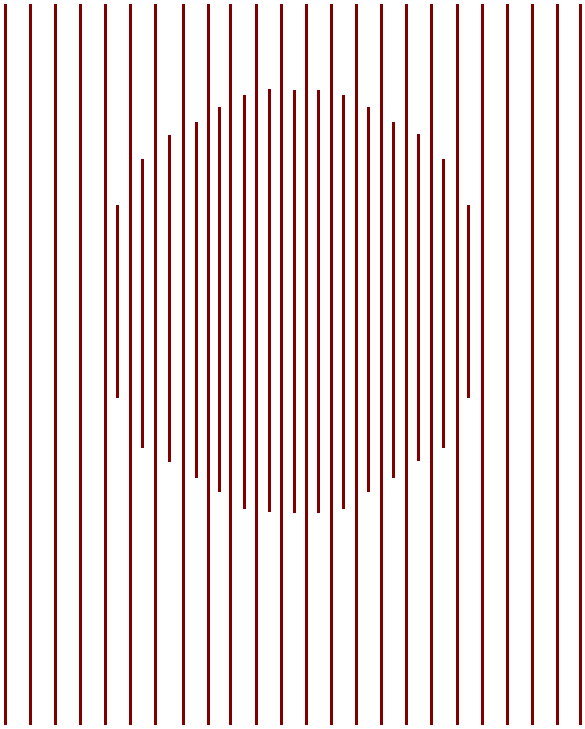
CBO PAPERS

ISSUES IN DETERMINING PAY RAISES FOR FEDERAL WHITE-COLLAR EMPLOYEES

May 1995



CONGRESSIONAL BUDGET OFFICE

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CONGRESSIONAL BUDGET OFFICE
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WASHINGTON, D.C. 20515

NOTES

Numbers in the text and tables may not add to totals because of rounding.

Unless othewise indicated, all years in this paper are fiscal years.

PREFACE

The system by which the federal government determines pay raises for federal white-collar employees is complex and controversial. This paper describes that system and examines three issues often raised in connection with it. In addition, it describes the advantages and disadvantages of continuing the practice of limiting pay raises for federal employees below the levels authorized under current law. The Congressional Budget Office (CBO) undertook this analysis in support of work on its annual report to the House and Senate Committees on the Budget.

R. Mark Musell of CBO's Special Studies Division prepared the analysis under the supervision of Robert W. Hartman. Susan Strandberg and Amy Plapp of CBO's Budget Analysis Division prepared the budget estimates that appear in Chapter III. Kathy Ruffing, also of the Budget Analysis Division, prepared the description of the CBO pay model and provided helpful advice and comments. Other current and former CBO analysts provided useful comments, including James L. Blum, Richard Fernandez, Leslie Griffin, James Hearn, and James Horney.

Staff at the Office of Personnel Management provided data and comments, and the author gratefully acknowledges the assistance of Phil Etzel, Allan Hearne, Paul Hershey, Fred Hohlweg, Gordon Klang, Tony Ingrasia, Don Winstead, and James N. Woodruff. Helpful comments were also provided by Jordan Pfuntner at the Bureau of Labor Statistics.

Sherry Snyder edited the manuscript, and L. Rae Roy and Marlies Dunson prepared it for publication.

The author also acknowledges with much gratitude the help and support provided on this and other projects by his long-time friend and assistant, Mary V. Braxton, who passed away before the paper was completed.

June E. O'Neill
Director

May 1995

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SUMMARY

Pay for federal civilian employees will total about $90 billion for 1995, representing about 6 percent of all federal expenditures. In his budget for 1996, President Clinton has again proposed limiting pay raises for those employees to a level well below that allowed under the Federal Employees Pay Comparability Act of 1990 (FEPCA). The act provides for annual pay raises that would, over time, move federal salaries for most white-collar employees toward comparability with nonfederal rates that prevail in different localities. Raises under the act in part reflect comparisons with nonfederal salaries. The information on nonfederal salaries used in those comparisons is collected in surveys conducted by the Bureau of Labor Statistics. The first comparability pay raise under the act occurred in 1994.

Like its predecessor, FEPCA has not been without critics. The President has expressed reservations about the methodology adopted under FEPCA for determining pay raises. Three long-standing areas of concern examined in this paper have to do with how the government collects data on nonfederal salaries, how it compares jobs, and how it applies raises.

PAY AND EMPLOYMENT UNDER THE GENERAL SCHEDULE

The General Schedule (GS) represents the government's largest pay plan, covering 76 percent of the workforce in the executive branch. This plan was the primary focus of reform under FEPCA and of pay limits proposed by the President. Employees covered by the General Schedule hold white-collar jobs in a wide array of occupations. They are concentrated, however, in occupations designated professional, administrative, and technical. Those occupations include accountants, lab technicians, and personnel administrators. The GS workforce is also well educated, with 46 percent holding a bachelor's or higher degree (see Summary Table 1). The payroll for GS employees totaled $57 billion in 1994.

The Structure of the General Schedule

The General Schedule is a table of salaries consisting of 15 pay grades. The federal government assigns jobs to a grade based mainly on the duties and responsibilities the job involves. Each pay grade of the General Schedule has a salary range divided

into 10 intervals referred to as steps. Employees progress up the steps at each grade primarily on the basis of length of service.

Under FEPCA, pay at each GS grade varies among geographic areas, depending on how federal and nonfederal salaries compare in each. Base salaries--that is, salaries without locality pay factored in--range from $12,141 for a GS grade 1, step 1, to $88,326 for a GS grade 15, step 10. With locality adjustments, the highest salary reaches $95,860.

Pay Raises Under the General Schedule

Payroll for GS employees grew by 50 percent during the 1985-1994 period. About 60 percent of that growth reflects general increases in GS salaries, which rose more than 30 percent. That increase is less than the increase in private-sector salaries and in the cost of living. (A general increase refers to an adjustment that affects most

SUMMARY TABLE 1. OCCUPATIONAL DISTRIBUTION AND EDUCATIONAL ATTAINMENT OF GENERAL SCHEDULE WORKERS, SEPTEMBER 1980 AND SEPTEMBER 1993

Occupational Group	Percentage of General Schedule Workforce		Percentage of General Schedule Workforce with Bachelor's or Higher Degree	
	1980	1993	1980	1993
Professional	22	28	86	87
Administrative	26	27	44	60
Technical	22	25	13	14
Clerical	28	17	5	7
Other	3	3	7	11
All Occupations	100	100	35	46

SOURCE: Congressional Budget Office using data provided by the Office of Personnel Management.

NOTE: Data cover employees in the executive branch and those on full-time work schedules.

workers. Pay may also rise as a result of a promotion to a higher grade or an increase in step, but those raises are not considered general increases for purposes of this discussion.)

Under FEPCA, the government may make two adjustments in federal salaries each January. Both of those increases are guided by the principle that federal pay should be comparable with nonfederal pay for the same work. One adjustment is intended to keep federal salaries abreast of changes in private-sector rates as measured by the employment cost index (ECI). The relevant measure is the change in the ECI over a 12-month period minus one-half of a percentage point. The government canceled the 2.2 percent adjustment scheduled for 1994 and reduced the scheduled raise for 1995 from 2.6 percent to 2.0 percent. The full ECI adjustment under FEPCA for 1996 would total 2.4 percent.

The other adjustment helps federal salaries to catch up to nonfederal salaries in areas where they lag by more than 5 percent. In contrast to adjustments based on the ECI, those raises vary from locality to locality based on how federal and nonfederal salaries compare in each. The first locality adjustments, in 1994, averaged 3.95 percent and represented two-tenths of the amount needed to reduce pay gaps in 28 different areas to 5 percent. In 1995, and for the next seven years, the minimum adjustment equals one-tenth of the amount needed to reduce pay differences to 5 percent. The 1995 adjustment, which the government capped below the level authorized by FEPCA, averaged about 1 percent of pay (see Summary Table 2). The raise for 1996 under FEPCA would average 3.37 percent.

CONCERNS ABOUT LOCALITY PAY SURVEYS

The Bureau of Labor Statistics (BLS) conducts sophisticated pay surveys in support of FEPCA. Efforts by private-sector firms are often less elaborate. Nevertheless, critics over the years have charged that BLS surveys fail to reflect accurately the experience outside the federal government. (BLS also collected the data used in comparisons for the national pay system that preceded FEPCA.) In response to such concerns, BLS has repeatedly adjusted its methodology and plans further refinements, resources permitting.

To answer criticisms that its surveys are not broad enough, BLS has repeatedly added jobs and has expanded the number of industries and small firms included in the surveys. (A job, for purposes of this discussion, is a position in an occupation and at a given level--for example, entry-level secretary.) In 1979, BLS surveys produced data for 21 occupations covering 89 different jobs. By contrast, the survey

SUMMARY TABLE 2. GENERAL SCHEDULE EMPLOYMENT AND PAY GAPS, WITH 1995 LOCALITY PAY RAISES AND MINIMUM AND MAXIMUM SALARIES

Location	General Schedule Employment (Percent)[a]	Pay Gap (Percent)	1995 Locality Pay Raise (Percent)[b]	Salary (Dollars)[c] Minimum	Salary (Dollars)[c] Maximum
Atlanta	1.8	25.82	0.77	12,707	92,442
Boston	1.7	36.14	1.42	12,987	94,482
Chicago	1.9	35.92	1.50	12,981	94,438
Cincinnati	0.5	28.81	1.07	12,788	93,034
Cleveland	0.8	23.92	0.86	12,655	92,062
Columbus	0.7	28.67	2.14	12,784	93,007
Dallas	1.3	30.26	1.38	12,827	93,316
Dayton	1.2	28.18	1.37	12,771	92,910
Denver	1.7	30.68	1.16	12,839	93,405
Detroit	1.0	34.43	1.67	12,941	94,147
Houston	0.9	43.13	1.89	13,177	95,860
Huntsville	1.0	24.60	0.28	12,674	92,204
Indianapolis	0.8	25.44	0.87	12,697	92,371
Kansas City	1.3	22.74	0.65	12,623	91,833
Los Angeles	3.3	38.03	1.61	13,038	94,853
Miami	0.7	29.07	2.23	12,795	93,087
New York	4.3	37.63	1.45	13,027	94,774
Philadelphia	2.6	32.96	1.24	12,901	93,855
Portland	0.7	26.06	1.57	12,713	92,486
Richmond	0.6	22.87	0.88	12,627	91,859
Sacramento	0.8	28.56	1.52	12,781	92,981
St. Louis	1.5	24.14	1.15	12,661	92,106
San Diego	1.3	32.42	2.18	12,886	93,749
San Francisco	2.4	41.38	1.85	13,129	95,516
Seattle	1.7	31.09	1.85	12,850	93,484
Washington, D.C.	21.1	29.50	1.20	12,806	93,166
Rest of United States	42.2	21.73	0.63	12,595	91,629
Total United States	100	27.53	1.05	12,655	95,860

SOURCE: Congressional Budget Office using data provided by the Office of Personnel Management.

a. These data show employment in each locality as a percentage of total General Schedule employment excluding workers in Alaska and Hawaii and others not eligible for locality raises.

b. These raises are the capped levels granted under spending limits adopted in 1994.

c. Minimum salaries are for grade 1, step 1, of the General Schedule. Maximum salaries are for grade 15, step 10. Those salaries reflect locality adjustments and raises based on the employment cost index, but not special rates or interim geographic differentials. In New York and Los Angeles, interim geographic differentials push the maximum rate to about $95,400.

conducted for the 1995 locality adjustment produced data for 25 occupations and 107 jobs. Surveys for FEPCA also responded to a long-standing criticism by collecting pay data from state and local governments. The benefits of further refining the locality surveys, however, must be weighed against the added costs and complexity.

