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# HUMAN CAPITAL

## Building on the Current Momentum to Address High-Risk Issues

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Highlights of [GAO-03-637T](#), testimony before congressional subcommittees

## Why GAO Did This Study

Federal employees represent the government's knowledge base, drive its capacity to perform, and define its character, and as such, are its greatest asset. The early years of the 21st century are proving to be a period of profound transition for our world, our country, and our government. In response, the federal government needs to engage in a comprehensive review, reassessment, reprioritization, and as appropriate, reengineering of what the government does, how it does business, and in some cases, who does the government's business. Leading public organizations here and abroad have found that strategic human capital management must be the centerpiece of any serious change management initiative and effort to transform the cultures of government agencies.

At the request of the subcommittees, GAO discussed the status of the federal government's efforts to address high-risk human capital weaknesses, possible short- and longer-term legislative solutions to those weaknesses, and other human capital actions that need to be taken to ensure that federal agencies are successfully transformed to meet current and emerging challenges.

[www.gao.gov/cgi-bin/getrpt?GAO-03-637T](http://www.gao.gov/cgi-bin/getrpt?GAO-03-637T).

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

## HUMAN CAPITAL

# Building on the Current Momentum to Address High-Risk Issues

## What GAO Found

Since GAO designated strategic human capital management as a governmentwide high-risk area in January 2001, Congress, the administration, and agencies have taken a number of steps to address the federal government's human capital shortfalls. In fact, more progress in addressing the government's long-standing human capital challenges was made in the last 2 years than in the last 20, and GAO is confident that more progress will be made in the next 2 years than the last 2 years.

Despite the building momentum for comprehensive and systematic reforms, it remains clear that today's federal human capital strategies are not yet appropriately constituted to meet current and emerging challenges or to drive the needed transformation across the federal government. The basic problem is the long-standing lack of a consistent strategic approach to marshaling, managing, and maintaining the human capital needed to maximize government performance and assure its accountability.

Committed and sustained leadership and persistent attention on behalf of all interested parties will continue to be essential to building on the progress that has been and is being made. Congress has had and will need to continue to have a central role in improving agencies' human capital approaches. The basic principles underlying the legislative proposals Congress is considering have merit. Collectively, these proposals would make a positive contribution to addressing high-risk human capital issues and advancing the needed cultural transformation across the federal government. At the same time, additional safeguards should be considered by Congress in order to prevent potential abuse. Moreover, certain additional proposals should be considered as part of this legislative package.

Looking forward, the time has come to seriously explore more market- and performance-based approaches to federal pay. As part of this exploration, we need to continue to experiment with providing agencies with the flexibility to pilot alternative approaches to setting pay and linking pay to performance. A more performance-based approach to Senior Executive Service pay would be a good place to start. The bottom line, however, is that in order to receive any additional performance-based pay flexibility for broad-based employee groups, agencies should have to demonstrate that they have modern, effective, credible, and validated performance management systems, with adequate safeguards, including reasonable transparency and appropriate accountability mechanisms in place, that are capable of supporting such decisions. Unfortunately, most federal agencies are a long way from meeting this requirement. GAO, on the other hand, has taken numerous steps to meet this requirement and is well positioned to experiment with additional pay for performance flexibility.

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Chairman Voinovich, Chairwoman Davis, and Members of the Subcommittees:

It is a great pleasure to appear before you today to discuss the federal government's greatest asset—its people. Federal employees represent the government's knowledge base, drive its capacity to perform, and define its character. The early years of the 21st century are proving to be a period of profound transition for our world, our country, and our government. This transition is being driven by a number of key trends, including global interdependence; diverse, diffuse, and asymmetrical security threats; changes in the nature of the economy; rapidly evolving science and technologies; dramatic shifts in the age and composition of our population; important quality of life issues; and evolving governance structures and concepts. As the nation and government policymakers grapple with the challenges presented by these evolving trends, they do so in a time when increasing fiscal pressures created by the retirement of the baby boom generation and rising health care costs threaten to overwhelm the nation's fiscal future.<sup>1</sup>

In response to the emerging trends and long-term fiscal challenges the government faces in the coming years, we have an opportunity—and a responsibility—to create highly effective, performance-based organizations that can strengthen the nation's ability to meet the challenges of the 21st century and reach beyond our current level of achievement. Leading public sector organizations here and abroad have found that strategic human capital management must be the centerpiece of any serious government transformation effort. Contrary to the assertions of some public officials and other parties, federal workers can be an important part of the solution to our overall transformation effort. Federal workers are not the problem. They are trapped in and encumbered by outdated and ineffective policies and procedures that must be changed. In addition, they need more consistent and enlightened leadership to show the way forward. They also need help from Congress.

Since we designated strategic human capital management as a governmentwide high-risk area in January 2001, Congress, the administration, and agencies have taken a number of steps to address the federal government's human capital shortfalls. In fact, and this is my major

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<sup>1</sup>U.S. General Accounting Office, *Major Management Challenges and Program Risks: A Governmentwide Perspective*, [GAO-03-95](#) (Washington, D.C.: January 2003).

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point today, I believe that we have made more progress in addressing the government's long-standing human capital challenges in the last 2 years than in the last 20, and I am confident that we will make more progress in the next 2 years than we have made in the last 2 years.

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## Key Actions Have Been Taken over the Last 2 Years to Address Human Capital Weaknesses

When we placed strategic human capital management on our high-risk list back in January 2001, as a governmentwide high-risk challenge, we noted that after a decade of government downsizing and curtailed investments of human capital, it had become increasingly clear that federal human capital strategies were not appropriately constituted to adequately meet the current and emerging needs of the government and its citizens.<sup>2</sup> We provided many examples of where human capital shortfalls were eroding the ability of agencies—and threatening the ability of other agencies—to effectively, efficiently, and economically perform their missions. In short, strategic human capital management was a pervasive challenge across the federal government.

