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Testimony before the Subcommittee on Oversight of Government Management, the Federal Workforce, and the District of Columbia, Committee on Homeland Security and Governmental Affairs, U.S. Senate

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## HUMAN CAPITAL

# Selected Agencies Have Implemented Key Features of Their Senior Executive Performance-Based Pay Systems, but Refinements Are Needed

Statement of J. Christopher Mihm, Managing Director  
Strategic Issues





Highlights of [GAO-08-1019T](#), a testimony before the Subcommittee on Oversight of Government Management, the Federal Workforce, and the District of Columbia, Committee on Homeland Security and Governmental Affairs, U.S. Senate

### Why GAO Did This Study

In 2003, Congress and the administration established a performance-based pay system for Senior Executive Service (SES) members that requires a link between individual and organizational performance and pay. Specifically, agencies are allowed to raise SES pay caps if their systems are certified by the Office of Personnel Management (OPM) with concurrence by the Office of Management and Budget (OMB) as meeting specified criteria.

GAO was asked to testify on preliminary results of ongoing work analyzing selected executive branch agencies' policies and procedures for their SES performance-based pay systems in the following areas: (1) factoring organizational performance into senior executive performance appraisal decisions, (2) making meaningful distinctions in senior executive performance, and (3) building safeguards into senior executive performance appraisal and pay systems. GAO selected the U.S. Departments of Defense (DOD), Energy (DOE), State, and the Treasury; the U.S. Nuclear Regulatory Commission (NRC); and the United States Agency for International Development (USAID) based on variations in agency mission, organizational structure, and size of their career SES workforces. To date, GAO has analyzed agencies' SES performance management policies and guidance and analyzed aggregate SES performance appraisal data as provided by the agencies for fiscal year 2007.

To view the full product, including the scope and methodology, click on [GAO-08-1019T](#). For more information, contact J. Christopher Migh at (202) 512-6806 or [mihmj@gao.gov](mailto:mihmj@gao.gov).

## HUMAN CAPITAL

### Selected Agencies Have Implemented Key Features of Their Senior Executive Performance-Based Pay Systems, but Refinements Are Needed

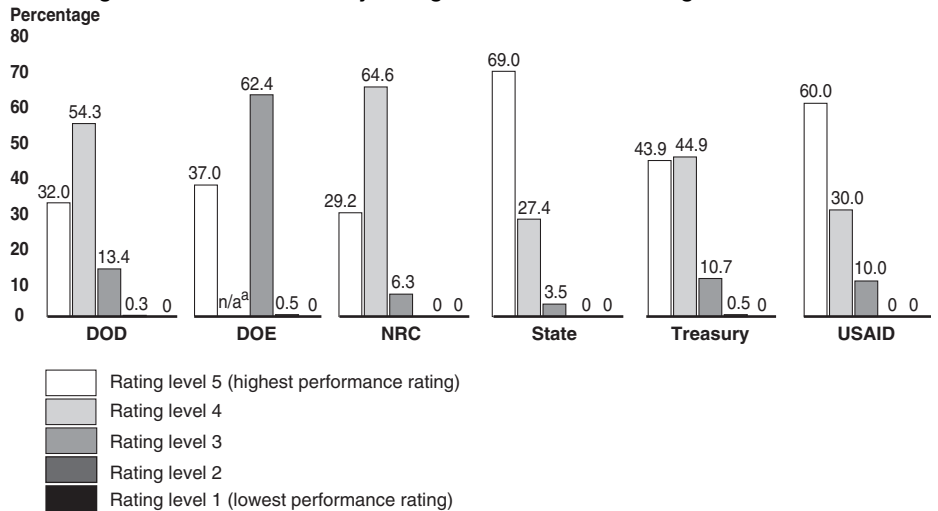
#### What GAO Found

Overall, the selected agencies are making positive steps toward three key areas related to OPM and OMB's certification criteria, with some opportunities for refinements in these areas.

**Factoring organizational performance into senior executive performance appraisal decisions:** All of the selected agencies have policies in place that require senior executives' performance expectations to be aligned with organizational results and organizational performance to be factored into appraisal decisions. Improvements in communicating organizational performance to reviewing officials could be made.

**Making meaningful distinctions in senior executive performance:** While all of the selected agencies have multiple rating levels in place for assessing senior executive performance, senior executives were concentrated at the top two rating levels in the fiscal year 2007 appraisal cycle, as shown below.

**Percentage of Senior Executives by Rating Level at the Selected Agencies**



Source: GAO analysis of agency data.

Note: DOE uses a four-level appraisal system.

**Building safeguards into senior executive performance appraisal and pay systems:** The selected agencies varied in how they implemented predecisional checks of appraisal recommendations through higher-level reviews and Performance Review Boards as well as transparency in the aggregate results with opportunities to improve communication of aggregate appraisal results to all senior executives.

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Mr. Chairman, Senator Voinovich, and Members of the Subcommittee:

I am pleased to be here today to discuss our preliminary results concerning selected agencies' policies and procedures for the performance-based pay systems for career members of the Senior Executive Service (SES). As you know, in recent years, Congress and the administration modernized the performance appraisal and pay systems for senior executives by requiring a clearer link between individual performance and pay. Specifically, agencies are allowed to raise SES base pay and total compensation caps if their performance appraisal systems are certified by the Office of Personnel Management (OPM) with concurrence by the Office of Management and Budget (OMB) as, among other things, linking performance for senior executives to the organization's goals and making meaningful distinctions based on relative performance.

In our past work on performance management and pay issues, we have reported that performance-based pay cannot be simply overlaid on most organizations' existing performance management systems.<sup>1</sup> Rather, as a precondition to effective pay reform, individual expectations must be clearly aligned with organizational results, communication on individual contributions to annual goals must be ongoing and two-way, meaningful distinctions in employee performance must be made, and cultural changes must be undertaken. Most important, leading organizations have recognized that effective performance management systems create a "line of sight" showing how unit and individual performance can contribute to overall organizational goals and can help them drive internal change and achieve external results.<sup>2</sup> As you know, effective performance management systems that hold executives accountable for results can help provide continuity during times of leadership transition, such as the upcoming change in the administration, by maintaining a consistent focus on organizational priorities. We have reported that there are significant opportunities to strengthen agencies' efforts in holding senior executives accountable for results through their performance management systems—

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<sup>1</sup>GAO, *Human Capital: Symposium on Designing and Managing Market-Based and More Performance-Oriented Pay Systems*, [GAO-05-832SP](#) (Washington, D.C.: July 27, 2005). For additional information on our past work related to SES performance management systems and the certification process, see app. II of this statement.

<sup>2</sup>GAO, *Human Capital: Senior Executive Performance Management Can Be Significantly Strengthened to Achieve Results*, [GAO-04-614](#) (Washington, D.C.: May 26, 2004).

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in particular, by linking senior executives' performance expectations to the achievement of results-oriented organizational goals.

OPM's recently released 2008 governmentwide SES survey results found that senior executives across the government recognize the importance of linking pay to performance with about 93 percent of the respondents strongly agreeing or agreeing that pay should be based on performance. In addition, the majority of senior executives reported that their performance ratings were linked to their salary increases and bonuses to a very great or great extent. However, senior executives recognized the challenge of making meaningful distinctions in performance—a key criterion for agencies' certification of their SES appraisal systems. Specifically, less than a third of senior executives governmentwide strongly agreed or agreed that bonuses or pay distinctions were meaningfully different among executives.

At your request and Senator Dorgan's, we are preparing a report highlighting selected federal agencies' policies and procedures for their SES performance appraisal and pay systems and OPM and OMB's oversight of the certification process (for additional background on the governmentwide SES performance-based pay system and certification criteria, see app. I). Today, I will present preliminary observations from our ongoing review. As requested, I will discuss the policies and procedures at selected agencies addressing three key areas: (1) factoring organizational performance into senior executive performance appraisal decisions, (2) making meaningful distinctions in senior executive performance, and (3) building safeguards into senior executive performance appraisal and pay systems. In our forthcoming report, we plan to report on OPM and OMB's oversight role and make recommendations to the selected agencies on areas of refinement for their senior executive performance appraisal and pay systems and to OPM and OMB to strengthen their oversight roles.