CONCERNS ABOUT HOW THE GOVERNMENT COMPARES JOBS

The pay system helps to set the salaries at each grade of the General Schedule, and the classification system assigns jobs to each grade based primarily on the duties and responsibilities each job entails. If, as critics contend, many employees hold jobs with grade assignments not justified by the work they do, workers will be over- or underpaid by these practices.

No one knows how often such misclassification occurs. The only recent information on the subject comes from Department of Defense (DoD) audits conducted by the Army and the Navy. For the years 1989 through 1992, data from more than 3,500 audits show that 2.0 percent of positions were overgraded and 1.3 percent were undergraded. (An overgraded job is at a higher grade than warranted by the work involved, and an undergraded job is at a lower grade.) The DoD figures are much lower than those in a 1983 study by the Office of Personnel Management that estimated that 14.3 percent of the GS workforce was overgraded and 1.5 percent was undergraded.

The government has a number of alternatives in dealing with misclassification. If the problem is more widespread than suggested by DoD's studies, it may require using a lower level of nonfederal work for purposes of setting locality raises. That action could have a significant impact on the pay increases granted to all employees. For example, if the government concluded that widespread overgrading warranted lowering by one level the nonfederal work used to set federal salaries, the pay gap could be reduced by between 15 and 20 percentage points.

If the problem of misclassification is not widespread, the government might be better served to leave the pay system alone and instead correct individual cases of misclassification as it finds them. That approach would primarily affect employees in misgraded jobs. The government could, for example, move jobs to the correct grade. In the case of downgrading, however, the government would experience no near-term savings because current statutes protect the grade and pay of downgraded employees for two years. Rather than change grades in cases of misclassification, the government could simply add or subtract duties and responsibilities to justify

existing grade assignments. Of course, in any complex organization, one would expect a certain number of misclassifications. Some agencies, most notably the Department of Defense, already routinely audit positions and correct misclassification. If classification errors are as low as indicated in DoD audits, the question arises whether the problem merits any additional resources and attention.

CONCERNS ABOUT HOW THE GOVERNMENT APPLIES LOCALITY RAISES

Under FEPCA, all employees in an area receive the same percentage locality raise based on the difference between the average federal salary and the average nonfederal salary in the area. In other words, the government combines information for grades and occupations to come up with one raise for all employees. Under that system, employees at some grades and occupations in an area will have salaries that are higher or lower than those of their nonfederal counterparts. FEPCA requires that raises be comparable only on average.

Current practice generally will overpay employees in lower grades and less skilled jobs, relative to similar employees outside the government, and underpay employees in higher grades and more skilled occupations. The Congressional Budget Office's (CBO's) analysis suggests that over the long run, about 13 percent of the workforce will receive salaries that exceed comparability by more than 10 percent, and about 17 percent will be shortchanged by more than 10 percent.

The government could significantly reduce such over- and underpayments. Many observers have recommended having a national system for professional and administrative workers and a locality system, similar to current practice, for clerical and technical workers. Other arrangements are possible. In fact, putting all professional workers into a separate, national pay system could significantly improve the efficiency of pay setting in government. The government would have to weigh the advantages of further disaggregation of the system, however, against the added complexity and cost.

ALTERNATIVES TO CURRENT PRACTICE

If granted in full, raises under FEPCA would push the federal payroll to about $110 billion by 2000. With federal deficits projected to continue into the foreseeable future, pressures to limit this growth in salaries will probably remain unabated even in the absence of concern about pay-setting practices. Accordingly, CBO has prepared estimates of alternatives to current practices. The government could accompany those options with reforms in pay surveys, job classification, and other aspects of pay setting. Such measures, as described above, could improve the

effectiveness of the pay system. Most would not, however, significantly alter the savings estimated for each option.

The estimated savings indicate how much less the government would spend under each option than it would by granting full raises under FEPCA (see Summary Table 3). The government would have to adopt much greater limits on pay and

SUMMARY TABLE 3. PAY RAISES AND OUTLAY SAVINGS UNDER ALTERNATIVES TO CURRENT LAW, 1996-2000

	1996	1997	1998	1999	2000	Cumulative Five-Year Totals
Option I: Grant No Raises in 1996						
ECI Raises (Percent)	0	3.20	3.10	3.00	3.00	12.88
Locality Raises (Percent)	0	6.05	3.96	2.65	2.68	16.20
Savings (Billions of dollars)	3.18	2.91	1.59	1.15	1.00	9.83
Option II: Grant Only ECI Raises						
ECI Raises (Percent)	2.90	3.70	3.60	3.50	3.50	18.42
Savings (Billions of dollars)	1.32	2.87	4.32	5.83	7.63	21.97
Option III: Grant Only Locality Raises						
Locality Raises (Percent)	3.37	2.59	3.96	5.10	5.65	22.42
Savings (Billions of dollars)	1.21	3.37	4. 94	5.64	5.95	21.11
Option IV: Target Locality Raises Toward the Most Underpaid Workers						
ECI Raises (Percent)	2.40	3.20	3.10	3.00	3.00	15.59
Locality Raises (Percent)	8.11	3.63	3.34	3.34	3.34	23.64
Savings (Billions of dollars)	0.16	0.74	1.44	2.21	3.14	7.68

SOURCE: Congressional Budget Office.

NOTES: The pay raises described are the average increases in pay for employees who receive them. Actual increases in federal payroll would be less because some employees--for example, those who receive special pay rates designed to help the government recruit and retain employees--do not always receive locality adjustments.

ECI = employment cost index.

employment if it wants to reduce pay below some current level rather than just limit its growth.

Under the first alternative to current practice, the government would forgo raises in 1996. That approach would save $10 billion over five years and would represent only a temporary departure from current practice. Under Option II, the government would abandon the current system of locality pay and grant only ECI-based raises. That option would save $22 billion over five years but would mean abandoning the principle of comparability. Federal salaries would keep abreast of changes in rates of nonfederal pay, but they would never catch up to that level of pay. The option would appeal to people who criticize the current locality pay system.

A less dramatic departure from current practice is embodied in Option III, under which the government would grant only locality pay raises. Pay would still reach comparability, but some of the raises necessary to get there would shift to later years. Savings would accumulate to $21 billion over five years. Finally, under Option IV, the government would grant locality raises only to employees whose salaries are far below those in the private sector. If, for example, the government granted raises only to employees in occupations it designates as professional (the group with the largest pay gaps), five-year savings would accumulate to $8 billion. That approach would direct scarce federal resources to where they were needed most.

CHAPTER I
INTRODUCTION

Pay and benefits for the government's 2 million civilian employees will total about $110 billion in 1995.[1] Salaries paid to employees account for about $90 billion of that amount, representing about 6 percent of all federal expenditures.

Pay continues to be a target for reduction as part of efforts to limit federal spending and reduce federal budget deficits (see Box 1). For 1994 and 1995, the government limited pay raises authorized under the Federal Employees Pay Comparability Act of 1990. FEPCA provides for annual pay raises that would eventually move salaries for most federal white-collar workers toward comparability with nonfederal rates that prevail in different localities. The first of those comparability pay raises occurred in 1994.

The reforms introduced by FEPCA have not escaped criticism. Much of the criticism, moreover, is a continuation of that directed at the national system that preceded FEPCA. Critics often cite problems with pay-setting practices in government to support further reductions in federal pay. This paper examines three common concerns about how the government determines and applies pay raises. The analysis suggests that some concerns may be overstated and that others lend themselves to solutions other than limiting pay. Even in the absence of problems with FEPCA, however, federal pay would probably not escape consideration in the government's continuing struggle with budget deficits. Accordingly, this paper also describes the budgetary and other consequences of further limiting federal pay raises.

FEDERAL EMPLOYMENT AND PAYROLL

The federal payroll, which includes wages and salaries, nearly tripled between 1975 and 1994, rising from $30 billion to $86 billion (see Table 1). The average salary during the period rose from $13,700 to $39,400. That increase reflects not only the pay raises granted to federal employees but also the shifts in the occupational mix of the workforce.

1. Unless otherwise indicated, this analysis covers civilian employees only--that is, employees outside the uniformed military services. The analysis also excludes employees of the U.S. Postal Service, who numbered about 800,000 in 1994. Postal employees are covered by a pay system that is separate from that of other civilian employees and funded by revenue from the sale of stamps rather than federal taxes.

By contrast, employment in government has remained fairly stable. After increasing by 4 percent between 1975 and 1985, the federal workforce then declined by the same amount, returning in 1994 to about the level of almost two decades earlier (see Table 1). Recent reductions at the Department of Defense (DoD) are largely responsible for the decline since 1985. Overall, the relative stability in federal employment reflects the efforts of successive Administrations to improve the efficiency of government operations and reduce the size and scope of federal activities.