We noted that while legislation and other actions have been put in place since 1990 to address most major management areas, human capital was the critical missing link in reforming and modernizing the federal government's management practices. Our high-risk report pointed to actions that federal leaders and their agencies, the Office of Personnel Management (OPM), the Office of Management and Budget (OMB), and Congress needed to take to address high-risk human capital issues.

Since then, a real and growing momentum for change has become evident.

- In August 2001, President Bush placed the strategic management of human capital at the top of the administration's management agenda.
- In October 2001, OMB notified agencies that they would be assessed against standards for success for each part of the *President's Management Agenda* (PMA), including the strategic management of human capital. The first agency assessment was made public in February 2002 as part of the President's proposed fiscal year 2003 budget. Subsequent assessments were later released in June and

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<sup>2</sup>U.S. General Accounting Office, *High-Risk Series: An Update*, [GAO-01-263](#) (Washington, D.C.: January 2001).

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September 2002 and in January 2003, reporting on both the status and progress of agency efforts.

- In December 2001, OPM released a human capital scorecard to assist agencies in responding to the human capital standards for success in the PMA.
- In March 2002, we released *A Model of Strategic Human Capital Management*, designed to help agency leaders determine how well they integrate human capital considerations into daily decision making and planning for the program results they seek to achieve.<sup>3</sup>
- In April 2002, the Commercial Activities Panel, which I was honored to chair, sought to elevate attention to human capital considerations in making sourcing decisions.
- In October 2002, OMB and OPM approved revised standards for success in the human capital area of the PMA, reflecting language that was developed in collaboration with GAO. To assist agencies in responding to the revised PMA standards, OPM released the *Human Capital Assessment and Accountability Framework*.
- In the fall of 2002, OPM began realigning its organizational structure and appointed four new associate directors with proven human capital expertise to lead federal efforts as part of a larger OPM effort to be more customer-focused.
- In November 2002, Congress passed the Homeland Security Act of 2002, which created the Department of Homeland Security (DHS) and provided the department with significant flexibilities to design a modern human capital management system. The effective development and implementation of these flexibilities will prove essential to the performance and accountability of DHS, as well as provide a potential model for Congress to consider for wider application governmentwide.
- The Homeland Security Act of 2002 also included additional significant provisions relating to governmentwide human capital management, such as direct hire authority, the ability to use categorical ranking in the

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<sup>3</sup>U.S. General Accounting Office, *A Model of Strategic Human Capital Management*, GAO-02-373SP (Washington, D.C.: Mar. 15, 2002).

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hiring of applicants instead of the “rule of three,” the creation of chief human capital officer (CHCO) positions and a CHCO Council, an expanded voluntary early retirement and “buy-out” authority, a requirement to discuss human capital approaches in Government Performance and Results Act plans and reports, and a provision allowing executives to receive their total performance bonus in the year in which it is awarded.

- Congress has further underscored the consequences of human capital weaknesses in federal agencies and pinpointed potential solutions through its oversight process and a range of hearings.

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## Strategic Human Capital Management Remains at High Risk

Despite the building momentum for comprehensive and systematic reforms, it remains clear that today’s federal human capital strategies are not yet appropriately constituted to meet current and emerging challenges or to drive the needed transformation across the federal government. The basic problem is the long-standing lack of a consistent strategic approach to marshaling, managing, and maintaining the human capital needed to maximize government performance and assure its accountability. Specifically, as detailed in our January 2003 high-risk volume on human capital, agencies continue to face challenges in four overarching areas:<sup>4</sup>

- **Leadership:** Top leadership in agencies must provide the committed and inspired attention needed to address human capital and related organization transformation issues.
- **Strategic human capital planning:** Agencies’ human capital planning efforts need to be more fully and demonstrably integrated with mission and critical program goals.
- **Acquiring, developing, and retaining talent:** Additional efforts are needed to improve recruiting, hiring, professional development, and retention strategies to ensure that agencies have the needed talent.
- **Results-oriented organizational cultures:** Agencies continue to lack organizational cultures that promote high performance and

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<sup>4</sup>U.S. General Accounting Office, *High-Risk Series: Strategic Human Capital Management*, GAO-03-120 (Washington, D.C.: January 2003).

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accountability and empower and include employees in setting and accomplishing programmatic goals.

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## Building on the Current Momentum Can Create Lasting Change

Committed and sustained leadership and persistent attention on behalf of all interested parties will continue to be essential to building on the progress that has been and is being made, if lasting reforms are to be successfully implemented. First and foremost, individual federal agencies need to more consistently adopt a strategic approach to the use of their people. This requires persistent leadership and a long-term commitment; aligning human capital approaches with the accomplishment of agency goals; implementing recruiting, hiring, training, professional development, performance reward, and retention approaches that foster mission accomplishment; and instilling a results-oriented organizational culture. Agencies' CHCOs will need to play a particularly important role in this regard. The careful and strategic selection of these officials is therefore critical. The CHCO is not fundamentally an "HR" or personnel administration position, although knowledge in those areas is important. Rather, agency CHCOs should have the ability, experience, vision, attributes, and credibility needed to successfully integrate human capital considerations with program goals and to play a major leadership role in driving agency transformation efforts. Agencies also must make effective use of the tools and flexibilities that Congress has provided. To assist agencies in this regard, and at the request of Chairman Voinovich, Ranking Minority Member Durbin, and other Members of Congress, we issued a report last December detailing the practices that agencies need to employ to effectively use human capital flexibilities.<sup>5</sup> These practices are shown in figure 1.

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<sup>5</sup>U.S. General Accounting Office, *Human Capital: Effective Use of Flexibilities Can Assist Agencies in Managing Their Workforces*, [GAO-03-2](#) (Washington, D.C.: Dec. 6, 2002).