For our review, we selected the U.S. Departments of Defense (DOD), Energy (DOE), State, and the Treasury; the U.S. Nuclear Regulatory Commission (NRC); and the United States Agency for International Development (USAID) based on variations in agency mission, organizational structure, size of their career SES workforces, and past results of their SES performance appraisal systems through rating and bonus distributions. To date, we have analyzed these agencies' SES performance management policies, directives, and guidance, and other related documents; interviewed cognizant agency officials, including OPM and OMB officials, regarding the certification process; and analyzed

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aggregate SES performance rating, bonus, and pay adjustment data as provided by the agencies for fiscal year 2007. In analyzing the fiscal year 2007 appraisal data, we defined our universe of analysis as career senior executives who received ratings. In calculating the percentage of eligible senior executives who received bonuses (cash awards) or pay adjustments (increases to basic pay) and average amounts, we excluded executives who received a rating less than “fully successful” (level 3), as applicable, from the eligible population since those executives are not eligible to receive bonuses or pay increases, according to the selected agencies’ policies. We also excluded senior executives at NRC, Treasury, and State who received Presidential Rank Awards from our calculations of percentages of eligible SES members receiving bonuses and average amounts because those individuals were not considered for bonuses that year, according to the agencies’ policies. In order to have consistency in our analysis across selected agencies, we included senior executives who were rated but left their positions—because of retirement, attrition, or assignment to a lower grade—prior to performance payouts being made in our analysis. The agencies’ policies and practices varied in whether or not senior executives who retired were eligible for performance payouts. We checked the agency data for reasonableness and the presence of any obvious or potential errors in accuracy and completeness. We also reviewed related agency documentation, interviewed agency officials knowledgeable about the data, and brought to the attention of these officials any concerns or discrepancies we found with the data for correction or updating. On the basis of these procedures, we believe the data are sufficiently reliable for use in the analyses presented in this statement. Agency officials also verified the accuracy of the facts presented in this statement.

The examples of the selected agencies’ policies and procedures for their SES performance-based pay systems are not generalizable to the governmentwide SES population and all executive branch agencies. We did not assess how the selected agencies are implementing all the policies and procedures for their SES performance-based pay systems. An agency may have implemented a policy related to the three key areas even if it is not specifically highlighted in this statement. We conducted our work from October 2007 to July 2008 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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In summary, the selected agencies are making positive steps in generally addressing three key areas related to OPM and OMB's certification criteria through their SES performance-based pay systems with some opportunities for refinements of their systems. First, all of the selected agencies have policies in place that require senior executives' performance expectations to be aligned with organizational results and organizational performance to be factored into senior executive appraisal decisions. However, OPM has found that while many agencies are doing a good job of clarifying the alignment of executive performance plans with agency mission and goals, some of the plans often still fall short of identifying the measures used to determine whether the results are achieved. While the agencies identified common organizational assessments for consideration in senior executive appraisal decisions, NRC and Treasury identified other types of tools to assess performance at the office or bureau level. OPM has emphasized the importance of communicating to individuals involved in appraisal decisions the effect organizational performance can have on individual ratings and overall rating distributions through briefings or other communications. Several of the selected agencies shared the organizational performance assessments and communicated the importance of considering organizational performance through briefings, training, or document packages for the Performance Review Board (PRB) meetings, while State did not communicate any information regarding organizational performance.

Second, while all of the selected agencies have multiple rating levels in place for assessing senior executive performance, several of the agencies, such as NRC, State, and DOE, designed their appraisal systems to help allow for differentiations when assessing and rewarding executive performance by establishing tier structures or prescribed performance payout ranges based on the resulting performance rating. However, our analysis shows that the senior executives are concentrated at the top two rating levels for the most recently completed appraisal cycle. Further, at almost all of the agencies, the highest-performing executives, rated as "outstanding" (level 5), made up the greatest percentage of eligible executives receiving bonuses with the largest bonuses on average, with the exception of NRC where all the eligible executives rated at the top two levels received a bonus. For pay adjustments, the majority of eligible senior executives rated at fully successful or higher received pay increases, but unlike bonus distributions, at some of the selected agencies, the highest performing executives did not comprise the greatest percentage of executives receiving pay increases with the largest increases on average.

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Third, all of the selected agencies have built safeguards into their senior executive performance appraisal and pay systems—such as predecisional checks of performance appraisal recommendations through higher-level reviews and PRBs as well as transparency in the aggregate results—to help enhance the credibility, fairness, and transparency of their systems, although they varied in how the safeguards have been implemented. Our preliminary results show that there are opportunities for USAID to improve the communication of aggregate appraisal results to all senior executives, rather than just individual appraisal results to the appropriate executive. Communicating an executive’s individual rating conveys information about how well the executive has performed against the expectations in the performance plan, but is not sufficient to provide a clear picture of how the executive’s performance compares with other executives in the agency.

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## Factoring Organizational Performance into Senior Executive Performance Appraisal Decisions

In our past work on performance management, we have identified the alignment of individual performance expectations with organizational goals as a key practice for effective performance management systems.<sup>3</sup> Having a performance management system that creates a “line of sight” showing how unit and individual performance can contribute to overall organizational goals helps individuals understand the connection between their daily activities and the organization’s success. According to OPM, agency systems do not yet place sufficient emphasis on achieving measurable results. OPM has said that the criterion for alignment with organizational results is often the hardest of the certification criteria for agencies to meet. While many agencies are doing a good job of clarifying the alignment of executive performance plans with agency mission and goals, some of the plans often still fall short of identifying the measures used to determine whether the results are achieved, according to OPM. This challenge of explicitly linking senior executive expectations to results-oriented organizational goals is consistent with findings from our past work on performance management.<sup>4</sup>

To help hold senior executives accountable for organizational results, beginning in 2007, OPM required agencies to demonstrate that at least 60 percent of each senior executive’s performance plan is focused on

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<sup>3</sup>GAO, *Results-Oriented Cultures: Creating a Clear Linkage between Individual Performance and Organizational Success*, [GAO-03-488](#) (Washington, D.C.: Mar. 14, 2003).

<sup>4</sup>[GAO-04-614](#).

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achieving results and has clear measures associated with those results to show whether the goals have been achieved in order to receive certification of their SES appraisal systems. The selected agencies in our review have designed their appraisal systems to address OPM's requirement of aligning individual expectations with organizational goals. For example, in setting expectations for the individual performance plans, DOE requires the senior executives and supervisors to identify three to five key performance requirements with metrics that the executive must accomplish in order for the agency to achieve its strategic goals. Weighted at 60 percent of the summary rating, the performance requirements are to be specific to the executive's position and described in terms of specific results with clear, credible measures (e.g., quality, quantity, timeliness, cost-effectiveness) of performance, rather than activities. For each performance requirement, the executive is to identify the applicable strategic goal in the performance plan. To ensure that agencies are implementing their policies for alignment of performance expectations with organizational goals, OPM requires agencies as part of their certification submissions to provide a sample of executive performance plans, the strategic plan or other organizational performance documents for establishing alignment, and a description of the appraisal system outlining the linkage of executive performance with organizational goals.

Further, OPM requires agencies to consider organizational performance in appraising senior executive performance to receive certification of their SES appraisal systems. According to OPM and OMB officials, the main sources of organizational performance that agencies use are the performance and accountability reports (PAR) and Program Assessment Rating Tool (PART) summaries, which capture agencywide as well as program- or office-specific performance. While identifying appropriate assessments of organizational performance to be used in appraisal decisions, agencies are also to communicate the organizational performance to the senior executives, PRB members, and other reviewing officials—including supervisors who complete the ratings—involved in appraisal decisions prior to the completion of individual performance ratings. In its certification regulations,<sup>5</sup> OPM does not specify the format in which agencies need to communicate organizational performance; however, OPM has emphasized the importance of communicating to individuals involved in appraisal decisions the effect organizational

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<sup>5</sup>5 CFR Ch. 1, Pt. 430, Subpart D.



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performance can have on individual ratings and overall rating distributions through briefings or other communications.

All of the selected agencies have policies in place for factoring organizational performance into senior executive appraisal decisions. While the agencies identified common organizational assessments, such as the President's Management Agenda (PMA), PAR, or PART results for consideration in senior executive appraisal decisions, several agencies identified other types of tools to assess performance at different levels of the organization, such as the bureau, office, or program levels. For example, NRC provides summary reports capturing office-level performance to rating and reviewing officials for appraising senior executive performance. Twice a year, NRC's senior performance officials (SPO)—two top-level executives responsible for assessing organizational performance—conduct assessments for each office that take into account quarterly office performance reports on their operating plans, an interoffice survey completed by the other directors as identified by NRC on the office's performance, as well as the office director's self-assessment of the office's performance. According to an NRC official, the resulting SPO summary reports are used in the midyear feedback by senior executives and their supervisors to identify areas for improvement for the remainder of the appraisal cycle. At the end of the appraisal cycle, rating officials and PRB members are to consider the SPO summary reports in appraising senior executive performance.

To assess bureau-level performance, Treasury uses a departmentwide organizational assessment tool that provides a "snapshot" of each bureau's performance across various indicators of organizational performance, such as the PAR, PART results, PMA areas, OPM's Federal Human Capital Survey results, budget data, and information on material weaknesses. The performance information is provided to PRB members and reviewing officials to help inform their senior executive appraisal recommendations.

The selected agencies varied in how they provided and communicated organizational performance assessments to PRB members and other reviewing officials to help inform senior executive appraisal recommendations. Several of the selected agencies shared the organizational performance assessments and communicated the importance of considering organizational performance through briefings, training, or document packages for the PRB meetings, while one agency did not provide or communicate any information regarding organizational performance.