The federal system represents a large and highly complex undertaking. The 2 million government workers account for about 2 percent of all workers in the United States. Federal employees work in 850 different occupations, more than 100 different agencies direct their efforts, and dozens of pay plans govern their wages and salaries.

Within this complexity, however, are several defining characteristics. Just three federal agencies, for example, employ about 6 of every 10 federal civilian workers and account for 56 percent of the federal payroll--the Department of Defense, the Department of Veterans Affairs, and the Department of the Treasury (see Table 2). Although its workforce has declined in recent years, DoD remains the largest federal agency, employing about 4 of every 10 federal civilian workers and accounting for about 37 percent of the federal payroll.

BOX 1.
RECENT PROPOSALS BY THE PRESIDENT
TO CONTROL FEDERAL PERSONNEL COSTS

President Clinton has targeted federal personnel costs for reduction in each of his budgets. The President's proposals have sought to curtail the growth in payroll and other personnel expenses through cuts in federal employment and limits on federal pay raises.

In his 1996 budget, the President proposes limiting pay raises to 2.4 percent. Although the Administration does not allocate this amount between the two annual raises authorized for federal civilian employees under the Federal Employees Pay Comparability Act of 1990 (FEPCA), the level of the proposed raise is well below the combined increase that would occur under the act. If implemented, this cap on pay raises would continue what has become an annual event. The government limited raises under FEPCA in both 1994 and 1995.

The President's budget also proposes to continue reductions in federal employment mandated by the Federal Workforce Restructuring Act of 1994. Limits in the act would reduce federal employment to 1.88 million through 1999. Those reductions build upon others authorized in earlier Presidential memorandums. According to estimates in the President's budget, federal employment through 1995 will have fallen by 121,000 below the 1993 level of 2.14 million.

In addition, the federal workforce is largely white-collar (see Table 3). About 8 of every 10 employees in the executive branch hold jobs in white-collar occupations such as secretary, engineer, and accountant. Those workers accounted for about 88 percent of the federal payroll in 1994. A table of salary rates, referred to as the General Schedule, governs the pay of most of those workers. Blue-collar workers, in jobs such as plumber and electrician, make up about 15 percent of federal employment and account for about 12 percent of the federal payroll. DoD employs most federal blue-collar workers (80 percent of the government total).

EMPLOYMENT AND PAYROLL COVERED BY THE GENERAL SCHEDULE

The General Schedule (GS) is the government's primary pay plan, covering 76 percent of the workforce. This pay plan was the main focus of reform under FEPCA. Employees covered by the General Schedule hold white-collar jobs that range from clerical positions to highly trained professional positions. The government bases pay for those workers on comparisons with salaries in the private sector and in state and local governments. The payroll for full-time GS employees totaled $57 billion for 1994. (See Appendix A for a description of the government's other major white-collar pay systems.)

TABLE 1. FEDERAL CIVILIAN EMPLOYMENT AND PAYROLL, 1975-1994

				Percentage Change		
	1975	1985	1994	1975-1985	1985-1994	1975-1994
Employment (Thousands of workers)	2,173.3	2,267.5	2,179.2	4	-4	a
Payroll (Billions of dollars)	29.8	60.8	85.9	104	41	188
Average Salary (Dollars)[b]	13,700	26,800	39,400	96	47	188

SOURCE: Congressional Budget Office using data provided by the Office of Personnel Management.

NOTE: Data cover all three branches of government and all work schedules. Employment figures represent averages of monthly totals.

a. Less than one-half of one percent.

b. Growth reflects pay raises and shifts in the occupational mix of the workforce.

The General Schedule Workforce

The General Schedule workforce is highly educated and highly skilled. About 80 percent hold jobs in occupations designated professional, administrative, or technical (see Table 4). Among the larger job categories in those occupational groups are engineering and engineering support, nurse and medical technician, and computer specialist. About 17 percent of all GS workers hold clerical jobs.

As the problems with which government is asked to deal have become larger and more complex, the portion of the workforce in higher-skilled occupations has grown (see Table 4). In 1980, about 48 percent of the GS workforce held jobs in professional and administrative occupations. By 1993, the share in such jobs had increased to 55 percent. The workforce has also become more highly educated. In 1980, 35 percent of the GS workforce had earned a bachelor's or higher degree. For 1993, the figure stood at 46 percent. The trend toward a more educated federal workforce has surpassed the trend for the United States as a whole; in 1993, only 27 percent of the U.S. civilian labor force had four years of college or more, up from 22 percent in 1980.

TABLE 2. FEDERAL CIVILIAN EMPLOYMENT AND PAYROLL BY AGENCY, 1994

	Employment		Payroll	
	Thousands of Workers	Percentage of Total	Billions of Dollars	Percentage of Total
Legislative Branch	36.9	2	1.6	2
Judicial Branch	27.9	1	1.3	1
Executive Branch				
Department of Defense	900.3	41	32.1	37
Department of Veterans Affairs	264.2	12	9.1	11
Department of the Treasury	159.7	7	6.5	8
Other agencies	790.2	36	35.4	41
Subtotal	2,114.4	97	83.0	97
Total	2,179.2	100	85.9	100

SOURCE: Congressional Budget Office using data provided by the Office of Personnel Management.

NOTE: Data cover all three branches of government and all work schedules. Employment figures represent averages of monthly totals.

What Is the General Schedule?

The General Schedule, according to which the government pays the employees described above, consists of 15 pay grades. Each grade has a salary range divided into 10 salary steps. The federal government assigns jobs to a grade on the basis of the duties and responsibilities involved. Under this system, lesser-skilled jobs are in the lower grades and higher-skilled jobs in the upper grades. Most mail and file clerks, for example, are at GS grades 3, 4, and 5; most aerospace engineers are at GS grades 12, 13, and 14. The practice of assigning pay levels on the basis of a job's duties and responsibilities contrasts with the practice in other white-collar federal pay plans of determining pay levels based primarily on individual accomplishments (see Appendix A).

Progress up the 10 salary steps at each grade depends largely on length of time spent in a grade. Employees generally progress to GS steps 2, 3, and 4 after one year of satisfactory service, to the next three steps after two years of satisfactory service,

TABLE 3. FEDERAL CIVILIAN EMPLOYMENT AND PAYROLL BY PAY PLAN, 1994

	Employment		Payroll	
	Thousands of Workers	Percentage of Total	Billions of Dollars	Percentage of Total
Blue-Collar	287.8	15	9.0	12
White-Collar				
Executive pay	8.2	a	0.9	1
Foreign Service	13.5	1	0.8	1
Doctors and nurses at Veterans Affairs	42.2	2	2.2	3
General Schedule	1,474.6	76	56.6	76
Other white-collar	114.1	6	5.3	7
Subtotal	1,652.7	85	65.9	88
Total	1,940.5	100	74.8	100

SOURCE: Congressional Budget Office using data provided by the Office of Personnel Management.

NOTE: Data cover employees in the executive branch and those on full-time work schedules. Employment figures are totals as of March 1994.

a. Less than one-half of one percent.

and to steps 8, 9, and 10 after three years. (Agencies may grant accelerated advances for outstanding performance.) Step increases generally boost pay by about 3 percent. Promotions move employees from grade to grade.

Under the Federal Employees Pay Comparability Act of 1990, pay at any given grade will vary from area to area depending on how federal and nonfederal rates compare. The base salaries--that is, the salaries before any locality pay is factored in--range from $12,141 for a GS grade 1, step 1, to $88,326 for a GS grade 15, step 10 (see Table 5). With locality adjustments, the top salary of the General Schedule may reach as high as $95,860. Other special pay supplements designed to help the government recruit and retain workers push the figure even higher. Grade 10 is roughly the median GS grade.

Growth of the General Schedule Payroll

Between 1985 and 1994, the GS payroll grew by more than 50 percent. About 60 percent of that growth reflected pay raises granted to most GS workers. Those raises

TABLE 4. OCCUPATIONAL DISTRIBUTION AND EDUCATIONAL ATTAINMENT OF GENERAL SCHEDULE WORKERS, SEPTEMBER 1980 AND SEPTEMBER 1993

Occupational Group	Percentage of General Schedule Workforce		Percentage of General Schedule Workforce with Bachelor's or Higher Degree	
	1980	1993	1980	1993
Professional	22	28	86	87
Administrative	26	27	44	60
Technical	22	25	13	14
Clerical	28	17	5	7
Other	3	3	7	11
All Occupations	100	100	35	46

SOURCE: Congressional Budget Office using data provided by the Office of Personnel Management.

NOTE: Data cover employees in the executive branch and those on full-time work schedules.

totaled more than 30 percent, which was less than the increase in both private-sector salaries and inflation for the same period. Federal GS employment, which grew by about 2 percent, contributed to only about 4 percent of the growth in payroll over the 1985-1994 period. Shifts in the distribution of jobs toward higher grades, primarily reflecting the greater share of workers employed in professional, administrative, and other higher-skilled jobs, contributed another 20 percent to the growth in pay. The average grade during the period increased from 8.4 to 9.3.

Most of the remaining growth reflects a rise in the average step of the workforce, the proliferation of special pay rates, and the implementation of geographic differentials in pay. Special rates are salaries higher than those in the General

TABLE 5. PAY AND EMPLOYMENT OF THE GENERAL SCHEDULE WORKFORCE

Grade	Salary Range (Dollars)[a]	Percentage of General Schedule Workforce[b]
1	12,141 to 15,183	c
2	13,650 to 17,174	c
3	14,895 to 19,368	2
4	16,721 to 21,734	7
5	18,707 to 24,323	11
6	20,852 to 27,107	7
7	23,171 to 30,119	10
8	25,662 to 33,357	3
9	28,345 to 36,850	10
10	31,215 to 40,584	1
11	34,295 to 44,582	14
12	41,104 to 53,434	16
13	48,878 to 63,539	11
14	57,760 to 75,085	6
15	67,941 to 88,326	3
All Grades	12,141 to 88,326	100

SOURCE: Congressional Budget Office using data provided by the Office of Personnel Management.

a. Salaries are those that became effective in January 1995. They are base rates that do not reflect locality pay differentials or other supplements to pay designed to boost the government's efforts to recruit and retain employees.

b. Data cover full-time executive branch workers as of March 1994.

c. Less than 1 percent.