**Figure 1: Key Practices for Effective Use of Human Capital Flexibilities**

<b>Plan strategically and make targeted investments</b>	<ul style="list-style-type: none"> <li>• Obtain agency leadership commitment</li> <li>• Determine agency workforce needs using fact-based analysis</li> <li>• Develop strategies that employ appropriate flexibilities to meet workforce needs</li> <li>• Make appropriate funding available</li> </ul>
<b>Ensure stakeholder input in developing policies and procedures</b>	<ul style="list-style-type: none"> <li>• Engage the human capital office</li> <li>• Engage agency managers and supervisors</li> <li>• Involve employees and unions</li> <li>• Use input to establish clear, documented, and transparent policies and procedures</li> </ul>
<b>Educate managers and employees on the availability and use of flexibilities</b>	<ul style="list-style-type: none"> <li>• Train human capital staff</li> <li>• Educate agency managers and supervisors on existence and use of flexibilities</li> <li>• Inform employees of procedures and rights</li> </ul>
<b>Streamline and improve administrative processes</b>	<ul style="list-style-type: none"> <li>• Ascertain the source of existing requirements</li> <li>• Reevaluate administrative approval processes for greater efficiency</li> <li>• Replicate proven successes of others</li> </ul>
<b>Build transparency and accountability into the system</b>	<ul style="list-style-type: none"> <li>• Delegate authority to use flexibilities to appropriate levels within the agency</li> <li>• Hold managers and supervisors directly accountable</li> <li>• Apply policies and procedures consistently</li> </ul>
<b>Change the organizational culture</b>	<ul style="list-style-type: none"> <li>• Ensure involvement of senior human capital managers in key decision-making processes</li> <li>• Encourage greater acceptance of prudent risk taking and organizational change</li> <li>• Recognize differences in individual job performance and competencies</li> </ul>

Source: GAO.

The central management agencies—OPM and OMB—also have continuing vital roles to play. As the agency responsible for leading human capital management governmentwide, OPM plays a central role in helping agencies tackle the broad range of human capital challenges that are at the root of transforming what agencies do, how they do it, and with whom they partner. As detailed in our *Performance and Accountability Series* volume on OPM, our work and the work of others continues to show that agencies need and want greater leadership from OPM in helping them to address their human capital challenges, especially in identifying new human capital flexibilities, removing obstacles from the federal hiring process, and assisting agency workforce planning efforts.<sup>6</sup> Opportunities exist for OPM to be more vigorous in responding to a number of critical program challenges, such as applicant examination, staffing, and compensation approaches. In addition, OPM shares responsibility with agencies for

<sup>6</sup>U.S. General Accounting Office, *Major Management Challenges and Program Risks: Office of Personnel Management*, GAO-03-115 (Washington, D.C.: Jan. 30, 2003).



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ensuring that human capital practices are carried out in accordance with merit system principles and other national goals. Effective and strategic oversight of agencies' systems is even more critical today because an increasing number of agencies are seeking and obtaining exemptions from traditional civil service rules at the same time that human capital staffs responsible for overseeing these activities have dwindled.

In response to these ongoing challenges, OPM has taken a number of important actions. First, OPM realigned its organizational structure and workforce to create a new, flexible structure that seeks to "de-stovepipe" the agency; enable it to be more responsive to its primary customers, federal departments and agencies; and focus on the agency's core mission. In November 2002, OPM's Director appointed four new associate directors with proven human capital expertise to lead the organization. OPM also has the key role in leading the administration's efforts to address strategic human capital management, a critical part of the PMA. OPM also published two reports in 2001 to increase agencies' awareness of available human capital flexibilities, and released a report on federal compensation practices in April 2002. A major initiative begun in the spring of 2002 is designed to improve the hiring process. Furthermore, OPM is addressing its oversight challenge in part by encouraging agencies to develop and maintain internal accountability systems in line with its *HRM Accountability Standards*. OPM recently released the results of its 2002 Federal Human Capital Survey. This survey is providing a wealth of important information on the views and attitudes of federal employees. The results demonstrate the importance of routinely surveying employees across the federal government through the Federal Human Capital Survey or a similar survey. Consideration should be given to exploring ways to assure that these surveys will be conducted on a periodic basis. Finally, OPM is at the center of the DHS's efforts to create a modern personnel system that serves the needs of the department and could serve as a potential model for others.

The designation of human capital as the first item on the PMA and the supporting standards for success have raised the profile of human capital issues on OMB's agenda. As OMB and the agencies learn to evaluate themselves against the standards and implement policies to make improvements, OMB will need to ensure that the standards are consistently and appropriately applied while assessing agencies' progress in managing their human capital. Perhaps most important, OMB support will be needed as agencies identify targeted investment opportunities to address human capital shortfalls.

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## Congressional Leadership Continues to Be Critical

Congress has had and will need to continue to have a central role in improving agencies' human capital approaches. Traditionally, Congress has been an institutional champion in improving management of executive agencies across the government. Support and pressure from Congress has been indispensable to instituting and sustaining management reforms at specific agencies. Its confirmation, oversight, appropriations, and legislative responsibilities provide Congress with continuing opportunities to ensure that agencies recognize their responsibilities to manage people for results. For example, as Chairman Voinovich has often stressed, the Senate has the opportunity during the confirmation process to articulate its commitment to sound federal management by exploring how prospective nominees plan to make a link between mission accomplishment and human capital policies.<sup>7</sup> As part of the oversight and appropriations process, Congress can continue to examine whether agencies are managing their human capital to improve programmatic effectiveness and to encourage agencies to use the range of appropriate flexibilities available under current law.

## Targeted Human Capital Reforms

Congress will also play a critical role in determining the nature and scope of any additional human capital flexibilities that will be made available to agencies, while assuring that adequate safeguards are incorporated to prevent abuse. Congress also has the responsibility to ensure the reasonableness and adequacy of financial resources that are made available to agencies.