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For example, at Treasury, all the PRBs across the department were briefed on the tool used to assess organizational performance and the importance of considering organizational performance in appraising senior executive performance. DOD provided the heads of its components with a departmentwide organizational assessment to be used in appraising senior executive performance and, as a check across the components, asked for copies of the training given to the PRB members and other reviewing officials on factoring organizational performance into senior executive appraisal recommendations. Through the office of the Deputy Secretary for Defense, DOD developed an assessment of the department's overall performance against its overall priorities for fiscal year 2007. According to a DOD official, the components had the flexibility to develop their own organizational assessments using the department's assessment as a guide and to consider other indicators of organizational performance. Having the components provide the department with their communications of organizational performance helps provide a check in the process across the components and ensures that the spirit and policies of the performance management system are being followed, according to a senior DOD official.

As part of the documents received prior to the meeting, NRC provides PRB members with various indicators of organizational performance, such as the SPO summary reports, PAR, and PART information. As part of communicating the organizational assessments, NRC instructs the PRB members to review the summary of proposed ratings and scores for consistency with SPO reports, PAR, and PART outcomes, with rankings of executives recommended by office directors, and across offices and programs. Similarly, DOE provides its PRB members snapshots of the Consolidated Quarterly Performance Reports relevant to the senior executives that measure how each departmental element performed respective to the goals and targets in its annual performance plan. According to the Director of the Office of Human Capital Management, the Deputy Secretary also verbally briefed the PRB members on the importance of considering organizational performance in appraising executive performance.

On the other hand, State did not provide its PRB members and other reviewers with any specific information on organizational performance to help inform their senior executive appraisal recommendations for the most recently completed appraisal cycle. According to State officials, PRB members received packages of information to help inform their decisions, including senior executives' performance plans and appraisals, the performance management policy, and the memo from the Director General

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of the Foreign Service and Director of Human Resources on performance bonuses and pay adjustment amounts and distributions for that cycle. While a senior State human resources official said that the PRB was made aware of a variety of organizational performance assessments that could be readily accessible, if needed, the PRB members did not receive any specific assessments of organizational performance.

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## Making Meaningful Distinctions in Senior Executive Performance

Effective performance management systems make meaningful distinctions between acceptable and outstanding performance of individuals and appropriately reward those who perform at the highest level. In order to receive certification of their SES systems from OPM with OMB concurrence, agencies are to design and administer performance appraisal systems that make meaningful distinctions based on relative performance through performance rating and resulting performance payouts (e.g., bonuses and pay adjustments). Specifically, agencies are to use multiple rating levels—four or five levels—and reward the highest-performing executives with the highest ratings and largest pay adjustments and bonuses, among other things.

Several of the agencies designed their appraisal systems to help allow for differentiations when assessing and rewarding executive performance by establishing tier structures or prescribed performance payout ranges based on the resulting performance rating. For example, NRC uses three tiers called position groups to differentiate its senior executives' basic pay and the resulting bonus amounts based on ratings received at the end of the appraisal cycle. NRC divides its executives into three groups (A, B, and C) based on difficulty of assignment and scope of responsibilities of the positions and annually sets basic pay ceilings for each of the groups tied to the levels of the Executive Schedule (EX), as shown in table 1. Pay ceilings within each group allow NRC to reserve pay above EX-III for executives who demonstrate the highest levels of performance, including the greatest contribution to organizational performance as determined through the appraisal system.

NRC uses the position groups and resulting performance ratings as the basis for its bonus structure to help ensure that executives in the higher position groups with the higher performance ratings receive the larger bonuses. For example, for fiscal year 2007, an executive in the highest position group (A) that received an outstanding rating was to receive \$30,000, while an executive in the lowest group (C) with the same rating was to receive a \$20,000 bonus. According to an NRC official, the bonus range for executives in group C with excellent ratings was intended to

help allow for meaningful distinctions in performance to be made within that group, as well as to give the agency flexibility in the amount of bonuses to be awarded.

**Table 1: NRC’s SES Position Groups with Basic Pay Ceilings and Resulting Bonus Amounts Based on Position Group and Performance Ratings for the Fiscal Year 2007 Appraisal Cycle**

Examples of SES positions by group	Basic pay ceiling (comparable to EX pay)	Resulting bonus amount based on performance rating received		
		Outstanding	Excellent	Meets expectations
A: Executive Director for Operations, Chief Financial Officer, General Counsel, major program office directors (e.g., Director of the Office of Nuclear Reactor Regulation)	\$172,200 (EX-II)	\$30,000	\$25,000	\$0
B: Support and small program office directors (e.g., Directors of the Offices of Administration and Human Resources), Deputy Directors of the Offices of the General Counsel and the Chief Financial Officer	165,350 (Midpoint between EX-II and III)	25,000	20,000	0
C: All other SES members	158,500 (EX-III)	20,000	8,000 – 13,800	0

Source: NRC.

Notes: NRC has a five-level appraisal system, but senior executives in the two lowest rating categories—unsatisfactory and needs improvement—are not eligible to receive bonuses based on their performance ratings. The governmentwide basic pay cap for SES under certified performance appraisal systems is EX-II.

State also uses a structure with six tiers to help differentiate executive performance based on the ratings and bonuses and allocate pay adjustment amounts for its senior executives, with executives who are placed in the highest tier (I) receiving a larger percentage pay adjustment than executives in a lower tier (V) who received the annual percentage adjustment to the EX pay schedule, which was 2.5 percent in 2008.

DOE sets prescribed ranges tied to performance ratings prior to finalizing ratings to help create a greater distinction between bonus amounts for the top and middle performers and differentiate pay adjustment caps. Specifically, for fiscal year 2007, DOE required that all executives receiving an outstanding rating receive a bonus of 12 to 20 percent of base pay, while executives receiving a meets expectations rating were eligible to receive a bonus of 5 to 9 percent, but at management’s discretion. For pay adjustments, executives were eligible to receive a discretionary increase of up to 5 or 7 percent of basic pay if rated at meets expectations

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or outstanding, respectively. Executives who receive the other two rating levels—needs improvement or unsatisfactory—cannot receive any bonuses or pay increases.<sup>6</sup>

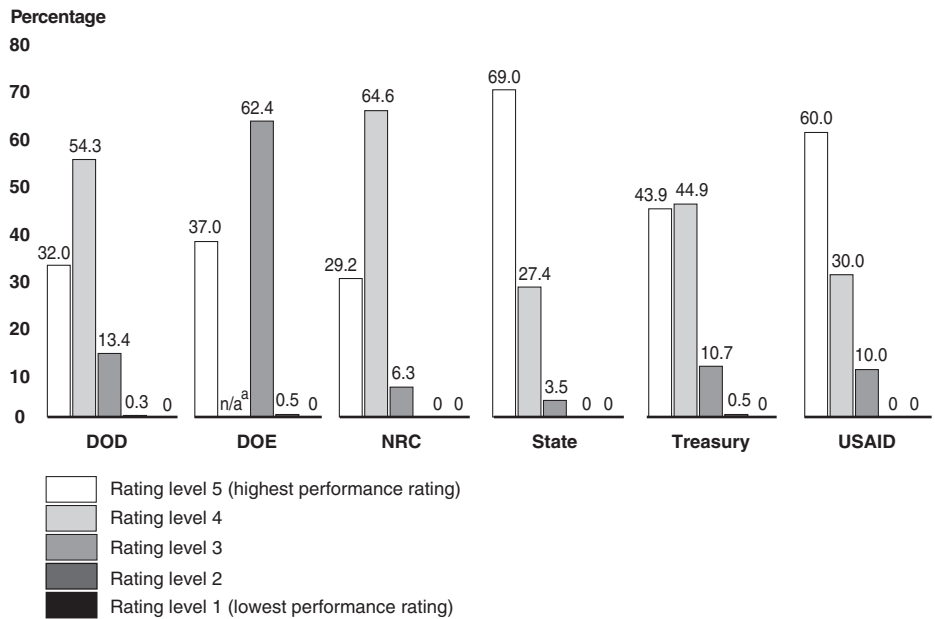
We have reported that using multiple rating levels provides a useful framework for making distinctions in performance by allowing an agency to differentiate among individuals' performance.<sup>7</sup> All of the selected agencies have four or five rating levels in place for assessing senior executive performance. While the selected agencies designed their appraisal and pay systems to help make meaningful distinctions in performance through ratings, our analysis shows that the senior executives were concentrated at the top two rating levels for the most recently completed appraisal cycle, as shown in figure 1. At State and USAID, about 69 percent and 60 percent of senior executives, respectively, received the top performance rating. At the other four agencies, the largest percentage of executives received the second highest rating—ranging from about 65 percent at NRC to 45 percent at Treasury. Conversely, less than 1 percent of senior executives across the selected agencies received a rating below fully successful (level 3). As a point of comparison, about 43 percent of career SES governmentwide received the top performance rating for fiscal year 2006, the most recent governmentwide data available as reported by OPM. Similar to the selected agencies, less than 1 percent of career SES governmentwide received a rating below fully successful in fiscal year 2006.