Schedule that are intended to help the government to recruit and retain employees for certain jobs in certain areas. The Office of Personnel Management sets them based on requests from agencies. The number of employees receiving special rates rose from 47,000 in 1985 to about 189,000 in 1994. Geographic differentials, authorized by FEPCA, are supplements to General Schedule salaries primarily for employees in New York and Los Angeles. Those differentials were intended as a temporary measure to help agencies to recruit and retain employees while the government phased in comparability. Employees receiving either special rates or geographic differentials will not receive locality pay adjustments (see discussion below) until such adjustments push GS salaries over the rates those employees currently receive.

PAY RAISES UNDER THE GENERAL SCHEDULE

As just described, general increases in salaries contributed significantly to the growth of the total GS payroll. (A general increase refers to one that affects the pay of most workers. Employee pay may also rise because of promotions or increases in step, but those are not general increases for purposes of this discussion.) Under FEPCA, the government may make two such increases in the salaries of the General Schedule every January. The basic principle that federal employees should receive salaries comparable with those paid outside the federal government for the same work guides both increases. The first increase helps to keep federal salaries abreast of most changes in private-sector wages and salaries as measured by the employment cost index (ECI). The second raises federal salaries, in nine annual installments, to roughly the level of nonfederal salaries for comparable work. In other words, the adjustment based on the ECI helps to keep federal salaries from falling any farther behind, and the second adjustment helps them, over a period of years, to catch up. The government thus far has a spotty record in granting the full raises authorized by FEPCA. Raises it has granted to date under the act have increased salaries for most employees by an average of about 7 percent.

Adjustments Based on the ECI

Under FEPCA, when the government adjusts federal salaries to reflect changes in the ECI, it grants the same percentage to all eligible employees, regardless of location. The increase granted, according to the formula set out in law, equals the percentage increase in the ECI over a 12-month period minus one-half of one percentage point. The 12-month reference period occurs long before the raise takes effect, ending in September--15 months before the date of the pay raise. For example, the raise scheduled for January 1996 is based on changes in the ECI from the third quarter of 1993 through the third quarter of 1994.

The government canceled the first ECI-based raise scheduled for January 1994. Had it granted the raise, federal salaries would have risen by 2.2 percent. For 1995, the government granted a raise of 2.0 percent rather than the full 2.6 percent allowed by FEPCA. The full raise scheduled for 1996 would, if granted, raise federal salaries by 2.4 percent.

Locality Pay Increases

In contrast to adjustments based on the ECI, pay raises designed to help federal salaries catch up to nonfederal salaries vary from area to area. Generally, the size of an adjustment in an area depends on the size of the gap between the average federal and nonfederal salaries in that area. (The term pay gap, as used here, refers to the percentage by which federal salaries would have to rise to meet the level of their nonfederal counterparts.)

Under FEPCA, locality adjustments occur only in areas where nonfederal salaries exceed federal salaries by more than 5 percent. Such pay disparities, however, are not remedied all at once. The law establishes a schedule of minimum pay raises designed to close a specific portion of the pay gap each year and from which the President may deviate only under specific circumstances.[2] Those minimum raises would reduce any pay gap in an area to 5 percent over nine years.

For 1994, the schedule of minimum raises set out in FEPCA required the government to grant locality raises designed to close 20 percent of the targeted pay gap. (The targeted pay gap is the percentage increase in federal pay that would bring it to within 5 percent of nonfederal pay.) The locality raises for the 28 pay localities established by the government for 1994 averaged 3.95 percent, based on pay gaps that ranged from 21 percent to 39 percent.

For 1995, FEPCA calls for closing an additional 10 percent of the targeted pay gap so that, together with the 1994 adjustment, the government would have reduced differences in pay by 30 percent. (Adjustments in subsequent years would also close 10 percent of the pay gap.) Legislation enacted late last year (the Treasury, Postal Service, and General Government Appropriations Act of 1995), however, imposed a cap on the 1995 adjustment by restricting the amount that the government could spend on locality raises for the year to the equivalent of 0.6 percent of the civilian, executive branch payroll. Under that formula, adjustments through January 1995 would close about 24 percent of the pay gap.

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2. In the future, the President may set a locality adjustment at a level below the minimum set in law when a national emergency occurs or serious economic conditions exist. Nothing in the law prevents the President from granting bigger raises.

TABLE 6. GENERAL SCHEDULE EMPLOYMENT AND PAY GAPS, WITH 1995 LOCALITY PAY RAISES AND MINIMUM AND MAXIMUM SALARIES

Location	General Schedule Employment (Percent)[a]	Pay Gap (Percent)	1995 Locality Pay Raise (Percent)[b]	Salary (Dollars)[c] Minimum	Salary (Dollars)[c] Maximum
Atlanta	1.8	25.82	0.77	12,707	92,442
Boston	1.7	36.14	1.42	12,987	94,482
Chicago	1.9	35.92	1.50	12,981	94,438
Cincinnati	0.5	28.81	1.07	12,788	93,034
Cleveland	0.8	23.92	0.86	12,655	92,062
Columbus	0.7	28.67	2.14	12,784	93,007
Dallas	1.3	30.26	1.38	12,827	93,316
Dayton	1.2	28.18	1.37	12,771	92,910
Denver	1.7	30.68	1.16	12,839	93,405
Detroit	1.0	34.43	1.67	12,941	94,147
Houston	0.9	43.13	1.89	13,177	95,860
Huntsville	1.0	24.60	0.28	12,674	92,204
Indianapolis	0.8	25.44	0.87	12,697	92,371
Kansas City	1.3	22.74	0.65	12,623	91,833
Los Angeles	3.3	38.03	1.61	13,038	94,853
Miami	0.7	29.07	2.23	12,795	93,087
New York	4.3	37.63	1.45	13,027	94,774
Philadelphia	2.6	32.96	1.24	12,901	93,855
Portland	0.7	26.06	1.57	12,713	92,486
Richmond	0.6	22.87	0.88	12,627	91,859
Sacramento	0.8	28.56	1.52	12,781	92,981
St. Louis	1.5	24.14	1.15	12,661	92,106
San Diego	1.3	32.42	2.18	12,886	93,749
San Francisco	2.4	41.38	1.85	13,129	95,516
Seattle	1.7	31.09	1.85	12,850	93,484
Washington, D.C.	21.1	29.50	1.20	12,806	93,166
Rest of United States	42.2	21.73	0.63	12,595	91,629
Total United States	100	27.53	1.05	12,655	95,860

SOURCE: Congressional Budget Office using data provided by the Office of Personnel Management.

a. These data show employment in each locality as a percentage of total General Schedule employment excluding workers in Alaska and Hawaii and others not eligible for locality raises.

b. These raises are the capped levels granted under spending limits adopted in 1994.

c. Minimum salaries are for grade 1, step 1, of the General Schedule. Maximum salaries are for grade 15, step 10. Those salaries reflect locality adjustments and raises based on the employment cost index, but not special rates or interim geographic differentials. In New York and Los Angeles, interim geographic differentials push the maximum rate to about $95,400.

The average locality raise for the 27 pay localities established for 1995 amounted to about 1 percent, based on pay gaps averaging 27.5 percent (see Table 6). Adjustments ranged from 0.3 percent to 2.2 percent. The average increase under FEPCA for 1996 is 3.37 percent.[3]

3. The pay increases reported here differ slightly from those presented by the Federal Salary Council. The council, which prepares recommendations for pay increases among other things, reports percentage-point increases in pay. The figures used by the Congressional Budget Office are percentage increases in pay.

CHAPTER II

ISSUES IN MAKING PAY COMPARABLE FOR GENERAL SCHEDULE WORKERS

Using salaries outside government as a guide in setting federal rates is not new. The Federal Salary Reform Act of 1962 established comparability as the guiding principle in setting pay. Comparability, supporters contended, would help to ensure the government's ability to attract and retain the employees needed to carry out government programs. The act ended a long period of haphazard adjustments to federal salaries. The Federal Pay Comparability Act of 1970 reaffirmed federal policy and established a methodology and procedures for adjusting rates of pay.

Under the comparability system that preceded the most recent reform (the Federal Employees Pay Comparability Act of 1990), a single pay scale provided a uniform pay range at each grade of the General Schedule nationwide. Under that system, a grade 4 secretary in Washington, D.C., had the same salary as a grade 4 secretary in Syracuse, New York. As under current practice, the system relied on surveys of salaries outside the federal government but made no distinctions by geographic area.

Primarily for budgetary reasons, the government capped most raises granted under the old system below the levels needed to achieve comparability. In fact, not one raise granted after 1977 was at the full level. Moreover, the government applied the same reduced raises to all grades regardless of the size of the pay gap at a grade. Consequently, the pay gap by the late 1980s had grown to about 30 percent on average, with much larger gaps for the upper grades and for some professional and other occupations.

With pay gaps growing, concern mounted about the government's ability to recruit and retain workers, and calls for reform became more frequent. Reforms embodied in FEPCA were intended to achieve a number of objectives. The act reaffirmed the importance of comparability in ensuring the government's ability to compete for labor. To minimize the budgetary impact of establishing comparability, the adjustments were to be made over many years. In implementing locality pay and thereby moving away from a single national pay scale, the act allowed for some response to local differences in labor markets. The act also provided for long-urged reforms of government pay surveys.

Nevertheless, FEPCA has not escaped criticism. Many of the concerns surrounding the former national system are also being raised about the locality

system. The President himself has expressed reservations about the methodology for determining pay raises adopted under FEPCA.[1]

This paper addresses three long-standing issues: how the government collects data on nonfederal salaries, how it matches jobs for purposes of comparison, and how it applies locality raises once they have been set. Reforms in FEPCA have addressed some complaints about the government's pay program, and other complaints may be overstated. Despite its problems, the current system represents one of the largest, most sophisticated, and most complex adopted by an employer to ensure fair and competitive salaries. The benefits of further refinements must be weighed against added costs and complexity.

CONCERNS ABOUT PAY SURVEYS

Salary data collected by the Bureau of Labor Statistics (BLS) has helped to determine comparability raises under both the current system and its predecessor. Those surveys have been the subject of considerable concern over the years. Current surveys incorporate a number of reforms, and BLS plans further improvements.