Congress is currently considering several pieces of legislation to help agencies address their current and emerging human capital challenges. I believe that the basic principles underlying these legislative proposals have merit and collectively they would make a positive contribution to addressing high-risk human capital issues and advancing the needed cultural transformation across the federal government. I also believe that certain additional safeguards and provisions should be considered by Congress. We look forward to working with the subcommittees as you consider these and related legislative initiatives. Today, I will provide observations on selected provisions of the various proposals.

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<sup>7</sup>Toward this end, we developed a set of questions for political appointees that the Senate may use during the confirmation process. See U.S. General Accounting Office, *Confirmation of Political Appointees: Eliciting Nominees' Views on Leadership and Management Issues*, GAO/GGD-00-174 (Washington, D.C.: Aug. 11, 2000).

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## The Senior Executive Service Reform Act of 2003

The proposed Senior Executive Service Reform Act of 2003 includes a number of important reforms. For example, the legislation would move to a single Senior Executive Service (SES) pay range, increase the pay cap, and link SES pay more closely to performance. I strongly believe that these are worthwhile reforms that must be considered together, as they are in this proposed legislation. The legislation seeks to link pay and performance of senior executives by replacing the current system of six grades with a single pay band. Agencies would have flexibility to set basic pay for SES members at any amount within the range plus locality pay, to a total annual salary that may not exceed level II of the Executive Schedule. In addition, agencies could employ a broadbanding approach to SES pay should they so desire. This important change would provide agencies with needed flexibility to set SES pay in a way that reflects the reality of the great diversity in the work that members of the SES do rather than using a set of rigid SES pay grades. In fact, I have the authority to adopt such an approach in setting the pay for the SES in the GAO, and we plan to do so.

The legislation would raise the highest basic pay rate for an SES member from the current maximum of \$134,000 (level IV of the Executive Schedule) to \$142,500 (level III of the Executive Schedule). SES basic pay currently ranges from \$116,500 to \$134,000, before locality pay is included. The problems of SES pay compression are real and must be addressed, with over 60 percent of SES members being at the current cap.

The SES needs to lead the way in the federal government's effort to better link pay to performance. The legislation would require that agencies base their SES pay decisions on "individual performance, contribution to the agency's performance, or both." We have reported that there are significant opportunities to strengthen efforts to hold senior executives accountable for results.<sup>8</sup> In particular, more progress is needed in explicitly linking senior executive expectations for performance to results-oriented organizational goals, fostering the necessary collaboration both within and across organizational boundaries to achieve results, and demonstrating a commitment to lead and facilitate change. These expectations for senior executives will be critical to keep agencies focused on transforming their cultures to be more results-oriented, less hierarchical, more integrated, and

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<sup>8</sup>U.S. General Accounting Office, *Results-Oriented Cultures: Using Balanced Expectations to Manage Senior Executive Performance*, GAO-02-966 (Washington, D.C.: Sept. 27, 2002).

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externally focused and thereby be better positioned to respond to emerging internal and external challenges, improve their performance, and assure their accountability.

Agencies should be required to have modern, effective, credible, and validated performance management systems in place before they are granted authority to better link pay to performance for broad-based employee groups. In this regard, Congress should consider providing specific statutory standards that agencies' performance management systems would be required to meet before OPM could approve any such pay for performance effort. Our own experience in implementing such reforms in GAO and the practices of other leading organizations that I will discuss shortly could serve as a starting point for that consideration.

Finally, the legislation's provision to allow agencies to credit nonfederal work experience for purposes of providing annual leave recognizes that the federal government must effectively recruit in a larger labor market. The increasing number of retirement-eligible federal employees is most concentrated in mid- and senior- level positions. To attract top talent, both at the entry and at midcareer levels, it is important to offer applicants an attractive compensation and benefits package that is not structured entirely on a model that assumes a 30-year career of federal service. Simply stated, this provision recognizes the reality of increased mobility in the workforce and the need to modernize our annual leave provisions to attract and retain experienced people with critical skills.

### **The Federal Workforce Flexibility Act of 2003**

The Federal Workforce Flexibility Act of 2003 would expand the authority to use and increase the amount of recruitment and retention bonuses. For example, the legislation would allow the payment of a recruitment bonus of up to 100 percent of an employee's annual salary for critical, hard-to-fill positions, subject to approval by the agency. The legislation also expands the use of recruitment bonuses to employees currently employed in another federal agency and retention bonuses to employees who might leave to go to another federal agency. Previously, recruitment bonuses could only be paid to employees coming from outside the federal government and retention bonuses could only be paid to employees likely to leave federal employment altogether. We support providing agencies with these types of additional tools and flexibilities to attract and retain needed staff as long as such payments are targeted, based on a business need, and are implemented with adequate safeguards. In that regard,

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Congress should consider capping the number or percentage of employees in an agency who would be eligible for such payments.

As you know, the federal government faces a looming wave of employees who will be eligible for retirement. Agencies need succession planning programs to ensure that knowledge is transferred from one generation of employees to another. An approach that should be explored would be to allow “phased retirements.” There are a number of ways that a phased retirement program could work; the legislation seeks to provide one option for employees who would like to work part time as they end their federal careers by prorating retirement annuities for the period of service that was performed on a part-time basis, thus removing a current disincentive to such part-time work.

The Federal Workforce Flexibility Act of 2003 would also expand the authority to conduct personnel demonstration projects. Such projects, authorized by OPM under the Civil Service Reform Act of 1978, provide a means for testing and introducing improvements in governmentwide human resources management systems. To become a demonstration project, a federal agency obtains authority from OPM to waive existing federal human resources management laws and regulations in Title 5 and propose, develop, test, and evaluate interventions for its own human resources management system that can help shape the future of federal human resource management.<sup>9</sup>

As a general rule, current law limits the size of a demonstration project to 5,000 employees and the life of a project to a 5-year time limit. The legislation would eliminate the cap on the number of employees who could participate in a demonstration project and allow the projects to have up to a 10-year life span. This more flexible approach to demonstration projects is consistent with the approach Congress took in 1996 in authorizing the Department of Defense civilian acquisition workforce demonstration project to expand the number of personnel eligible to participate from the statutory cap of 5,000 to a maximum of 95,000 and extend the project's length from a 5-year time limit to 13 years.

