opportunity to have their concerns and their views considered by management. Further, it affords represented employees an opportunity to resolve conflict through avenues not controlled entirely by management, an irreducible conflict of interest since management will always be a party to the conflict. In addition, we believe that it offers the only mechanism that will ensure that DoD's employees will not become helpless victims of the whims of various Secretaries of Defense as they exercise the broad authorities granted elsewhere in the legislation.

### **Individual Pay for Performance: A Perpetual War of All Against All**

There is no reason to believe that individualized pay for performance is a wise choice for the federal pay system generally, or for a new pay system applicable only in the Department of Defense. The House bill specifically does not ask Congress to approve a new pay system or a new personnel system, but instead asks Congress to relinquish this authority to successive Secretaries of Defense. In contrast, the Senate bill does set forth the broad outlines of a pay for performance system. The Navy's China Lake Plan is often cited as an example of a pay for performance plan that might be a model for a DoD-wide pay system, and it is likely that it would comply with the guidelines described in the Senate bill.

The question of whether the China Lake Plan is a worthy successor to the General Schedule for DoD or any other agency is one useful way to consider how the authorities in the legislation might be used or abused. Indeed, comparing it to the GS system is just one way of gauging whether pay for performance would mean going from the frying pan into the fire, or would constitute some form of progress for either federal employees or federal agencies. To that end, it is worth providing an accurate description of the GS system and its performance elements, since it has been unfairly maligned as a system that makes little or no connection between productivity and pay.

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 who claim that it is an aged and inflexible historical relic, 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.

### **Flexibility in Times of Peace**

FEPCA introduced a panoply of pay flexibilities into the allegedly rigid General Schedule of which DoD has made ample use:

- 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 two or 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, and proper steps can be taken either to discipline the employee, demote the employee, and give him an opportunity to improve.

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 has done much to prevent 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 41<sup>st</sup> 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 as a result of Congressional action, 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 and is particularly acute in DoD because of the downsizing of more than 200,000 jobs in that decade, has turned into a full-fledged human capital crisis, as the stubborn refusal to implement the locality pay system which was designed to improve recruitment and retention of the next generation of federal employees continues.

### **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.

China Lake has extremely elaborate and complex mechanics for calculating performance pay, and has an equally elaborate classification system. The particulars of the system demonstrate that while China Lake's design may be appropriate to some scientists and engineers, it would not be appropriate for the full range of federal positions, since many are in occupations and workplaces that place extreme or even total limitations on creativity, individual initiative, or individualized performance. China Lake also shows that administrative ease is not 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.

### **AFGE’s Views on the General Schedule vs. “Individualized Pay for Performance”**

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. Most recently, DoD's own data from its "Best Practices" pay demos has shown that they have not led to improvements in productivity, accomplishment of mission, or cost control.

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?

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. DoD employees, in particular, are drawn to the agency's national security mission.

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.<sup>1</sup>

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 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

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<sup>1</sup> “Six Dangerous Myths about Pay”, by Jeffrey Pfeffer, Harvard Business Review, May-June 1998 v. 76, no.3, page 109 (11).

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 DoD's civilian 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.

Perhaps most 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.

Given these data, it is 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?

We believe that the advocates of pay for performance in DoD or elsewhere 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. Before an entire agency is sent down the path of pay for performance, they must develop a better track record to show 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. The language in the Senate bill that instructs DoD to impose pay for performance gradually is a step in the right direction, but it continues to allow far too much discretion and too little accountability.

No one has shown either how or why individualized pay for performance might be superior to systems that provide financial reward for group and organizational excellence, especially in a public sector context. No one has demonstrated exactly how or 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.

The Senate bill does instruct DoD to invest in the training, oversight, and staffing necessary to administer elaborate and complex, federal employee by federal

employee pay for performance plans. All we can say in that context is that the investment will need to be very large and ongoing, and must be made available to affected employees as well as managers. Finally, although the Senate bill asks for funding for the pay for performance system that will be equivalent to what continued funding of the GS system would entail, we strongly suggest that that individualized performance incentive payments should be a supplement, not a substitute for a fully funded regular pay system that reflects labor markets and protects purchasing power. Without adequate funding, it is certain that pay for performance will 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.

## **Conclusion**

Pentagon officials have argued their case as a plea for freedom – freedom *to* waive the laws and regulations that comprise the federal civil service – so that the nation’s security can be assured. We ask Members of the Committee to consider that our opposition is a plea for freedom as well – freedom *from* political influence, freedom from cronyism, freedom from the exercise of unchecked power. As the Defense Department is not a private corporation, the pressures of the competitive market will not hold it accountable for mismanagement or cronyism. That is why government agencies operate under a set of laws and regulations set by the Congress; that way, taxpayers and government employees are guaranteed freedom from coercion and corruption.

We have no reason to suspect that there is any intention to abuse the power DoD has sought for its Secretaries of Defense. Nevertheless, history has shown that a concentration of power in the hands of one individual does not necessarily translate into success on the battlefield. Our nation’s tradition of checks and balances on power has been tremendously successful in allowing our military the freedom *to* pursue our nation’s security interests at the same time that the public and the civilian workforce are allowed freedom *from* unfettered military authorities.

Pay for performance is notoriously easy to support in concept; it is in its execution that its flaws are revealed. Indeed, the practical issues of implementation of pay for performance reveal why it can be especially inappropriate for the public sector. The civil service is sworn to uphold the highest standards of objectivity, professionalism, and public spiritedness. Pay systems that vest political appointees and the management staff that works directly under them, with the discretion to award or withhold salary adjustments on the basis of subjective judgements are inherently dangerous. The truth is that even in the private sector, managerial discretion over the awarding of jobs and raises are severely restrained – every effort is made to tie awards to objectively

measurable factors, and every effort is made to encourage group or division awards in order to promote a sense of teamwork and cooperation.

AFGE has always supported our nation's military mission, and we remain ready and willing to sit down with Pentagon leaders to work collaboratively to solve any real problems they have experienced with regard to accomplishing that mission that can be traced to the civil service infrastructure.

Again I would like to commend you, Chairman Collins, as well as Senators Levin and Voinovich, for preserving the collective bargaining and appeals processes for rank and file DoD workers. These are time- proven and constructive ways to promote effective communication between labor and management and accountability to the merit system principles, and the Senate bill is right to insist on their protection. Nevertheless, I urge the Committee in the strongest possible terms to reject the other authorities contained in the legislation, particularly the rush to replace the General Schedule and the Federal Wage System with a management-controlled pay for performance system that is wholly inappropriate to the public sector.

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