BLS Surveys and the Computation of Pay Gaps

The Bureau of Labor Statistics has for years conducted surveys of wages and salaries for use by both business and government. For FEPCA, BLS has combined and modified two established surveys--the Area Wage Surveys and the White-Collar Pay Surveys. Surveys for the 1995 locality raise cover establishments with 50 or more workers. The firms surveyed represent all nonagricultural industries, including communications, construction, finance, retailing, and transportation. Surveys also cover state and local governments.

Under current procedures, survey experts visit establishments and collect data for jobs they find that correspond to official descriptions of federal jobs included in the survey. The experts use the same descriptions in all geographic areas. The Office of Personnel Management (OPM) develops those descriptions, in collaboration with BLS, on the basis of official job standards that set out the duties and responsibilities of most jobs in government. Federal employees, however, may or may not actually perform at the level put forth in the job descriptions used in the pay surveys. BLS tests descriptions to ensure their relevance to work performed outside the federal government. BLS gathers data at various points in time; OPM

1. Executive Office of the President, *A Vision of Change for America*, report accompanying the President's address to the Joint Session of the Congress (February 17, 1993), p. 85.

then uses the employment cost index to adjust, or "age," the data to a date that corresponds to federal pay on the date used in comparisons. (The ECI aging factor covers wages and salaries for white-collar workers, excluding those in retail sales.)

BLS collects data for only a sample of the more than 450 federal white-collar occupations. Surveys for the 1995 locality raise cover 25 different occupations spanning 107 different jobs. Those jobs represent about 30 percent of the General Schedule workforce. (In this discussion, a job refers to work of a given level in an occupation--for example, entry-level secretary. Occupations in a BLS survey often cover several levels of work. Generally, work levels correspond to grades of the General Schedule.) BLS could not find acceptable data for all jobs in any of the areas surveyed. Only 19 jobs produced publishable data in all areas, according to OPM (see the discussion below). The government established 27 pay areas for the 1995 locality adjustment.

OPM uses a three-step process to collapse the nonfederal data on various jobs into the single average used in estimating a pay gap for each locality. First, it calculates a single average nonfederal salary for each group of similar occupations at a grade. For example, the salaries for the technical jobs at grade 3 would become a single average salary. The figure calculated is a weighted average. The weights the government uses reflect nationwide (continental United States) federal employment for the grade and occupation, not local federal employment. Using nationwide federal weights at this point in the calculation permits the use of more of the nonfederal data the government collects.[2]

Next, OPM collapses the averages for all occupational groups in a grade into a single weighted average for that grade, based on local federal employment. Finally, the average at each grade is collapsed into a single weighted average for the locality based on the grade distribution of federal employment in the area. Table 7 illustrates the process by which data on a set of jobs in a locality are combined into a single average.

2. The government does not have federal employees in every surveyed job in each area. In such cases, there is no local federal employment to use as a weight. Thus, if the government chose to use local weights in the initial stages of its calculations, it would not always have all the weights it needed and could not always use all the nonfederal data it collected. Retaining a broad mix of data is important because each surveyed job represents itself and all similar jobs. Excluding data could lead to results that are not representative. Subsequent stages in the calculations cover broader categories of workers for which the government is more likely to have local employment data to use as weights.

TABLE 7. ILLUSTRATION OF THE THREE-STEP PROCESS FOR CALCULATING A SINGLE AVERAGE NONFEDERAL SALARY USING DATA FOR A SET OF JOBS

	Number of Federal Employees	Average Nonfederal Pay (Dollars)
Step 1. Use National Federal Employment Data to Combine Nonfederal Salaries for a Set of Jobs into a Single Average for Each Occupational Group[a]		
Grade 3		
Clerical occupations		
Account clerk II	81	18,811
Word processor I	3,079	19,348
Total	3,160	19,334
Technical occupations		
Drafter I	2	23,863
Engineer technician I	15	23,326
Total	17	23,389
Grade 4		
Clerical occupations		
Account clerk III	426	23,164
Word processor II	14,405	23,110
Secretary I	6,772	20,853
Total	21,603	22,404
Technical occupations		
Drafter II	34	28,002
Engineer technician II	172	22,143
Total	206	23,110
Step 2. Use Local Federal Employment Data to Combine Occupational Averages into Averages for Each Grade[b]		
Grade 3		
Clerical occupations	77	19,334
Technical occupations	14	23,389
Total	91	19,958
Grade 4		
Clerical occupations	398	22,404
Technical occupations	115	23,110
Total	513	22,562
Step 3. Use Local Federal Employment Data to Combine the Grade Averages into a Single Average for All Grades[c]		
Grade 3	91	19,958
Grade 4	513	22,562
All Grades	604	22,170

SOURCE: Congressional Budget Office.

NOTE: This illustration covers only some of the jobs and grades used in actual calculations. The roman numerals after occupations indicate the level of work. A level I job, for example, generally indicates an entry-level position.

a. Employment data reflect the nationwide total at the grade and job indicated.

b. Employment data reflect local employment in each grade and occupational group.

c. Employment data reflect local employment in each grade.

To compute the pay gap, OPM compares the single weighted average for each locality with the federal average salary for the area. Pay gaps and locality raises are part of the annual report to the President from the Pay Agent.[3]

Coverage of Nonfederal Jobs in BLS Pay Surveys

The most persistent concerns about pay comparability in government are those having to do with pay surveys, particularly their coverage. Adequate and balanced coverage ensures that the survey results accurately represent the nonfederal experience the government attempts to match under FEPCA. If, for example, BLS surveys covered only high-paying industries and jobs, or if BLS was able to find reliable data only for such industries and jobs, then estimates of the pay gap would overstate differences in salaries.

Many difficult issues arise in putting together locality pay surveys. An ongoing concern is finding data that meet BLS's standards for publication and statistical reliability for the many jobs surveyed in each locality. Surveys conducted for the 1995 locality adjustment produced usable data for about two-thirds of the jobs surveyed. The range of jobs used, according to OPM, runs from a low of 47 in Albuquerque, New Mexico, to a high of 97 for the area designated "Rest of United States." The government supplements raw survey data with data generated by a multiple regression model of nonfederal pay that makes salary a function of area, occupational group, and grade. Under that approach, data are available in each geographic area for all jobs used in pay comparisons.

Whether the federal survey covers a sufficient number of jobs has also been of concern to critics. Under current practice, BLS chooses a job for its survey if the job has a large federal representation and if it will produce an adequate amount of suitable data from nonfederal sources. Based on data collected for the 1994 locality adjustment, the jobs included in pay surveys covered directly about 37 percent of the GS workforce at the lower five grades, 21 percent at the middle grades, and 33 percent at the top five grades.

Over the years, BLS has responded to concerns about coverage by repeatedly adding jobs and by substituting jobs or revising job descriptions to increase the amount of publishable data yielded. In addition, it adopted changes designed to expand the number of industries surveyed and to cover more small firms. In 1979, for example, BLS surveys covered firms with a minimum of 50, 100, or 250

3. The President's Pay Agent is the Secretary of Labor and the Directors of the Office of Personnel Management and the Office of Management and Budget.

employees, depending on the industry. Surveys for that year produced data for 21 occupations covering 89 different jobs. By 1990, the minimum firm size had been lowered to 50 employees for all industries, and surveys had been expanded to include 32 occupations covering 147 jobs. The 26 occupations and 110 jobs covered by the first locality pay survey represent a reduction from the 1990 level, but BLS continues to plan for the expansion of the survey as resources permit. The first locality survey for FEPCA also responded to a long-standing concern of critics by covering state and local governments for the first time.

CONCERNS ABOUT MATCHING JOBS IN PAY COMPARISONS AND THE POSITION CLASSIFICATION SYSTEM

The process for comparing jobs has also been an issue for many years. Under current and past practices, the government collects data on nonfederal salaries for jobs that correspond to official descriptions of federal work. Under such a plan, mispayments will occur if the actual duties of federal employees do not correspond to official descriptions. Employees whose job involves less responsibility than it is supposed to will be overpaid, and employees with more responsibility will be underpaid. How often such misclassification of jobs occurs is uncertain. Reforming the system used to rank and classify jobs, however, would be a more appropriate response to the problem than changing the pay system, unless misclassification is widespread and uniform.

The General Schedule Classification System

In the federal system, pay comparisons help to establish the salary range at each grade of the General Schedule, and the federal classification system assigns the different jobs in government to those grades. As previously described, grade assignments primarily reflect duties and responsibilities; for example, computer analyst jobs that involve supervisory responsibility generally rate a higher grade than those that do not. The classification system plays an essential role in achieving comparability between federal and nonfederal salaries. Pay surveys and other practices under FEPCA may produce a salary for GS grade 6 that accurately reflects nonfederal experience at that grade, but if some federal jobs assigned to that grade do not involve the level of work expected--that is, they are misclassified--employees in those jobs will be over- or underpaid.

The current federal GS classification system began with the Classification Act of 1949. In addition to grade, that system determines pay plan, occupational group, and job title. Agency managers and classifiers have primary responsibility for classifying positions. OPM provides oversight and direction. The basic objectives

of the system are to provide equal pay for equal work, ensure fair differences in pay for unequal work, and offer a systematic approach to organizing federal jobs.

In assigning grades, agency classifiers use official position classification standards prepared by OPM that describe the duties, responsibilities, scope of command, and other factors that should be associated with each job at each grade. The government uses those standards in preparing the job descriptions used in pay surveys. Such standards help to achieve some consistency in decisions about job classifications.

Increases in Average Grade

From March 1985 to March 1994, the average grade for full-time employees under the General Schedule increased by about one grade, from 8.4 to 9.3. That pattern continues a long-term upward trend: in 1975, the average GS grade was 7.9, more than a grade below the current level.

Many factors have contributed to the increase in the average grade of the GS workforce. Determining the actual size of each factor's contribution is difficult, but analysis by OPM suggests that the changing nature of governmental work accounts for over half of the increase. As described in Chapter I, federal agencies rely increasingly on professional and administrative workers, who generally have higher grades than workers in other occupations. That emphasis reflects an increase in both the size and complexity of the demands placed on government.

Several other factors may have contributed to grade increases. One is the government's routine reclassification of jobs to reflect changes in the nature of work the jobs involve. Also, the increased reliance on contracting with the private sector for goods and services has heightened the government's need for well-trained professionals to prepare and monitor contracts while shifting some lesser-skilled positions to private contractors. Misclassification, too, may have contributed to the overall rise in average grade.