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<sup>9</sup>No waivers of law are permitted in areas of employee leave, employee benefits, equal employment opportunity, political activity, merit system principles, or prohibited personnel practices.

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Demonstration projects' testing, evaluation, and reporting requirements have provided invaluable lessons learned to other federal organizations. Much of the federal government's knowledge and real-world experience with performance-based pay reform has been obtained through demonstration projects. In fact, of the 17 demonstration projects that have been implemented over the past 25 years, 12 have tested some form of linking compensation to performance. In addition, a demonstration project done at the Department of Agriculture provided an important test of using categorical ranking as part of the applicant selection process and was therefore useful to the Congress in deciding to expand such authorities governmentwide as part of the Homeland Security Act of 2002.

The Federal Workforce Flexibility Act of 2003's reforms to enhance agencies' training and career development programs are also positive steps that should help improve human capital management. The legislation calls for agencies to evaluate their training programs and plans to ensure that they are linked to strategic and performance goals and contribute to achieving the agency's mission. Such evaluations of training and development efforts are important in demonstrating how these efforts help develop employees and improve the agency's performance. As part of a balanced approach, training and development evaluations should consider organizational results and feedback from customers and employees. The strategic evaluation requirement in this legislation should help move agencies away from an orientation on activities or processes (such as the number of participants, courses offered, and hours of training provided), and instead use information on how training and development efforts (1) contribute to improved performance, (2) strengthen capacity to meet new and emerging challenges, and (3) reduce the cost of poor performance.

The legislation focuses agencies on several specific areas of importance, including developing succession programs and informing managers about effective strategies to address performance problems, mentor employees, and improve performance and productivity. We have noted that linking an executive development program and comprehensive succession planning to agency goals and objectives can help foster a committed leadership team. Further, calling for agencies to identify and share effective human capital strategies can help improve individual and organizational performance and further efforts to transform the cultures of government agencies. At Chairman Voinovich's request, this fall we will report on selected agencies' efforts to design effective training and development programs.

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## **Generating Opportunity by Forgiving Educational Debt Service Act of 2003**

Congress previously passed legislation that allows agencies to set up programs to repay the student loans of federal employees in order to attract or keep highly qualified individuals. Several agencies, including GAO, have begun such programs and have found them to be valuable in attracting and retaining high-quality talent. These payments are currently included in gross income for federal tax purposes. However, the Generating Opportunity by Forgiving Educational Debt Service Act of 2003 (GOFEDS) would make these payments nontaxable. GOFEDS would therefore make payments by the federal government generally comparable to loan forgiveness programs in use by some educational institutions and nonprofit organizations. We believe that this provision has great merit. It would help to further leverage existing student loan repayment program dollars and would help agencies in their efforts to attract and retain top talent. Obviously, Congress will need to balance the federal human capital benefits of this provision as a tax expenditure with overall federal tax policy. Moreover, Congress should consider how GOFEDS could be implemented in such a way that the tax forgiveness provisions do not obscure the true costs of agency operations.

## **The Presidential Appointments Improvement Act of 2003**

The Presidential Appointments Improvement Act of 2003 would, among other things, require each executive agency to identify the number of presidentially appointed, Senate-confirmed positions and the layers of those positions. Related to this provision, last September I convened a roundtable to discuss the Chief Operating Officer (COO) concept and how it might apply within selected federal departments and agencies as one strategy to address certain systemic federal governance and management challenges.<sup>10</sup> There was considerable discussion on whether the senior management official in an agency should be presidentially appointed, requiring Senate confirmation, while Senate confirmation would not be required for those officials who lead specific management functions (e.g., financial management, information technology, human capital) and who

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<sup>10</sup>U.S. General Accounting Office, *Highlights of a GAO Roundtable: The Chief Operating Officer Concept: A Potential Strategy to Address Federal Governance Challenges*, [GAO-03-192SP](#) (Washington, D.C.: Oct. 4, 2002). The invited participants were generally individuals with current or recent executive branch leadership responsibilities, significant executive management experience, or both.

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report to that senior management official. While there was interest in considering such an arrangement, it was also acknowledged that it would likely require amending existing legislation, for example the Chief Financial Officers Act, and, therefore, would need careful analysis to ensure that any legislative changes result in augmented attention to management issues and do not inadvertently lead to a reduction in the authority of key management officials and/or the prominence afforded a particular management function.

An additional suggestion made at the roundtable that Congress may wish to consider would be to allow senior management officials in each agency to assume full authorities and responsibilities up to or for a specified period of time once they were formally nominated but before their confirmation. However, it was widely recognized that such an approach would be viable only if the senior management position was restricted to the professional and nonpartisan “good government” responsibilities that are fundamental to effectively executing any administration’s program agenda and did not entail program policy-setting authority. Furthermore, should Congress decide to adopt the COO concept noted above and not make subject certain management officials to the confirmation process (e.g., the Chief Financial Officer and the Chief Information Officer), the need for this flexibility would be greatly reduced.

More generally, the roundtable’s overall purpose was to discuss the COO concept and how it might apply within selected federal departments and agencies. The roundtable discussion neither sought nor achieved a consensus on the COO concept. However, it does appear that there was general agreement on a number of important overall themes that can serve as a basis for subsequent analysis, discussion, and consideration. These generally agreed-upon themes provide a course for action.

- Elevate attention on management issues and transformational change. The nature and scope of the changes needed in many agencies require the sustained and inspired commitment of the top political and career leadership. There is no substitute for top leadership involvement, including that of the President, through for example, the establishment of a governmentwide management agenda. Top leadership attention is essential to overcome organizations’ natural resistance to change, marshal the resources needed to implement change, and build and maintain the organizationwide commitment to new ways of doing business.