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<sup>6</sup>DOE uses a four-level appraisal system with no rating level between outstanding and meets expectations.

<sup>7</sup>GAO, *Financial Regulators: Agencies Have Implemented Key Performance Management Practices, but Opportunities for Improvement Exist*, [GAO-07-678](#) (Washington, D.C.: June 18, 2007).

**Figure 1: Percentage of Senior Executives by Rating Level at the Selected Agencies for the Fiscal Year 2007 Appraisal Cycle**



Source: GAO analysis of agency data.

Note: The percentages may not total 100 percent due to rounding.

<sup>a</sup>DOE uses a four-level appraisal system with no rating level between outstanding (rating level 5) and meets expectations (rating level 3).

According to State’s Deputy Assistant Secretary for the Bureau of Human Resources, historically, the vast majority of senior executives have received the highest rating of outstanding, including for fiscal year 2007. Since the implementation of performance-based pay, this official said State has struggled with changing the culture and general perception among senior executives that any rating less than outstanding is a failure. DOD is communicating the message that a fully successful or equivalent rating is a valued and quality rating to help change its culture and make more meaningful distinctions in ratings. Part of this communication is developing common benchmark descriptors for the performance elements at the five, four, and three rating levels. The Principal Deputy Under Secretary of Defense for Civilian Personnel Policy said she hopes that developing common definitions for the performance elements at all three levels will aid the development of a common understanding and in turn make more meaningful distinctions in ratings. The agency official recognizes that this shift to giving fully successful ratings is a significant cultural change and it will take some time to fully transform the culture.

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The percentage of eligible executives that received bonuses or pay adjustments varied across the selected agencies for fiscal year 2007, as shown in table 2. The percentage of eligible senior executives that received bonuses ranged from about 92 percent at DOD to about 30 percent at USAID, with the average dollar amount ranging from \$11,034 at State to about \$17,917 at NRC. For pay adjustments, all eligible executives at State received pay adjustments, while about 88 percent of eligible executives at DOE received adjustments, with the average dollar amount ranging from about \$5,414 at NRC to about \$6,243 at DOE. As a point of comparison, about 67 percent of career SES members received bonuses with an average dollar amount of \$13,292 for fiscal year 2006, according to governmentwide data reported by OPM. The governmentwide percentage of career SES receiving pay adjustments and average dollar amount of the adjustments in the aggregate are not available from OPM's governmentwide data report for fiscal year 2006.

The selected agencies have policies in place where only senior executives who receive a rating of fully successful (level 3) or higher are eligible to receive bonuses or pay increases. Also affecting executives' bonus eligibility are the agencies' policies on awarding bonuses to executives who also received Presidential Rank Awards that year, which varied among the selected agencies.<sup>8</sup> NRC, State, and Treasury do not allow executives to receive both awards in the same year, while DOD, DOE, and USAID allow the practice.

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<sup>8</sup>Agencies can nominate senior executives for Presidential Rank Awards, which recognize career senior executives who have demonstrated exceptional performance over an extended period of time. The OPM Director reviews agency nominations and recommends candidates to the President. These awards are either 20 percent or 35 percent of the recipient's base pay.

**Table 2: Percentage of Eligible Senior Executives Who Received Bonuses or Pay Adjustments and the Average Amounts at the Selected Agencies for the Fiscal Year 2007 Appraisal Cycle**

Agency	Bonuses		Pay adjustments	
	Percentage who received bonuses	Average amount	Percentage who received pay adjustments	Average amount
DOD	92	\$13,934	95	\$5,739
DOE	82	14,116	88	6,243
NRC	87	17,917	95	5,414
State	55	11,034	100	6,148
Treasury	77	16,074	93	6,120
USAID	30	11,083	90	6,227

Source: GAO analysis of agency data.

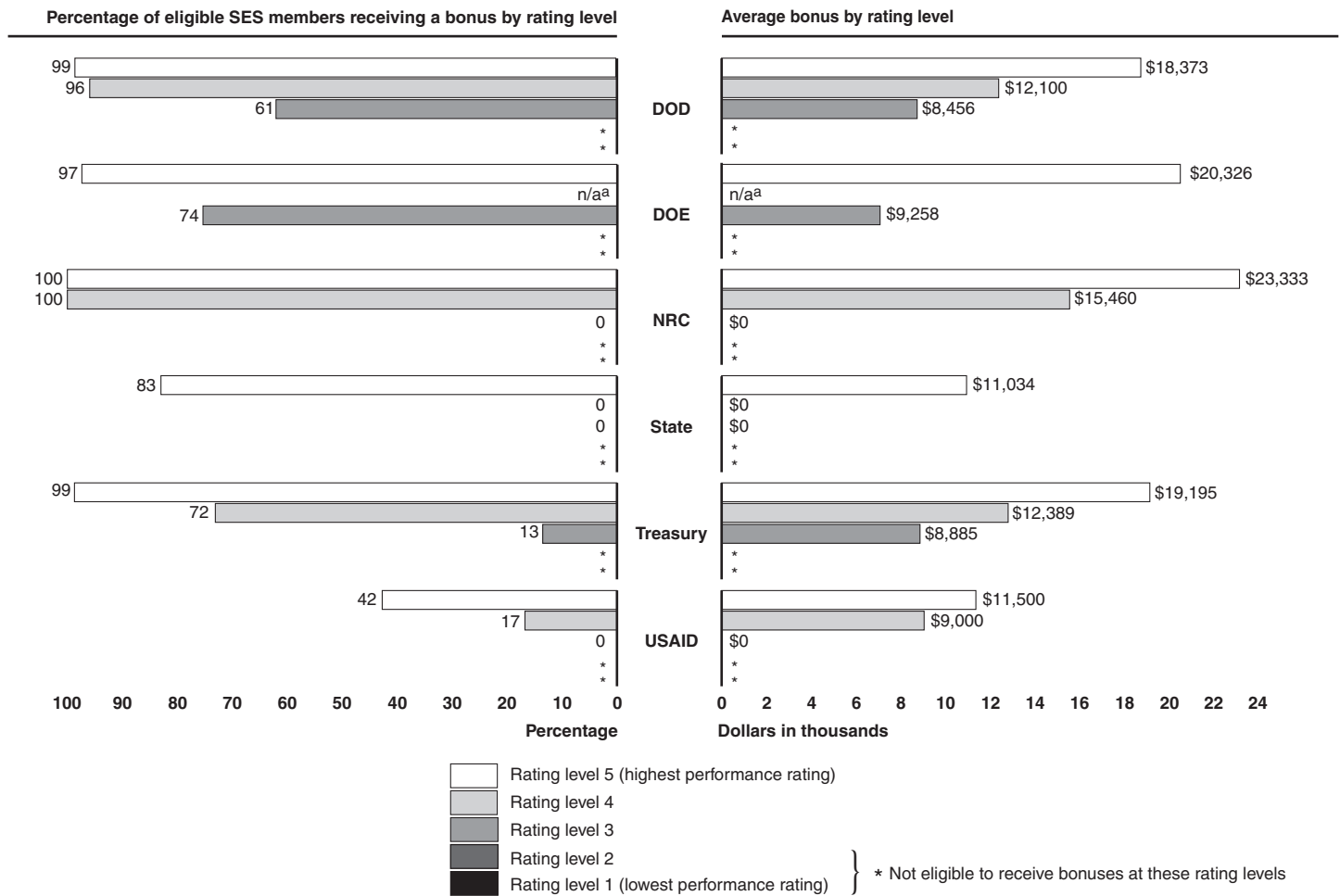
Notes: In calculating the percentage of eligible senior executives who received bonuses or pay adjustments and average amounts, we excluded executives who received a rating less than fully successful since those executives are not eligible to receive bonuses or pay increases, according to the selected agencies' policies. We also excluded SES members at NRC, State, and Treasury who received Presidential Rank Awards because according to the agencies' policies, those individuals were not considered for bonuses. For all agencies, we included senior executives who were rated but left their positions—because of retirement, attrition, or assignment to a lower grade—prior to performance payouts being made.

According to OPM regulations, agencies are to reward the highest-performing executives with the highest ratings and largest bonuses and pay adjustments.<sup>9</sup> At almost all of the agencies, the highest-performing executives (rated at level 5) made up the greatest percentage of eligible executives receiving bonuses, with the exception of NRC where all the eligible executives rated at the top two levels received a bonus. Similarly, the executives rated at the highest level received the largest bonuses on average—about \$23,333 at NRC compared to about \$11,034 at State. State only awarded bonuses to executives receiving the top rating of outstanding for fiscal year 2007. In addition, senior executives at NRC and USAID rated at fully successful (level 3) did not receive bonuses. (See fig. 2.)

<sup>9</sup>5 CFR § 430.404(a)(9).