Misclassification of Federal Jobs

Analyses by the Office of Personnel Management, the National Academy of Public Administration, and others have revealed some problems with misclassification of federal jobs. Those studies found both overgrading and undergrading (jobs assigned to a grade above or below that justified by the duties and responsibilities performed). The problems with misclassification, however, were not found to be very widespread.

How do jobs end up at the wrong grade? Some misclassification may result from simple errors by classifiers. Jobs may also become misclassified during reorganizations or reductions in employment. Grade assignments may not keep abreast of the changes in mission and scope of command that often accompany such efforts. Managers who feel that the low federal salaries of recent years have made it difficult to recruit and retain workers may also overstate a position's responsibilities to a obtain a higher grade and pay. Finally, the classification standards for a position may simply no longer reflect, in general, the nature of the work they intend to describe.

In a 1983 analysis, OPM estimated that 14.3 percent of the GS workforce was overgraded and 1.5 percent was undergraded.[4] That analysis involved audits conducted in 1980 and 1981 of more than 700 GS full-time permanent positions selected at random.

No one knows the current extent of overgrading. On the one hand, successive limits on federal pay raises may have increased pressures on managers to overgrade jobs to get higher pay for employees. At the time of the 1983 OPM report, the President's Pay Agent estimated the pay gap at around 20 percent--well below the current level of 28 percent. In addition, the many recent reorganizations and reductions in employment may have contributed to overgrading. On the other hand, the tight budgets of recent years may have, in some cases, made it harder for agencies to bear the costs of overgrading. Special pay rates, geographic differentials, and similar measures, moreover, may have reduced pressures to use the classification system to boost the pay of federal workers.

The only current data available on misgrading come from surveys done by the Department of Defense as part of its annual evaluations of personnel management. Though limited in scope, those annual reviews suggest that the incidence of overgrading is no higher than in 1983 and may have actually decreased dramatically. For the years 1989 through 1992, for example, audits of 3,534 positions in the Army and the Navy show that 2.0 percent of the workforce was overgraded and 1.3 percent was undergraded.

Costs of Misclassification in Government

When a job is overgraded, the government pays more for the work it receives than it would if the job was correctly graded. Overgrading also overstates the cost of

4. Office of Personnel Management, *Federal White-Collar Position Classification Accuracy* (March 1983). See also Congressional Budget Office, *Changing the Classification of Federal White-Collar Jobs*, CBO Paper (July 1991).

reaching pay comparability under FEPCA. Estimating overall costs is problematic, however, because the extent of overgrading in government is unclear.

The Congressional Budget Office's analysis suggests that each percent of overgrading costs government the equivalent of 0.15 percent of payroll. That estimate assumes that misgraded positions occur proportionately among grades and that positions are overgraded, on average, by one work level. (For most jobs in government, a work level corresponds to a grade; for jobs in professional and administrative occupations, a work level corresponds to two grades.)

The CBO estimate compares the salaries of federal workers at the wrong grade with those of workers at the correct grade. Compared with workers outside the federal government, however, overgraded workers may not be overpaid at all. From that perspective, the cost of misclassification appears insignificant against the savings the government realizes by paying salaries that are, on average, so far below comparability. Nevertheless, accurate classification remains important for ensuring the fairness, efficiency, and credibility of the pay system.

Correcting the Classification of Federal Jobs

The government has several alternatives in dealing with the misclassification of federal jobs. Should the problem prove much more widespread than suggested by available data, some basic adjustments in the process for comparing pay may be warranted. Such an effort could involve reconsidering the level of nonfederal jobs the government has selected to compare with federal jobs. That would mean across-the-board changes in the locality raises federal employees would otherwise receive and could have a significant budgetary impact. For example, if the government concluded that widespread overgrading warranted lowering by one level the nonfederal work that is compared with federal work, the pay gap could fall by between 15 and 20 percentage points.[5]

If misclassification is not widespread, however, the government could more appropriately deal with the problem directly through the classification system, correcting individual instances of error as it finds them. Under that approach, the primary impact would be on misclassified jobs, with a limited impact on near-term federal spending.

5. However the government chooses to address the problem of misclassification, translating any reductions in spending for salaries into near-term deficit reduction would require lowering the caps the government has set on overall spending. Without such action, Congressional committees and agencies could reallocate savings to other priorities.

The most direct method of dealing with misclassification is to move employees to the correct grade. In the case of downgrading, however, current statutes protect the grade and pay of workers, thus delaying savings to the government. Under those statutes, downgraded workers keep their same grade and pay for at least two years. Thereafter, workers whose salaries exceed the highest salary at the correct grade receive only half of the requlars pay adjustment until the top salary at the correct grade catches up. The government could eliminate or cut back protection of grade and pay, but such action would lower employee morale. And the prospect of a disrupted workplace might make federal managers reluctant to downgrade jobs at all.

As an alternative to changing grades, agencies can adjust the duties and responsibilities of a job to justify the current grade. No reductions in spending occur under this approach, but it often proves less disruptive and may make more sense for the day-to-day operation of an agency and for meeting demands for services. Some agencies, most notably DoD, already routinely try to find and correct errors in classification. Current efforts to reduce employment and reorganize government offer agencies a special opportunity to reallocate duties and responsibilities from jobs they have eliminated.

Errors in classification could increase, however, if agencies do not ensure that grade assignments stay current with work assignments. The Congress could encourage agencies to focus more attention on the accuracy of job classifications in its oversight hearings, but correcting misclassification entails costs. If the incidence of misclassification is as low as was suggested in DoD's audits, it probably does not merit the commitment of significant additional resources. However, even current levels of effort devoted to accurate classification may be threatened because federal employees who do that type of work are probably among the midlevel administrative staffs targeted for reduction under downsizing and reorganization plans. Of course, the Congress could always consider basic reform of the classification system, which offers the potential for benefits beyond enhanced accuracy. One approach would be to simplify the current grade structure (see Appendix B).

CONCERNS ABOUT HOW THE GOVERNMENT APPLIES LOCALITY RAISES

In establishing salary schedules and granting pay raises, the federal government has consistently relied on average rates that apply to a large variety of occupations and, in the case of the system that preceded FEPCA, to all geographic areas. Accordingly, some federal salaries will be higher or lower than corresponding salaries outside government. Federal systems have required that federal salaries be comparable with nonfederal salaries only on average. The practice of averaging pay raises has not caused the government to spend more or less, overall, than it would have otherwise;

in averaging, losses to some employees equal gains to others. Rather, the concern is primarily that some employees receive a larger or smaller piece of the pay-raise pie than necessary to ensure comparability with employees in similar jobs outside the federal government.

FEPCA has addressed part of the problem of over- and underpayments. Locality pay under FEPCA maintains the principle of comparability but also allows for local variation in rates. The new system, however, still groups occupations at each grade that often have widely varying rates of pay in the private sector. Thus, problems of over- and underpayment remain.

Consider, for example, the case of Oklahoma City, Oklahoma. In January 1994, GS salaries there increased by a uniform percentage to close partially an average pay gap estimated at 22.53 percent. (CBO prepared this analysis long before the tragic events in that city.) Yet data indicate that pay gaps varied greatly by grade within the area. Average differences in Oklahoma City ranged from an overpayment of 1 percent for grade 2 to an underpayment of 37 percent for grade 15 (see Table 8). Within grades, survey data reveal even wider disparities in pay. At grade 5, for example, pay differences ranged from an underpayment of 49 percent for professional occupations to an overpayment of 1 percent for the far more numerous clerical workers. Thus, the locality adjustment for 1994 fell short of the amount needed to move the salaries of federal professional workers toward comparability with those of their nonfederal counterparts. It also greatly exceeded the amount necessary to move clerical workers to comparability.

The pattern in the data for Oklahoma City is not unique. In general, current pay practices mean that employees in lower grades and less skilled occupations will generally receive pay raises above the amount necessary to reach pay comparability with similar workers outside the federal government, and employees in higher grades and occupations requiring greater skills will receive raises below the amount for comparability.

Governmentwide Impacts of Current Averaging Practices

To illustrate the widespread nature of over- and underpayment and the potential long-term consequences of current practice, CBO developed a scenario in which the government closed the entire locality gap in each region all at once. Under that scenario, the current system's practice of granting a flat, average raise to all workers regardless of grade or occupation would cause the pay of many professionals and similar employees to fall short of comparability by amounts that accumulate to 3.6

TABLE 8. PAY GAPS FOR OKLAHOMA CITY BY GRADE AND OCCUPATIONAL GROUP (In percent)

Grade	Occupation				
	All	Professional	Administrative	Technical	Clerical
1	n.a.	n.a.	n.a.	n.a.	n.a.
2	-1	n.a.	n.a.	n.a.	-1
3	11	n.a.	n.a.	28	4
4	12	n.a.	n.a.	14	11
5	6	49	10	17	-1
6	8	n.a.	n.a.	14	a
7	17	41	10	25	15
8	16	n.a.	n.a.	n.a.	17
9	19	39	8	28	n.a.
10	n.a.	n.a.	n.a.	n.a.	n.a.
11	21	32	17	20	n.a.
12	26	39	14	n.a.	n.a.
13	32	41	22	n.a.	n.a.
14	27	39	20	n.a.	n.a.
15	37	36	n.a.	n.a.	n.a.
All Grades	23	38	15	22	5

SOURCE: Congressional Budget Office using data for the 1994 locality pay raise provided by the Office of Personnel Management.

NOTES: The abbreviation n.a. indicates that data were not available, either because no employees had the grade and occupation indicated or because no nonfederal data could be found.