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- Integrate various key management and transformation efforts. By their very nature, the problems and challenges facing agencies are crosscutting and thus require coordinated and integrated solutions. However, the federal government too often places management responsibilities (for example, information technology, human capital, or financial management) into various “stovepipes” and fails to implement transformational change management initiatives in a comprehensive, ongoing, and integrated manner. While officials with management responsibilities often have successfully worked together, there needs to be a single point within agencies with the perspective and responsibility—as well as authority—to ensure the successful implementation of functional management and, if appropriate, transformational change efforts. At the same time, it is not practical to expect that the deputy secretaries, given the competing demands on their time in helping the secretaries execute the President’s policy and program agendas, will be able to consistently undertake this vital integrating responsibility. Moreover, while many deputy secretaries may be nominated based in part on their managerial experience, it has not always been the case and, not surprisingly, the management skills, expertise, and interests of the deputy secretaries have always varied and will continue to vary.
  - Institutionalize accountability for addressing management issues and leading transformational change. The management weaknesses in some agencies are deeply entrenched and long-standing and will take years of sustained attention and continuity to resolve. In addition, making fundamental changes in agencies’ cultures will require a long-term effort. The experiences of successful major change management initiatives in large private and public sector organizations suggest that it can often take at least 5 to 7 years until such initiatives are fully implemented and the related cultures are transformed in a sustainable manner. In the federal government, the frequent turnover of the political leadership has often made it difficult to obtain the sustained and inspired attention required to make needed changes.

## Implementing Market-Based and Results-Oriented Pay Reforms

Looking forward, Congress should consider making comprehensive legislative reforms to existing civil service laws, taking into account the extent to which traditional approaches make sense in the current and future operating environments. In that regard, there is a growing understanding that we need to fundamentally rethink our approach to federal pay and develop an approach that places a greater emphasis on a person’s knowledge, skills, position, and performance rather than the

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passage of time, the rate of inflation, and geographic location. The OPM Director's White Paper on modernizing federal pay, issued last April, amply demonstrated that the current federal pay system was designed for the heavily clerical and low graded workforce of the 1950s rather than today's knowledge-based government. Similarly, the National Commission on the Public Service, chaired by Paul Volcker, observed that agencies need greater freedom to connect pay both to the market and to performance. In short, as the nature of the federal workforce has changed, so too must our pay system if we are to effectively compete for top talent and create incentives for both individual and institutional success.

Under the current federal pay system, the overwhelming majority of each year's increase in federal employee pay is largely unrelated to an employee's knowledge, skills, position, or performance. In fact, over 80 percent of the cost associated with the annual increases in federal salaries is due to longevity and the annual pay increase. One approach that has been tested and that I believe deserves wider consideration is to reserve the annual pay adjustment for only those employees who receive an acceptable performance rating. This would send a clear message to the overwhelming majority of federal employees that their contributions are valued, and those few who are not contributing will not be rewarded for their lack of effort. More generally, current federal pay gaps vary by the nature of the person's position and yet the current method for addressing the pay gap assumes that it is the same throughout government.

We must move beyond this outdated, "one-size-fits-all" approach to paying federal employees and seriously explore more market- and performance-based approaches to federal pay. As part of this exploration, we need to continue to experiment with providing agencies with the flexibility to pilot alternative approaches to setting pay and linking pay to performance. The greater use of "broadbanding" is one of the options that should be considered as part of a broader discussion of pay reform. In the short term, Congress should explore the benefits of (1) providing OPM with additional flexibility that would enable it to grant governmentwide authority for all agencies (i.e., class exemptions) to use broadbanding for certain critical occupations and/or (2) allowing agencies to apply to OPM (i.e., case exemptions) for broadbanding authority for their specific critical occupations. However, agencies should be required to demonstrate to OPM's satisfaction that they have modern, effective, credible, and validated performance management systems before being able to adopt broader pay for performance systems for non-SES personnel. In this regard, Congress should consider providing specific statutory standards that agencies must

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meet before OPM would be able to grant an exemption from existing Title 5 requirements.

As with all pay for performance efforts, adequate safeguards, including reasonable transparency and appropriate accountability mechanisms, would need to be in place to ensure fairness, prevent politicalization, and prevent abuse. Such safeguards would include ensuring that an agency's career leadership and managers have significant roles in performance-related pay decisions and that employees have central roles in the design and implementation of the system to build their sense of ownership for the system. In our work looking at leading performance management efforts here and abroad, we have found that the involvement of employees is critical to the success of such initiatives.<sup>11</sup> Leading organizations consulted a wide range of stakeholders early in the process, obtained feedback directly from employees, and engaged employees' unions or associations.

The bottom line is that in order to receive any additional performance-based pay flexibility for broad-based employee groups, agencies should have to demonstrate that they have the modern, effective, credible, and validated performance management systems in place that are capable of supporting such decisions. Unfortunately, most federal agencies are a long way from meeting this requirement. As I noted earlier, the SES needs to lead the way in the federal government's effort to better link pay to performance. Given the state of agencies' performance management systems, Congress should consider starting federal results-oriented pay reform with the SES. Agencies should be granted the authority to implement additional pay for performance programs only after they have demonstrated that they have appropriate performance management systems and adequate safeguards in place. Building such systems and safeguards will likely require making targeted investments in agencies' human capital programs, as GAO's own experience has shown. In that regard, Congress and the Administration should consider how incentives can be provided to encourage agencies to modernize their performance management systems. This could include a potential governmentwide fund for such purposes, which could be allocated based on specific business case proposals by individual agencies. This approach could also help to

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<sup>11</sup>See for example, U.S. General Accounting Office, *Results-Oriented Cultures: Insights for U.S. Agencies from Other Countries' Performance Management Initiatives*, [GAO-02-862](#) (Washington, D.C.: Aug. 2, 2002).

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facilitate implementation of the high-performing organization (HPO) concept recommended by the Commercial Activities Panel that I chaired.