**Figure 2: Percentage of Eligible Senior Executives Who Received Bonuses and the Average Bonus Amounts by Rating Level at the Selected Agencies for the Fiscal Year 2007 Appraisal Cycle**



Source: GAO analysis of agency data.

Notes: In calculating the percentage of eligible senior executives who received bonuses and average amounts, we excluded executives who received a rating less than fully successful since those executives are not eligible to receive bonuses, according to the selected agencies' policies. We also excluded SES members at NRC, State, and Treasury who received Presidential Rank Awards because according to the agencies' policies, those individuals were not considered for bonuses. For all agencies, we included senior executives who were rated but left their positions—because of retirement, attrition, or assignment to a lower grade—prior to performance payouts being made.

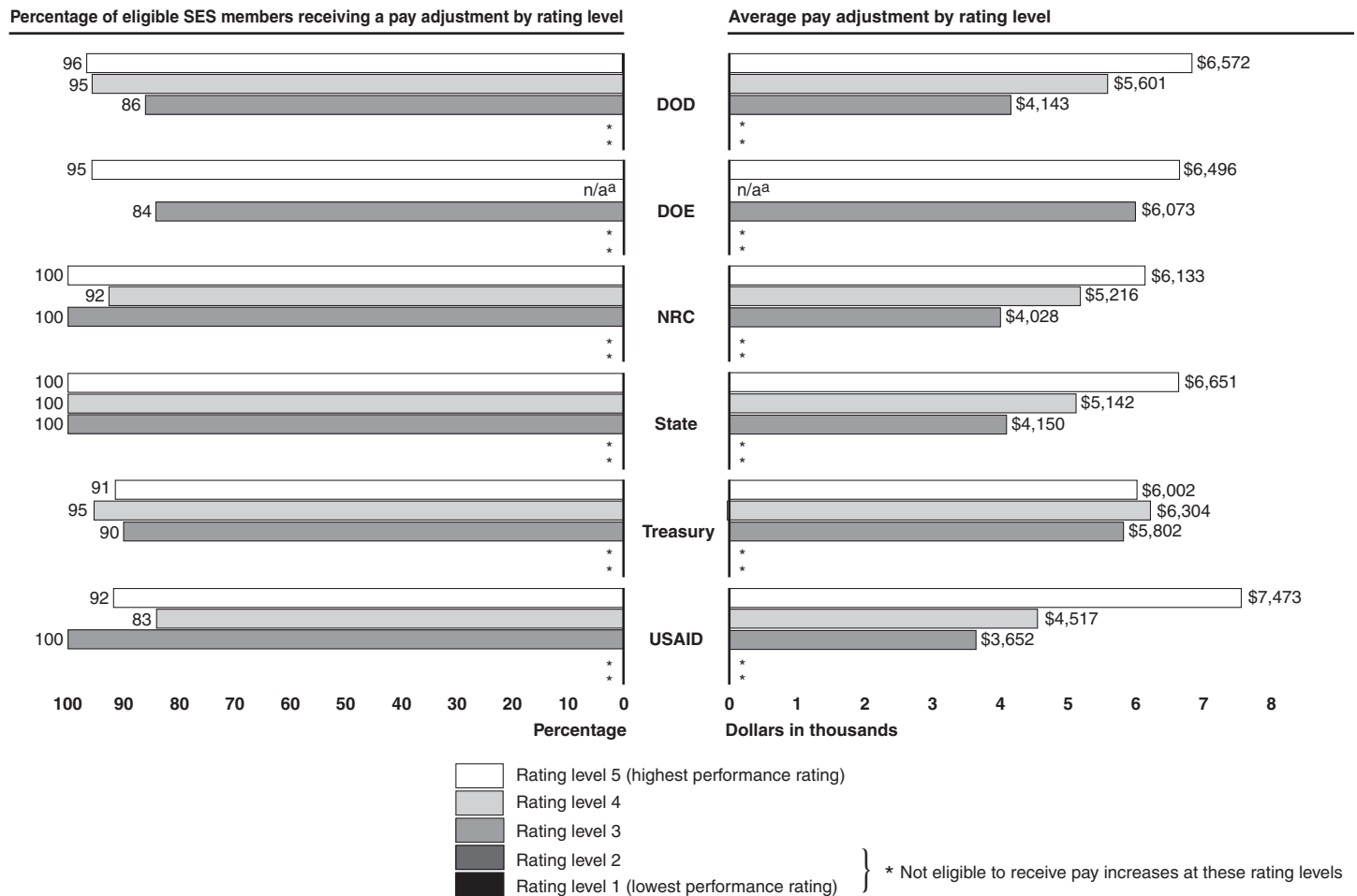
<sup>a</sup>DOE uses a four-level appraisal system with no rating level between outstanding (rating level 5) and meets expectations (rating level 3).

In a memo to agencies on the certification process, OPM stated that senior executives who receive a fully successful or higher rating and are

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paid at a level consistent with their current responsibilities should receive a pay increase. According to an OPM official, agencies are not required to give these executives pay increases, but OPM considers fully successful to be a good rating and encourages agencies to recognize and reward executives performing at this rating level. At the selected agencies, the majority of eligible senior executives rated at fully successful received pay adjustments for fiscal year 2007, as shown in figure 3. Unlike the bonus distributions by rating level, at some of the agencies, the highest-performing executives who received a rating of level 5 did not make up the greatest percentage of executives receiving pay adjustments with the largest increases on average. For example, at USAID, all eligible executives who received a level 3 rating received a pay adjustment, while about 92 percent of eligible executives rated at level 5 received an adjustment. For all the agencies except Treasury, the executives rated at the highest level received the largest pay adjustments on average—about \$7,473 at USAID compared to about \$6,133 at NRC. At Treasury, executives rated at levels five, four, and three on average received about the same pay adjustment amounts primarily due to pay cap issues.

**Figure 3: Percentage of Eligible Senior Executives Who Received Pay Adjustments and the Average Pay Adjustment Amount by Rating Level at the Selected Agencies for the Fiscal Year 2007 Appraisal Cycle**



Source: GAO analysis of agency data.

Notes: In calculating the percentage of eligible senior executives who received pay adjustments and average amounts, we excluded executives who received a rating less than fully successful since those executives are not eligible to receive pay increases, according to the selected agencies' policies. For all agencies, we included senior executives who were rated but left their positions—because of retirement, attrition, or assignment to a lower grade—prior to performance payouts being made.

<sup>a</sup>DOE uses a four-level appraisal system with no rating level between outstanding (rating level 5) and meets expectations (rating level 3).

The governmentwide results of the 2008 OPM SES survey show that the majority of senior executives responded that their bonus or salary increase was linked to their performance rating to a very great or great

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extent. However, less than a third of senior executives strongly agreed or agreed that bonus amounts or pay distinctions were meaningfully different among the executives. These results show that making meaningful distinctions in bonuses and pay can be a challenge.

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## Building Safeguards into Senior Executive Performance Appraisal and Pay Systems

We have reported that agencies need to have modern, effective, credible, and, as appropriate, validated performance management systems in place with adequate safeguards to ensure fairness and prevent politicization and abuse.<sup>10</sup> All of the selected agencies have built safeguards into their senior executive performance appraisal and pay systems—such as predecisional checks of performance appraisal recommendations through higher-level reviews and PRBs as well as transparency in communicating the aggregate results—to help enhance the credibility, fairness, and transparency of their systems, although they varied in how the safeguards have been implemented. Our preliminary results show that there are opportunities for improvement in the communication of aggregate appraisal results to all senior executives.

By law, as part of their SES appraisal systems, all agencies must provide their senior executives with an opportunity to view their appraisals and ratings and to request a review of the recommended performance ratings by higher-level officials, before the ratings become final.<sup>11</sup> The higher-level reviewer cannot change the initial summary rating given by the supervisor, but may recommend a different rating in writing to the PRB that is shared with the senior executive and the supervisor. For example, according to State's policy, an executive may request a higher-level review of the initial rating in writing prior to the PRB convening at which time the initial summary rating, the executive's request, and the higher-level reviewing official's written findings and recommendations are considered. The PRB is to provide a written recommendation on the executive's summary rating to State's Director General of the Foreign Service and Director of Human Resources, who makes the final appraisal decisions.

Further, all agencies must establish one or more PRBs to help ensure that performance appraisals reflect both individual and organizational

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<sup>10</sup>GAO-05-832SP. For more information including the complete list of safeguards, see GAO, *Defense Transformation: Preliminary Observations on DOD's Proposed Civilian Personnel Reforms*, GAO-03-717T (Washington, D.C.: Apr. 29, 2003).

<sup>11</sup>5 USC § 4312(b)(3).

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performance and that rating, bonus, and pay adjustment recommendations are consistently made. The PRB is to review senior executives' initial summary performance ratings and other relevant documents and make written recommendations on the performance of the senior executives to the agency head or appointing authority.