A minus sign indicates an overpayment--that is, the percentage by which federal salaries exceed nonfederal salaries.

a. Less than one-half of one percent.

percent of payroll, and pay for many less skilled employees would rise above comparability by the same overall amount.[6]

What effect would closing the full comparability gap have on federal workers? More than 1 million employees (about two-thirds of the GS workforce) hold jobs in occupations that would receive raises that, on average, exceeded the amount

6. CBO's estimate of 3.6 percent is based on data for the 1994 pay adjustment and represents the sum of the differences between the pay raises employees in 28 areas and five occupational groups would receive and the raises that would be needed to achieve comparability for each group in each area. Take, for example, an area with 100 professionals with payroll representing 1 percent of the total U.S. payroll. If those employees have a pay gap of 20 percent and would receive pay raises of 15 percent, CBO would count 100 employees as ending up short of comparability by 0.05 percent of payroll. Data on pay gaps, payroll, and employment by area and occupational group are from the Office of Personnel Management.

necessary to achieve comparability with their nonfederal counterparts. Of those 1 million employees, most of whom are in technical and clerical occupations, more than 200,000 would receive raises that, on average, were more than 10 percent above the level needed to achieve comparability. Conversely, over 400,000 employees, most of them in professional occupations, would receive less than the amount needed for comparability with workers in similar occupations. Almost 300,000 of them would be left short, on average, by 10 percent or more. Such data suggest that the current locality system recognizes differences in pay among regions but fails to address substantial, and sometimes greater, differences in pay among grades and occupations.

Granting Locality Raises by Grade or Occupational Group

Given the diversity and complexity of the federal workforce, no practical comparability system could match pay outside the federal government job for job. Most alternatives suggested over the years incorporate some grouping of workers for purposes of determining and granting pay increases. The current system groups by locality, but other groupings might permit closer matching of salaries and thus enhance federal efforts to hire and keep the workers it needs.

As an alternative to current practice, the government could amend FEPCA to allow for variation in raises by grade or some combination of grade and occupation. Most alternatives could be structured to represent simple redistributions of amounts that the government would otherwise have granted in raises and would therefore have no significant budgetary consequences. For example, if the government had differentiated raises in 1994 by occupational group and had held the average pay adjustment constant, employees in professional and other higher-skilled jobs would have received generally larger raises and those in clerical and other less skilled occupations would have received generally smaller raises. Based on data for 1994, raises for employees in jobs designated professional would have averaged 6.1 percent, and raises for employees in jobs designated clerical would have averaged 1.6 percent.

How might the government have allocated raises differently? In a 1989 study, the Wyatt Company reported that a survey of private-sector firms found that nearly all have nationwide pay systems for managers, professionals, and scientific positions.[7] Under such a system, for example, chief accountants would have the same pay scale across the country. According to the survey, firms use local labor markets to set pay primarily for technicians and clerical workers. A 1989 study by

7. Wyatt Company, *Study of Federal Employee Locality Pay* (Philadelphia: Wyatt Co., July 1989).

TABLE 9. COMPARISON OF OUTCOMES UNDER FULL COMPARABILITY FOR TWO PAY SYSTEMS

	Percentage of Payroll Misdirected[a]	Percentage of General Schedule Employees with Pay More Than 10 Percent: Below Comparability	Above Comparability
Current Locality-Based Pay System	3.6	17	13
Locality Pay System with Separate National System for Professional Occupations	1.7	1	11

SOURCE: Congressional Budget Office using data for 1994 provided by the Office of Personnel Management.

a. Misdirected payroll is the percentage of payroll that goes to over- and underpayments.

OPM offers some support for adopting a similar arrangement for federal employees.[8] In that study, OPM found that private-sector salaries for professional and administrative workers are more uniform among geographic areas than salaries for technical and clerical workers--suggesting some advantage in having a national system for the former group and a locality-based system, similar to current practice, for the latter group. Of course, other alternatives are possible. In fact, CBO's analysis suggests that the government could significantly improve the efficiency with which it allocates pay raises simply by taking employees in professional occupations out of the current system and establishing a separate national pay plan for them. (Other workers would remain, as a group, under the current locality-based system.)

A number of observations support the notion of having a separate national pay system for professionals. That group experiences less geographic variation in pay gaps than do other occupational groups. Professionals also account for almost all workers who receive pay raises that, under current practice, are well below the level necessary to match the salaries of professionals outside the federal government. Removing professional workers would also lower raises for employees remaining in the locality-based system and would thus reduce overpayments for the clerical workforce and others. For 1994, such a system would have produced a raise for professional workers averaging about 6 percent. Raises for all other employees

8. Office of Personnel Management, *Federal White-Collar Pay Systems: Report on a Market-Sensitive Study* (August 1989). For a summary of earlier proposals for reforming the federal pay system, see Robert W. Hartman, *Pay and Pensions for Federal Workers* (Washington, D.C.: Brookings Institution, 1983), pp. 77-106.

would have averaged about 3 percent. In addition, the portion of payroll misdirected under full comparability would drop to 1.7 percent from 3.6 percent under the current system (see Table 9). A definitive answer to the question of how best to allocate pay raises would require detailed information not currently available. CBO's analysis intends to show only that better arrangements are possible.

In addition to offering the chance to match salaries more closely, allowing for more alternatives in granting pay raises would facilitate consideration of other job market indicators, such as application rates, when setting pay. But having more alternatives would present practical problems. For example, with more differentiation in pay setting comes greater cost and complexity. The greater the level of disaggregation, moreover, the greater the difficulty in finding enough nonfederal data on which to base reliable comparisons. Finally, the more emphasis that is given to occupational groups or grades in setting pay, as opposed to geographic area or other factors, the smaller the raises are for employees at the low end of the job hierarchy, where women and minorities are represented in significant numbers. The benefits of further refinements to pay setting must be weighed against such costs.

CHAPTER III

THE COST OF FUTURE PAY RAISES UNDER CURRENT LAW AND ALTERNATIVES

With budget deficits projected to continue into the foreseeable future, the pay of federal employees will probably remain a target of efforts to reduce spending even in the absence of concern about the pay system. Accordingly, the Congressional Budget Office has prepared projections of costs under the current system and savings under several alternatives. The alternatives to current law all involve broad caps on federal raises--one of the more direct approaches to achieving large savings in pay costs.

Any of the options set forth below could be accompanied by changes in pay surveys, job classification, or the method of allocating raises among areas and occupations. As previously described, such reforms could improve the effectiveness of whatever level of raise the government granted and could offer other advantages. They would also significantly affect the raises some employees would otherwise receive. Most such reforms, however, would not markedly alter the savings estimates described for each option.

Under the first alternative, the government would grant no raises in 1996. That approach produces significant savings with only a temporary departure from current practice. The second alternative would abandon the process of comparing salaries in different localities and would instead grant across-the-board raises tied to the employment cost index. That action would reduce costs compared with those under current practice and would appeal to many critics of the locality pay system. The third option would leave the current system in place but would delay some of the raises under current law. The benefit of that approach is largely budgetary. The final option considers the impact of granting locality pay raises only to workers in occupations for which salaries are far behind the private sector, thereby directing federal resources to where they are needed most.

The savings estimated for different alternatives to current practice show how much the government would save--that is, by how much less spending would grow--compared with granting full raises under the Federal Employees Pay Comparability Act. To reduce the payroll below some current level rather than simply limit future growth as the four options do, the government would have to adopt limits on pay and employment that are much more severe than those considered here.

The savings estimates, which were derived using the pay model described in Box 2, assume that the current gap between federal and nonfederal salaries is 27.5

BOX 2.
CBO'S MODEL FOR ESTIMATING FEDERAL PAY COSTS

The Congressional Budget Office's (CBO's) model for estimating nonpostal civilian pay costs is designed to give quick and coherent answers to the types of questions most frequently asked by policymakers. The model is versatile enough to depict the effects of current law and many suggested alternatives. CBO actually employs two models--one for the Department of Defense and another for all civilian agencies. Both work in much the same manner.

CBO begins with a pay base and employment levels in the current or previous year. The pay base encompasses direct wage and salary payments--base salary plus overtime and other premium pay--to full- and part-time employees. It is augmented by agencies' costs for selected benefits (chiefly contributions to retirement plans) that move up or down with pay scales. CBO relies largely on object class data (information collected by the Office of Management and Budget describing agency obligations by the nature of the good or service obtained) for figures on direct pay and applies its own assumptions about retirement coverage and contribution rates.

The pay base must be split into many pieces. The General Schedule covers about three-fourths of both employees and payroll, but many other systems exist, each with its own statutory language governing pay raises. For the executive branch alone, CBO distinguishes among General Schedule, Wage Board, Veterans Administration medical, Foreign Service, revolving fund, uniformed (Coast Guard and Public Health Service), Executive Schedule, "other senior" (mainly Senior Executive Service), and "all other" personnel. A special category--foreign national indirect hires--is relevant only for the Defense Department and is often omitted from federal employment and payroll totals. The legislative and judicial branch payrolls are split into the (relatively small) amounts going to Members of Congress and judges, and the (much greater) amounts going to rank-and-file employees of the House and Senate, the legislative support agencies, and the court system. Despite gaps in the data, the resulting dollar figures are satisfactory though far from perfect.

CBO projects future pay costs simply by taking each initial pay base and adjusting it by three factors: changes in the level of employment, effective across-the-board raises, and effective locality raises. Other factors--such as changes in the skill mix or other composition of federal employment--are absent, not because they are irrelevant but because CBO seldom has solid information on which to base assumptions.

Unless otherwise specified, employment levels in the executive branch through 1999 are assumed to match the full-time-equivalent employment limits enacted in the Federal Workforce Restructuring Act of 1994. Across-the-board raises for most groups under current law are pegged to the growth in the employment cost index minus one-half of a percentage point. Current law grants locality raises only to General Schedule employees, although similar raises have also been given to other personnel. Locality raises are linked to the estimated gap between federal and nonfederal salaries in many areas; CBO combines them into a nationwide average. For both types of raises, several factors--such as salary caps, the exclusion of interim geographic adjustments, and many special rates granted in the first rounds of locality raises--can drive a wedge between the announced raise and the effective raise. CBO uses the effective raise in its estimates. The most common requests requiring CBO to use the model involve paring across-the-board raises, locality raises, or both.

Under current law, pay raises occur in January, three months into the federal fiscal year. Thus, CBO applies a timing factor of 0.75 to gauge the cost of a pay raise in its first year, unless a proposal specifically calls for a different schedule. An exception is Wage Board personnel, whose raises are staggered throughout the year depending on their area.

percent. The estimates cover all three branches of government and reflect the savings from reductions in federal employment under the Federal Workforce Restructuring Act of 1994. They also reflect the impact of the pay raises on the General Schedule payroll and the payroll of white- and blue-collar pay plans linked to the General Schedule.