A report we prepared at the request of Chairman Voinovich and Chairwoman Davis that was released last month shows specific practices that leading public sector organizations both here in the United States and abroad have used in their performance management systems to link individual performance and organizational success.<sup>12</sup> These practices include the following:

1. **Align individual performance expectations with organizational goals.** An explicit alignment helps individuals see the connection between their daily activities and organizational goals.
2. **Connect performance expectations to crosscutting goals.** Placing an emphasis on collaboration, interaction, and teamwork across organizational boundaries helps strengthen accountability for results.
3. **Provide and routinely use performance information to track organizational priorities.** Individuals use performance information to manage during the year, identify performance gaps, and pinpoint improvement opportunities.
4. **Require follow-up actions to address organizational priorities.** By requiring and tracking follow-up actions on performance gaps, organizations underscore the importance of holding individuals accountable for making progress on their priorities.
5. **Use competencies to provide a fuller assessment of performance.** Competencies define the skills and supporting behaviors that individuals need to effectively contribute to organizational results.
6. **Link pay to individual and organizational performance.** Pay, incentive, and reward systems that link employee knowledge, skills, and contributions to organizational results are based on valid, reliable,

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<sup>12</sup>U.S. General Accounting Office, *Results-Oriented Cultures: Creating a Clear Linkage between Individual Performance and Organizational Success*, [GAO-03-488](#) (Washington, D.C.: Mar. 14, 2003).

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and transparent performance management systems with adequate safeguards.

7. **Make meaningful distinctions in performance.** Effective performance management systems strive to provide candid and constructive feedback and the necessary objective information and documentation to reward top performers and deal with poor performers.
8. **Involve employees and stakeholders to gain ownership of performance management systems.** Early and direct involvement helps increase employees' and stakeholders' understanding and ownership of the system and belief in its fairness.
9. **Maintain continuity during transitions.** Because cultural transformations take time, performance management systems reinforce accountability for change management and other organizational goals.

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## GAO's Commitment to Lead by Example

We in GAO believe it is our responsibility to lead by example. We seek to be in the vanguard of the federal government's overall transformation efforts, including in the critically important human capital area. We are clearly in the lead at the present time, and we are committed to staying in the lead. We fully recognize that our people are our most valuable asset, and it is only through their combined efforts that we can effectively serve our clients and our country. By managing our workforce strategically and focusing on achieving positive and measurable results, we are helping to maximize our own performance and ensure our own accountability. By doing so, we also hope to demonstrate to other federal agencies that they can make similar improvements in the way they manage their people.

We have identified and made use of a variety of tools and flexibilities, some of which were made available to us through the GAO Personnel Act of 1980 and our calendar year 2000 human capital legislation, but most of which are available to all federal agencies. The most prominent change in human capital management that we implemented as a result of the GAO Personnel Act of 1980 was a broadbanded pay-for-performance system. The primary goal of this system is to base employee compensation primarily on the knowledge, skills, and performance of individual employees. It also provides managers flexibility to assign employees in a manner that is more suitable to multi-tasking and the full use of staff. Under our current

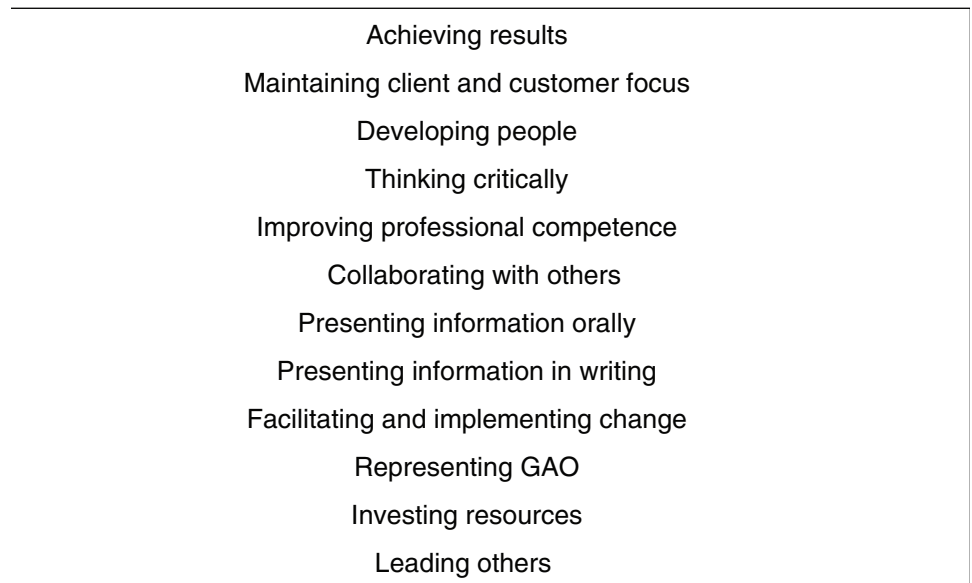
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broadbanded system, analyst and analyst-related staff in Grades 7 through 15 were placed in three bands. While our general experience has been positive, we expect to modify our banded system in the future based on our experience to date.

In January 2002, we implemented a new competency-based performance management system that is intended to link employee performance and our strategic plan and agency core values. It includes 12 competencies that our employees overwhelmingly validated as the keys to meaningful performance at GAO. (See fig. 2.) Modernizing performance management systems in the federal government is essential to the overall government transformation effort. Importantly, doing so can be accomplished without any additional legislation.

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**Figure 2: GAO's Competency-Based Model**



Source: GAO.

Our October 2000 legislation gave us additional tools to realign our workforce in light of mission needs and overall budgetary constraints; correct skills imbalances; and reduce high-grade, managerial, or supervisory positions without reducing the overall number of GAO employees. This legislation allowed us to create a technical and scientific career track at a compensation level consistent to the SES. It also allowed

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us to give greater consideration to performance and employee skills and knowledge in any reduction-in-force actions.