The selected agencies varied in their PRB structures and in who provided the final approval of the appraisal decisions. For example, given its small number of senior executives, USAID has one PRB that is responsible for making recommendations to the Administrator for his/her final approval on all rated career executives for their annual summary ratings, bonuses, performance-based pay adjustments, and Presidential Rank Award nominations. On the other hand, DOD has multiple PRBs within and across its components and agencies with separate authorizing officials who give the final approval of rating and performance payout recommendations. According to a DOD official, there is not a central PRB that oversees all the PRBs within the department responsible for recommending approval of the final appraisal decisions for all senior executives. To help ensure consistency in appraisal recommendations across the department and between the various authorizing officials, the components are to provide their final rating and performance payout distributions to the Under Secretary of Defense for Personnel and Readiness to be validated prior to executives receiving the bonuses and pay adjustments. As part of the validation process, the Under Secretary of Defense for Personnel and Readiness checks to ensure that meaningful distinctions were made and ratings, bonuses, and pay adjustments reflect organizational and individual performance, among other things, before performance bonuses and pay increases are made effective.

To help enhance the transparency of the system, agencies can communicate the overall aggregate results of the performance appraisal decisions—ratings, bonuses, and pay adjustment distributions—to senior executives while protecting individual confidentiality, and as a result, let executives know where they stand in the organization. Further, OPM has recognized the importance of communicating the overall rating distributions and performance payout averages through its guidance for certifying agencies' SES systems, and factors it into certification decisions. OPM asks agencies to brief their SES members on the results of the completed appraisal process to make sure that the dynamics of the general distribution of ratings and accompanying rewards are fully understood. The results of the OPM survey of senior executives show that the communication of overall performance appraisal results is not widely practiced throughout the government. Specifically, 65 percent of

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respondents said that they were not given a summary of their agency's SES performance ratings, bonuses, and pay adjustments.

The selected agencies communicated the aggregate results in varying ways. For example, Treasury and DOD posted the aggregate rating, bonus, and pay adjustment distributions for senior executives on their Web sites with comparison of data across previous fiscal years. In communicating the results of the most recent appraisal cycle, NRC sent an e-mail to all senior executives sharing the percentage of executives at each rating level and the percentages receiving bonuses and pay adjustments as well as the average dollar amounts. According to an NRC official, the agency periodically holds agencywide "all hands" SES meetings where the results of the appraisal cycle, among other topics, are communicated to executives.

Similarly, the Deputy Secretary of DOE provides a memo to all senior executives summarizing the percentage of executives at the top two rating levels and the average bonus and pay adjustment amounts. DOE also includes governmentwide results as reported by OPM as a point of comparison. Further, in that memo, the Deputy Secretary stated his concern with the negligible difference in bonuses and pay adjustments among executives receiving the top two rating levels and stressed the importance of making meaningful distinctions in the allocation of compensation tied to performance ratings in the upcoming appraisal cycle.

While USAID shares an individual's appraisal results with that executive, agency officials said that they do not communicate aggregate results to all senior executives. Communicating an executive's individual rating conveys information about how well the executive has performed against the expectations in the performance plan, but is not sufficient to provide a clear picture of how the executive's performance compares with that of other executives in the agency. Further, USAID communicated to all SES members the pay adjustment distributions in ranges by rating level, but not the aggregate results showing the percentage of executives receiving the pay adjustments in total or by rating level. There are opportunities for further refinements in how the aggregate appraisal results are communicated to all senior executives.

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Mr. Chairman, Senator Voinovich, and Members of the Subcommittee, this completes my prepared statement. I would be pleased to respond to any questions that you may have.

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## Contacts and Acknowledgments

For further information regarding this statement, please contact J. Christopher Mihm, Managing Director, Strategic Issues, at (202) 512-6806 or [mihmj@gao.gov](mailto:mihmj@gao.gov) or Robert N. Goldenkoff, Director, Strategic Issues, at (202) 512-6806 or [goldenkoffr@gao.gov](mailto:goldenkoffr@gao.gov). Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this testimony. Individuals making key contributions to this statement include Belva Martin, Assistant Director; Amber Edwards; Janice Latimer; Meredith Moore; Mary Robison; Sabrina Streagle; and Greg Wilmoth.

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# Appendix I: Background on the Senior Executive Performance-Based Pay System and Certification Criteria

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In November 2003, Congress authorized a new performance-based pay system for members of the Senior Executive Service (SES).<sup>1</sup> With the performance-based pay system, senior executives are to no longer receive annual across-the-board or locality pay adjustments. Agencies are to base pay adjustments for senior executives on individual performance and contributions to the agency's performance by considering the individual's accomplishments and such things as unique skills, qualifications, or competencies of the individual and the individual's significance to the agency's mission and performance, as well as the individual's current responsibilities. The system, which took effect in January 2004, also replaced the six SES pay levels with a single, open-range pay band and raised the cap on base pay and total compensation. For 2008, the caps are \$158,500 for base pay (Level III of the Executive Schedule) with a senior executive's total compensation not to exceed \$191,300 (Level I of the Executive Schedule). If an agency's senior executive performance appraisal system is certified by the Office of Personnel Management (OPM) and the Office of Management and Budget (OMB) concurs, the caps are increased to \$172,200 for base pay (Level II of the Executive Schedule) and \$221,100 for total compensation (the total annual compensation payable to the Vice President).

To qualify for senior executive pay flexibilities, agencies' performance appraisal systems are evaluated against nine certification criteria and any additional information that OPM and OMB may require to make determinations regarding certification. As shown in table 3, the certification criteria jointly developed by OPM and OMB are broad principles that position agencies to use their pay systems strategically to support the development of a stronger performance culture and the attainment of the agency's mission, goals, and objectives.

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<sup>1</sup>National Defense Authorization Act for Fiscal Year 2004, Pub. L. No. 108-136, November 24, 2003; 5 USC § 5382.



**Appendix I: Background on the Senior  
Executive Performance-Based Pay System and  
Certification Criteria**

**Table 3: Senior Executive Performance Appraisal System Certification Criteria**

<b>Criterion</b>	<b>Description</b>
Alignment	Individual performance expectations must be linked to or derived from the agency's mission, strategic goals, program/policy objectives, or annual performance plan.
Consultation	Individual performance expectations are developed with senior employee involvement and must be communicated at the beginning of the appraisal cycle.
Results	Individual expectations describe performance that is measurable, demonstrable, or observable, focusing on organizational outputs and outcomes, policy/program objectives, milestones, and so forth.
Balance	Individual performance expectations must include measures of results, employee and customer/stakeholder satisfaction, or competencies or behaviors that contribute to outstanding performance.
Assessments and guidelines	The agency head or a designee provides assessments of the performance of the agency overall, as well as each of its major program and functional areas, such as reports of agency's goals and other program performance measures and indicators, and evaluation guidelines based, in part, upon those assessments to senior employees and appropriate senior employee rating and reviewing officials. The guidance provided may not take the form of quantitative limitations on the number of ratings at any given rating level.
Oversight	The agency head or designee must certify that (1) the appraisal process makes meaningful distinctions based on relative performance; (2) results take into account, as appropriate, the agency's performance; and (3) pay adjustments and awards recognize individual/organizational performance.
Accountability	Senior employee ratings (as well as subordinate employees' performance expectations and ratings for those with supervisor responsibilities) appropriately reflect employees' performance expectations, relevant program performance measures, and other relevant factors.
Performance differentiation	Among other provisions, the agency must provide for at least one rating level above fully successful (must include an outstanding level of performance), and in the application of those ratings, must make meaningful distinctions among executives based on their relative performance.
Pay differentiation	The agency should be able to demonstrate that the largest pay adjustments, highest pay levels (base and performance awards), or both are provided to its highest performers, and that overall the distribution of pay rates in the SES rate range and pay adjustments reflects meaningful distinctions among executives based on their relative performance.

Source: GAO.

# Appendix II: Highlights of Selected GAO Products



Highlights of GAO-07-90, a report to congressional requesters

## Why GAO Did This Study

As the agency responsible for the federal government's human capital initiatives, the Office of Personnel Management (OPM) must have the capacity to successfully guide human capital transformations necessary to meet the governance challenges of the 21<sup>st</sup> century. Given this key role, GAO was asked to assess OPM's capacity to lead further reforms. In June 2006, GAO testified on several management challenges that OPM faces. This report—the second in a series—supplements that testimony and, using the new senior executive performance-based pay system as a model for understanding OPM's capacity to lead and implement reform, identifies lessons learned that can inform future reforms. GAO analyzed relevant laws and documents, and obtained views from the Chief Human Capital Officers (CHCO) Council and human resource directors, the Office of Management and Budget (OMB) staff, and OPM officials.

## What GAO Recommends

GAO is making recommendations to the Director of OPM to improve OPM's capacity for future reforms by reexamining agencywide skills, and to address issues specific to the senior executives' pay systems, such as sharing best practices and tracking progress towards goals. In commenting on a draft of this report, OPM stated it has made progress toward achieving its operational and strategic goals, but neither agreed nor disagreed with GAO's recommendations.