Since the legislation was enacted, we have established agency regulations and offered voluntary early retirement opportunities. Once employees registered their interest in participating in the program, we considered a number of factors, including employee knowledge, skills, performance, and competencies; the organizational unit or subunit in which an employee worked; an employee's occupational series, grade, or band level, as appropriate; and the geographic location of the employee. As authorized by the 2000 legislation, employee performance was just one of many factors we considered when deciding which employees would be allowed to receive the incentives. However, let me assure you, we did not use performance to target certain individuals. Early retirement was granted to 52 employees in fiscal year 2002 and 24 employees in fiscal year 2003. Our annual performance and accountability reports have provided additional information on our use of this authority. As required by the 2000 legislation, we will shortly be providing Congress a more comprehensive assessment of our use of the authorities granted to us under the act.

We are also using many recruiting flexibilities that are available to most agencies, including an extensive campaign to increase our competitiveness on college campuses and extending offers of employment during the fall semester to prospective employees who will come on board the following spring and summer. We are also using our internship program in a strategic fashion, and we often offer permanent positions to GAO interns with at least 10 weeks of highly successful work experience. Moreover, we are building and maintaining a strong presence of both senior executives and recent graduates on targeted college campuses. We have also taken steps to streamline and expedite our hiring process. Even after we hire good people, we need to take steps to retain them. We have taken a number of steps to empower and invest in our employees. For example, we have active employee feedback and suggestion programs. In addition, we implemented a student loan repayment assistance program for employees who have indicated interest and are willing to make a 3-year commitment to staying with the agency.

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Overall, we have implemented a number of human capital initiatives, including the following, some of which are relatively recent and some of which are long-standing:<sup>13</sup>

- Prepared a human capital profile and needs assessment to understand employee demographics and distribution.
- Conducted agencywide, confidential, and web-based employee surveys in 1999 and 2002 to understand the status and progress of the agency and the areas in which we need to improve.
- Completed a knowledge and skills inventory for all employees.
- Achieved a democratically elected Employee Advisory Council to facilitate open communication and direct input from line employees to the Comptroller General and other GAO senior leaders on matters of mutual interest and concern.
- Conducted an employee preference survey so that employees could be given the opportunity to work in the areas that interest and energize them in light of our institutional needs.
- Implemented an Executive Candidate Development Program to prepare candidates for assignments in the SES.
- Developed and implemented a strategy to place more emphasis on diversity in campus recruiting.
- Initiated a Professional Development Program for newly hired GAO analysts to help them transition and progress.
- Began developing a core training curriculum to directly link and support our validated core competencies.
- Provided an on-site child care center called “Tiny Findings” and a wellness and fitness center.

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<sup>13</sup>For more information on these efforts, see *Human Capital: Taking Steps to Meet Current and Emerging Human Capital Challenges*, GAO-01-965T (Washington, D.C.: July 17, 2001).



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- Implemented additional employee-friendly benefits such as business casual dress, flextime, and public transportation subsidies.
  - Implemented a program to reimburse GAO employees for the cost incurred in pursuit of relevant professional certifications.
  - Used recruitment bonuses, retention allowances, and student loan repayment assistance to attract and retain employees with specialized skills.
  - Implemented a new “state of the art” performance appraisal system that is linked to our strategic plan and based on key competencies, which have been validated by our employees. This new system has been implemented for analysts. This system is being adapted for our attorneys, and we have begun modifying the system for our administrative professional and support staff.

Many of the above initiatives required one-time investments to make them a reality. We worked with the Congress to present a business case for funding a number of these initiatives. Fortunately, the Congress has supported these and other GAO transformation efforts. The result is a stronger, better positioned, more effective, results-oriented, and respected GAO. As we engage in these changes, we also know that we are not perfect and we never will be. This is a work-in-progress for us as it is for others. In fact, we are constantly evaluating our internal efforts, seeking to learn from others, and making refinements as we go along. In that regard and as you know, we expect in the coming weeks to be formally approaching Congress with recommendations to provide us with additional statutory authorities to enable us to better manage our people. The legislation we plan to recommend would, among other things, facilitate GAO’s continuing efforts to recruit and retain top talent, develop a more performance-based compensation system, help realign our workforce, and facilitate our succession planning and knowledge transfer efforts. We believe that these authorities will strengthen our efforts to serve Congress and provide benefits to the American people. As has been the case in the past, we also expect that our use of these authorities will provide valuable lessons to Congress and agencies on how human capital flexibilities can be used in a context that helps an organization achieve its missions while still ensuring that adequate safeguards, including reasonable transparency and appropriate accountability mechanisms, are in place to prevent abuse.

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## Summary

When we placed strategic human capital management on our high-risk list in 2001, we all knew that successfully addressing human capital challenges would not be quick nor easy. Due to the combined efforts of Congress, OPM, OMB, the agencies, federal employees, and others, we have made a great deal of progress over the last 2 years. But more should be done. Comprehensive human capital legislative reforms will likely be needed, but agency leaders must not wait for them to happen. Congress has already provided much of the authority agencies need. Therefore, the first step toward meeting the government's human capital challenges is for agency leaders to identify and make use of all the appropriate administrative authorities available to them to manage their people for results. The use of these authorities often will need to be undertaken as part of and consistent with proven change management practices and with adequate safeguards to prevent abuse. The second step, as the subcommittees have made clear, is to consider selected legislative reforms to give agencies additional tools and flexibilities to hire, manage, and retain the human capital they need. These additional flexibilities also should be accompanied with adequate safeguards to prevent abuse. The third step is for all interested parties to work together to identify the kinds of comprehensive legislative reforms that should be enacted in the human capital area over time, with comprehensive pay reform being the likely centerpiece of that effort.

Chairman Voinovich and Chairwoman Davis, this concludes my prepared statement. I would be pleased to respond to any questions that you or other Members of the Subcommittees may have.

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## Contacts and Acknowledgments

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