[www.gao.gov/cgi-bin/getrpt?GAO-07-90](http://www.gao.gov/cgi-bin/getrpt?GAO-07-90).

To view the full product, including the scope and methodology, click on the link above. For more information, contact Brenda S. Farrell at (202) 512-6806 or [farrellb@gao.gov](mailto:farrellb@gao.gov).

January 2007

## OFFICE OF PERSONNEL MANAGEMENT

### Key Lessons Learned to Date for Strengthening Capacity to Lead and Implement Human Capital Reforms

#### What GAO Found

The congressionally authorized senior executive performance-based pay system, implemented in 2004, provides an opportunity to learn from experiences gained and apply those lessons to the design and implementation of future human capital reforms. Under the performance-based system, before an agency can receive the new pay flexibilities, OPM, with concurrence from OMB, must certify that the agency's appraisal system meets certain criteria. OPM is likely to play a similar leadership and oversight role for future reforms.

#### Lessons Learned from the Performance-based System and Other Human Capital Initiatives

<b>Ensure internal OPM capacity to lead and implement reform</b>	Executive branch agencies noted a lack of knowledge and experience among OPM staff to design and implement key human capital transformation efforts. GAO analysis of available OPM employee feedback data suggests that employees may not be receiving sufficient training to enhance their skills and competencies. OPM has begun aligning its workforce skills to meet future needs but has not conducted an agencywide skills assessment since updating its key strategic management documents. <b>Lesson:</b> Ensure that OPM's workforce is properly aligned to successfully design and implement human capital reforms, such as knowledge of innovative classification and pay and compensation approaches, and continue to prepare the workforce to meet changing demands of the future.
<b>Ensure that executive branch agencies' infrastructures support reform</b>	OPM's approach to certifying agencies' senior executive performance-based systems should more fully promote the building of the institutional infrastructure, such as robust performance management systems with adequate safeguards, within agencies needed to effectively implement the reforms. <b>Lesson:</b> Assist agencies in building the necessary infrastructure for a performance-based system by providing front-end and ongoing involvement—building on progress made to date.
<b>Collaborate with CHCO Council</b>	Executive branch agencies said the certification process was a missed opportunity for OPM to better collaborate with the CHCO Council. One agency CHCO said OPM traditionally uses council meetings to present information to the CHCOs, but does not always encourage discussions or seek input. <b>Lesson:</b> Cultivate effective partnerships with the CHCO Council by engaging them to solicit their ideas and suggestions during system design to build consensus and develop momentum for success.
<b>Develop clear and timely guidance</b>	The lack of clear and timely guidance from OPM created confusion as agencies attempted to understand and implement the broadly defined regulatory criteria for certification. <b>Lesson:</b> Provide agencies with clear and timely guidance—being sensitive to other ongoing human capital activities—to reach a common, consistent understanding and promote efficiency as agencies adjust to new requirements for reforms.
<b>Share best practices</b>	Executive branch agencies said OPM could have better facilitated sharing best practices to help them implement senior executive performance-based systems. <b>Lesson:</b> Facilitate the sharing of best practices for implementing human capital reforms by providing forums for agencies to learn from each others' experiences, share successful strategies, and avoid common pitfalls.
<b>Solicit and incorporate feedback</b>	Executive branch agencies said there was no formal mechanism, such as a customer survey, for them to provide feedback to OPM on its guidance and assistance. <b>Lesson:</b> Solicit feedback from executive branch agencies and incorporate to improve the implementation of human capital reforms.
<b>Track progress to ensure accountability</b>	OPM does not have an evaluation strategy for tracking the progress of the agencies' implementation of the new executive systems. <b>Lesson:</b> Develop a strategy to allow OPM, other federal agencies, and Congress to monitor progress toward achieving human capital reform goals.

Source: GAO analysis.

United States Government Accountability Office

September 26, 2006



Highlights of GAO-06-1125T, testimony before the Subcommittee on Oversight of Government Management, the Federal Workforce and the District of Columbia, Committee on Homeland Security and Governmental Affairs, U.S. Senate

### Why GAO Did This Study

The government's senior executives need to lead the way in transforming their agencies' cultures. Credible performance management systems—those that align individual, team, and unit performance with organizational results—can help manage and direct this process. In past work, GAO found that the performance management systems for senior executives fell short in this regard. In November 2003, recognizing that reforms were needed, Congress authorized a new performance-based pay system that ended the practice of giving annual pay adjustments to senior executives. Instead, agencies are to consider such factors as individual results and contributions to agency performance. If the Office of Personnel Management (OPM) certifies an agency's new performance system and the Office of Management and Budget (OMB) concurs, the agency has the flexibility to raise the pay of its highest performing senior executives above certain pay caps.

This testimony addresses (1) the performance management system's regulatory structure, (2) OPM's certification process and agencies' views of it, and (3) OPM's role in monitoring the system, and the number of agencies that have been certified to date. This statement is based on GAO's issued work, which included interviews with senior OPM officials, agency Chief Human Capital Officers and Human Resource officers, and reviews of agency documents.

[www.gao.gov/cgi-bin/getrpt?GAO-06-1125T](http://www.gao.gov/cgi-bin/getrpt?GAO-06-1125T).

To view the full product, including the scope and methodology, click on the link above. For more information, contact Brenda S. Farrell at (202) 512-3604 or [farrelb@gao.gov](mailto:farrelb@gao.gov).

## HUMAN CAPITAL

### Aligning Senior Executives' Performance with Organizational Results Is an Important Step Toward Governmentwide Transformation

#### What GAO Found

Overall, the regulations that OPM and OMB developed to administer a performance-based pay system for executives serve as an important step for agencies in creating an alignment or "line of sight" between executives' performance and organizational results. To qualify for the pay flexibilities included in the statute, OPM must certify and OMB must concur that an agency's performance management system meets nine certification criteria, including demonstrating that its performance management system aligns individual performance expectations with the mission and goals of the organization and that its system as designed and applied makes meaningful distinctions in performance. The certification criteria are generally consistent with key practices for effective performance management systems GAO identified that collectively create a line of sight between an individual's performance and an organization's success. To receive a full 2-calendar-year certification, an agency must document that its senior executive performance management system meets all nine of the criteria. Agencies can meet four of nine criteria and demonstrate that their system in design meets the remaining certification criteria to receive 1-year provisional certification and use the higher pay rates.

Two divisions in OPM, as well as OMB, independently review agencies' certification submissions. A number of agencies GAO contacted expressed concern over OPM's ability to communicate expectations, guidance, and deadlines to agencies in a clear and consistent manner. OPM officials agreed that agencies need better guidance and were working on improvements.

In monitoring agencies' performance management systems, OPM can suspend an agency's certification at any time with OMB concurrence if an agency is not complying with the certification criteria. According to OPM data, performance management systems at 24 agencies were certified during calendar year 2006. Of these, only the Department of Labor's system received full certification; the remaining systems received only provisional certification. These findings are not surprising. As GAO has noted in its past work, agencies could find it initially difficult to provide the necessary performance data to receive full certification. Going forward, it will be important for OPM to continue to monitor the certification process to help ensure that provisional certifications do not become the norm, and agencies develop performance management systems for their senior executives that meet all of OPM's requirements.

The new performance management system for the government's senior executives will help agencies align individual, team, and unit performance with organizational results. Although there have been some implementation challenges, what will be important is how OPM works with agencies to meet the certification criteria. Moreover, the lessons learned in implementing the senior executive performance management system can be applied to modernizing the performance management systems of employees at other levels.

United States Government Accountability Office



Highlights of GAO-06-708, a report to the Chairman, Subcommittee on the Federal Workforce and Agency Organization, Committee on Government Reform, House of Representatives

### Why GAO Did This Study

Critical to the success of the federal government's transformation are its people—human capital. Yet, the government has not transformed, in many cases, how it classifies, compensates, develops, and motivates its employees to achieve maximum results within available resources and existing authorities. GAO has reported that the federal government as a whole may face challenges in offering competitive compensation to its senior leaders who have reached a statutory pay cap.

As requested, GAO (1) provided trend data for basic pay rates of selected federal executive and judicial pay plans from 1970 to 2006, (2) identified elements of total compensation for the selected pay plans in 2006, and (3) identified principles for any possible restructuring of these pay plans. We selected 1970 as a baseline because salary increases went into effect in 1969 for executive-level positions as recommended by the Commission on Executive, Legislative, and Judicial Salaries. The pay plans cover the following—career Senior Executive Service (SES), administrative law judges (ALJ), senior-level (SL), Executive Schedule (EX), scientific or professional (ST), and members of Boards of Contract Appeals (BCA), as well as federal justices and judges—the Chief Justice, associate justices, circuit judges, district judges, and judges of the U.S. Court of International Trade.

[www.gao.gov/cgi-bin/getrpt?GAO-06-708](http://www.gao.gov/cgi-bin/getrpt?GAO-06-708)

To view the full product, including the scope and methodology, click on the link above. For more information, contact Lisa Shames at (202) 512-6806 or [shamesl@gao.gov](mailto:shamesl@gao.gov).

June 2006

## HUMAN CAPITAL

### Trends in Executive and Judicial Pay

#### What GAO Found

The basic pay rates for all of the selected federal pay plans increased in nominal dollars from 1970 to 2006. However, when adjusted for inflation to 2006 dollars using the Gross Domestic Product price deflator, the pay rates for those under the EX pay plan and the federal justices and judges decreased and the pay rates for the SES, SL/ST, and ALJ positions increased. For example, in 1970, cabinet secretaries were paid \$250,204 (in 2006 dollars) compared to \$183,500 in 2006. Their pay actually declined in value by about 27 percent during this period. In 1970, ALJs were paid \$148,058 (in 2006 dollars) compared to \$152,000 in 2006. Their pay increased in value by 3 percent during this period. In comparison, when adjusted for inflation to 2006 dollars using the Consumer Price Index, the pay rates for all of the selected pay plans decreased. For example, pay actually declined in value for cabinet secretaries and ALJs by 41 percent and 17 percent, respectively.

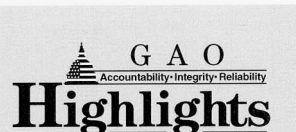
The elements of total compensation vary among the selected pay plans. For example, SES and SL/ST positions may receive cash awards/bonuses, while, at present, selected EX positions, ALJs, BCA positions, and federal justices and judges do not due to the nature of the positions. All of the positions within the selected pay plans may receive noncash or deferred benefits, such as health and life insurance, retirement, and access to child care facilities. However, there are differences in retirement, such as larger benefits, for federal justices and judges compared to other executive-level positions.

Regarding any possible restructuring of these pay plans, certain principles should be considered to attract and retain the executive leadership necessary to address 21st century challenges. The pay plans should be

- sensitive to hiring and retention trends;
- reflective of responsibilities, knowledge and skills, and contributions;
- transparent;
- market-sensitive;
- flexible to economic change;
- sustainable; and
- competitive.

Going forward, there are several illustrative issues that deserve further reconsideration—maintaining a reasonable relationship in total compensation across executive-level positions; recognizing equity issues in the basic pay rates within the same position, such as inspectors general; considering performance-based bonuses with appropriate safeguards for positions that do not receive them including selected EX positions, ALJs, BCA positions, and federal justices and judges; and recognizing anomalies between comparable pay plans, such as SES and SL/ST, in terms of basic pay caps, as well as aggregate pay (basic pay plus cash awards/bonuses).

United States Government Accountability Office



**Highlights**

Highlights of GAO-05-1048T, a testimony before the Subcommittee on Oversight of Government Management, the Federal Workforce, and the District of Columbia, Committee on Homeland Security and Governmental Affairs, U.S. Senate

**Why GAO Did This Study**

The federal government must have the capacity to plan more strategically, react more expeditiously, and focus on achieving results. Critical to the success of this transformation are the federal government's people—its human capital. Yet, in many cases the federal government has not transformed how it classifies, compensates, develops, and motivates its employees to achieve maximum results within available resources and existing authorities. A key question is how to update the federal government's compensation system to be market-based and more performance-oriented.

To further the discussion of federal pay reform, GAO partnered with key human capital stakeholders to convene a symposium in March 2005 to discuss public, private, and nonprofit organizations' successes and challenges in designing and managing market-based and more performance-oriented pay systems.

This testimony presents the strategies that organizations considered in designing and managing market-based and more performance-oriented pay systems and describes how they are implementing them.

[www.gao.gov/cgi-bin/getrpt?GAO-05-1048T](http://www.gao.gov/cgi-bin/getrpt?GAO-05-1048T)

To view the full product, including the scope and methodology, click on the link above. For more information, contact Lisa Shames at (202) 512-6806 or [shamesl@gao.gov](mailto:shamesl@gao.gov).

September 27, 2005

## HUMAN CAPITAL

### Designing and Managing Market-Based and More Performance-Oriented Pay Systems

#### What GAO Found

GAO strongly supports the need to expand pay reform in the federal government. While implementing market-based and more performance-oriented pay systems is both doable and desirable, organizations' experiences in designing and managing their pay systems underscored three key themes that can guide federal agencies' efforts.

- The shift to market-based and more performance-oriented pay must be part of a broader strategy of change management and performance improvement initiatives.
- Market-based and more performance-oriented pay cannot be simply overlaid on most organizations' existing performance management systems. Rather, as a precondition to effective pay reform, individual expectations must be clearly aligned with organizational results, communication on individual contributions to annual goals must be ongoing and two-way, meaningful distinctions in employee performance must be made, and cultural changes must be undertaken.
- Organizations need to build up the basic management capacity of their organizations. Training and developing new and current staff to fill new roles and work in different ways will play a crucial part in building the capacity of the organizations.

Organizations presenting at our symposium considered the following strategies in designing and managing their pay systems.

1. Focus on a set of values and objectives to guide the pay system.
2. Examine the value of employees' total compensation to remain competitive in the market.
3. Build in safeguards to enhance the transparency and help ensure the fairness of pay decisions.
4. Devolve decision making on pay to appropriate levels.
5. Provide training on leadership, management, and interpersonal skills to facilitate effective communication.
6. Build consensus to gain ownership and acceptance for pay reforms.
7. Monitor and refine the implementation of the pay system.

Moving forward, it is possible to enact broad-based reforms that would enable agencies to move to market-based and more performance-oriented pay systems. However, before implementing reform, each executive branch agency should demonstrate and the Office of Personnel Management should certify that the agency has the institutional infrastructure in place to help ensure that the pay reform is effectively and equally implemented. At a minimum, this infrastructure includes a modern, effective, credible, and validated performance management system in place that provides a clear linkage between institutional, unit, and individual performance-oriented outcomes; results in meaningful distinctions in ratings; and incorporates adequate safeguards.

United States Government Accountability Office



Highlights of GAO-04-614, a report to congressional requesters

May 2004

HUMAN CAPITAL

Senior Executive Performance Management Can Be Significantly Strengthened to Achieve Results

Why GAO Did This Study

Congress and the administration have established a new performance-based pay system for members of the Senior Executive Service (SES) that is designed to provide a clear and direct linkage between SES performance and pay. Also, GAO previously reported that significant opportunities exist for agencies to hold the SES accountable for improving organizational results.

GAO assessed how well selected agencies are creating linkages between SES performance and organizational success by applying nine key practices GAO previously identified for effective performance management. GAO selected the Department of Education, the Department of Health and Human Services (HHS), and the National Aeronautics and Space Administration (NASA).

What GAO Recommends

GAO makes specific recommendations to the agencies to reinforce the key practices through their SES performance management systems. NASA concurred with the recommendations, and HHS provided no comments. Education described specific actions it plans to take to revise its system, which are generally consistent with our recommendations. However, GAO disagrees that Education has already implemented or does not need to implement two of the recommendations.

[www.gao.gov/cgi-bin/getrpt?GAO-04-614](http://www.gao.gov/cgi-bin/getrpt?GAO-04-614).

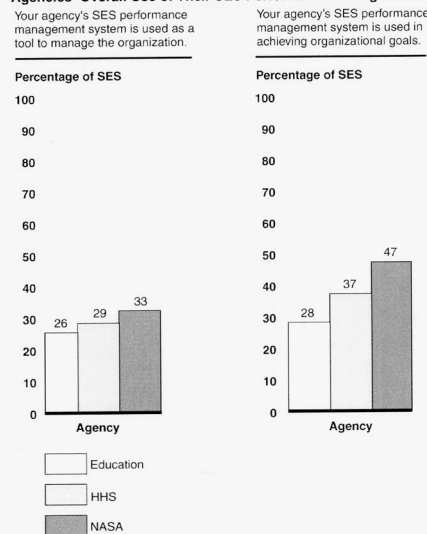
To view the full product, including the scope and methodology, click on the link above. For more information, contact J. Christopher Mihm at (202) 512-6806 or [mihmj@gao.gov](mailto:mihmj@gao.gov).

What GAO Found

Senior executives need to lead the way to transform their agencies' cultures to be more results-oriented, customer focused, and collaborative in nature. Performance management systems can help manage and direct this process. While Education, HHS, and NASA have undertaken important and valuable efforts to link their career SES performance management systems to their organizations' success, there are opportunities to use their systems more strategically. For example, as indicated below by the executives themselves, the agencies can better use their performance management systems as a tool to manage the organization or to achieve organizational goals.

As Congress and the administration are reforming SES pay to better link pay to performance, valid, reliable, and transparent performance management systems with reasonable safeguards are critical. Information on the experiences and knowledge of these agencies should provide valuable insights to other agencies as they seek to drive internal change and achieve external results.

Percentage of Senior Executives Responding to a "Very Great" or "Great" Extent on Their Agencies' Overall Use of Their SES Performance Management Systems



Source: GAO.

United States General Accounting Office

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