The amounts represent net savings to the government--that is, savings reduced to reflect contributions to federal retirement systems. (Those contributions are transfers between federal budget accounts that do not affect federal outlays.) Locking in deficit reduction by limiting pay raises, however, would require lowering caps on discretionary spending. Short of such action, savings from smaller pay raises for federal employees could be applied to other priorities--with no reduction in federal deficits.

FUTURE PAY RAISES UNDER CURRENT LAW

If the government adopted no limits on pay and granted the full raises authorized by FEPCA, ECI-based adjustments would accumulate to 16 percent of pay and locality raises to 14 percent of pay over five years (see Table 10). Those raises would cost $64 billion over five years and push the annual federal payroll to about $110 billion by 2000. Costs in 1996 would total $3 billion, assuming an ECI-based adjustment of 2.4 percent and an average locality adjustment of 3.4 percent.

A number of arguments support granting full raises. Federal employees have already sacrificed abundantly on behalf of deficit reduction. Before FEPCA, the raises the government granted in most years were well below the full level provided for under law. Under the new system established by FEPCA, battles over the size of raises have already become an annual occurrence.

Further limiting the pay of federal employees raises questions of fairness and workers' morale. Motivating employees and preserving their morale would seem particularly critical now as those spared by employment cutbacks take on the work of their departed colleagues while they attempt to cope with the growing workload of many programs. In fact, one wonders how long the government can continue to meet its expanding obligations in some areas, such as law enforcement, if it continues to simultaneously limit pay, reduce employment, and as proposed by some analysts, limit the use of contracts with private firms--the only means other than federal employees that the government has for delivering mandated services.

The government's need to recruit and retain workers also argues for full pay raises. Uncompetitive federal salaries and the associated problems agencies had in

TABLE 10. PAY RAISES AND THEIR COSTS UNDER CURRENT LAW, 1996-2000

	1996	1997	1998	1999	2000	Cumulative Five-Year Totals
Cost (Billions of dollars)	3.18	7.87	12.63	17.37	22.65	63.68
ECI Raises (Percent)	2.40	3.20	3.10	3.00	3.00	15.59
Locality Raises (Percent)	3.37	2.59	2.37	2.42	2.47	13.93

SOURCE: Congressional Budget Office.

recruiting and retaining workers gave rise to FEPCA in the first place. Yet systematic evidence of either widespread recruitment and retention problems in government, or the absence thereof, does not exist. And critics have noted that other conditions of federal employment--such as generous benefits, job security, and the chance to serve the public--can offset the effects of comparably low federal salaries. (Given recent downsizing and the proposals to cut federal retirement benefits, arguments about superior federal benefits and job security carry less force.) From that perspective, pay does not have to be comparable to be competitive. A 1992 survey by the General Accounting Office, in fact, confirms that many factors other than pay influence federal employees' decisions to stay in government.[1]

Nevertheless, salary undeniably plays a role in federal recruitment and retention efforts. Studies by both the Merit Systems Protection Board and the General Accounting Office demonstrate that pay holds a key place in decisions to join or stay in federal service--especially among the best and the brightest.[2] Repeated limits on federal pay cannot help but make federal service unattractive to ever increasing portions of the labor force and, at some point, will impose unacceptable burdens on agencies that need competent workers to get jobs done. Special rates and other similar measures help, but at the cost of fragmenting the federal pay system and greatly increasing its complexity.

Recent developments place a premium on the government's ability to compete for employees. The government needs talent to help support the reinvention of

1. General Accounting Office, *How Federal Employees View the Government as a Place to Work*, GAO/GGD 92-91 (June 1992).

2. Merit Systems Protection Board, *Why Are Employees Leaving the Federal Government?* (May 1990); and General Accounting Office, *Comparison of Applicants Who Accepted or Declined Federal Job Offers*, GAO/GGD 92-61 BR (March 1992).

government and other reforms and to help it in its increasingly difficult task of doing more with less. The government also needs to prepare to replace the large number of experienced workers expected to retire beginning around the turn of the century. Future conditions in the labor market could make competitive salaries even more important. Reports by the Office of Personnel Management warn that beginning early in the next century, the number of college graduates will decline even as the demand for skilled workers increases.[3]

OPTION I: GRANT NO RAISES IN 1996

If the government decides to try to limit costs under FEPCA, one option would be simply to skip raises for one or more years. Granting no raises in 1996, for example, would save $3 billion for the year and $10 billion over five years (see Table 11).

Limiting the growth of federal salaries may generally be viewed as part of an overall belt-tightening brought on by federal budget deficits. Such constraints on spending are not confined to the federal government; financially strapped firms in the private sector and local governments have been forced to cut personnel costs through layoffs, pay limits, or other measures.

This option represents a more temporary departure from FEPCA than some of the others described here. Federal salaries would still reach comparability, but some of the raises required to get there would not be given until after 1996. That outcome occurs because granting no adjustments in a year can generally be expected to produce higher pay gaps, and thus higher locality raises, in later years.

Should the government choose to skip raises, it would not be the first time. In 1986, out of concern for continuing high deficits, the government granted no general pay increase.

OPTION II: GRANT ONLY ECI RAISES

As another alternative to current practice, the government could do away with locality pay and grant only a raise tied to changes in the ECI. Such action would reduce the government's costs below what it would otherwise spend under FEPCA by $22 billion over five years. The estimate assumes annual pay raises accumulating to 18 percent over the period. Savings in 1996 would total $1 billion assuming a pay raise of 2.9 percent.

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3. Office of Personnel Management, *Federal Staffing Digest* (April 1991); and OPM, *Civil Service 2000* (June 1988).

TABLE 11. PAY RAISES AND OUTLAY SAVINGS UNDER ALTERNATIVES TO CURRENT LAW, 1996-2000

	1996	1997	1998	1999	2000	Cumulative Five-Year Totals
Option I: Grant No Raises in 1996						
ECI Raises (Percent)	0	3.20	3.10	3.00	3.00	12.88
Locality Raises (Percent)	0	6.05	3.96	2.65	2.68	16.20
Savings (Billions of dollars)	3.18	2.91	1.59	1.15	1.00	9.83
Option II: Grant Only ECI Raises						
ECI Raises (Percent)	2.90	3.70	3.60	3.50	3.50	18.42
Savings (Billions of dollars)	1.32	2.87	4.32	5.83	7.63	21.97
Option III: Grant Only Locality Raises						
Locality Raises (Percent)	3.37	2.59	3.96	5.10	5.65	22.42
Savings (Billions of dollars)	1.21	3.37	4. 94	5.64	5.95	21.11
Option IV: Target Locality Raises Toward the Most Underpaid Workers						
ECI Raises (Percent)	2.40	3.20	3.10	3.00	3.00	15.59
Locality Raises (Percent)	8.11	3.63	3.34	3.34	3.34	23.64
Savings (Billions of dollars)	0.16	0.74	1.44	2.21	3.14	7.68

SOURCE: Congressional Budget Office.

NOTES: The pay raises described are the average increases in pay for employees who receive them. Actual increases in federal payroll would be less because some employees--for example, those who receive special pay rates designed to help the government recruit and retain employees--do not always receive locality adjustments.

ECI = employment cost index.

This particular approach to limiting federal pay recognizes, based on a long record of failure, that the government will probably never accept the full cost of providing federal salaries comparable with those offered by nonfederal employers. Federal rates on average would keep pace with rates offered by other employers, but they would never catch up. (To this end, the CBO estimate assumes that the government grants the full ECI raise rather than the reduced raises under FEPCA.)

Supporters of this approach would argue that maintaining federal salaries at below-market rates is a fair trade for the generous package of benefits that federal employees have. In their view, raising pay to comparability, along with generous benefits, would push federal compensation well above levels in the private sector. (If, however, the government proceeds with proposed cuts in retirement benefits and continues to limit federal salaries, it could eventually face a crisis in its ability to recruit and keep quality workers.) In abandoning the principle of comparability, moreover, the government could drop the costly and controversial annual surveys, the results of which it uses to calculate locality pay adjustments that it might not grant anyway. Agencies could continue to handle recruitment and retention problems with special pay rates and other measures. That treatment would further complicate an already complex system, but it would also promote the kind of flexibility and decentralized control advocated by the National Performance Review.

Of course, the government would not have to abandon comparability raises forever. It could recommend annual surveys and adjustments at a later date when it deems budget conditions more favorable. Instead of using the current annual locality survey and adjustment process, the government could set up a system that provides for periodic review. Such a review could take many forms. For example, the government could, from time to time, appoint blue-ribbon panels of experts charged with developing recommendations for broad changes in basic federal salaries. Those panels could consider a variety of information, in addition to pay gaps, in making their recommendations. Such an approach would serve to mute criticism of the government's methods for comparing pay, criticism that has continued unabated despite repeated improvements in the methods. If such panels operated in full view of the public, with public hearings, they might also alleviate some of the concerns citizens have about excessive federal salaries.

OPTION III: GRANT ONLY LOCALITY RAISES

If the government discontinued ECI-based adjustments for most workers and instead granted only locality raises, five-year savings would accumulate to $21 billion. The estimated cost assumes cumulative annual locality adjustments of 22 percent. The savings in 1996 would total $1 billion, assuming locality raises averaging 3.4

percent. (The estimates assume that employees ineligible for locality pay raises would continue to receive ECI adjustments.)

This approach to limiting pay raises would represent less of a departure from current policy, if not practice, than granting only ECI-based adjustments. Federal salaries would still reach comparability by 2002, but as under Option I, some of the raises required to get there would occur later. Failure to grant ECI adjustments would widen the gap to be closed in later years, resulting in larger locality adjustments at that time. The option, in effect, would delay some of the costs of comparability, but it would preserve the notion that pay scales should differ in different labor markets.

OPTION IV: TARGET LOCALITY RAISES TOWARD THE MOST UNDERPAID WORKERS

Another alternative would grant locality pay raises only to federal employees whose pay is farthest behind that of their nonfederal counterparts. If, for example, the government granted locality raises only to professionals--the group with the largest overall pay gap--savings over five years would accumulate to $8 billion. (The estimate assumes that other workers would continue to receive ECI-based raises.) Locality raises for professionals would accumulate to 24 percent of pay through 2000.

This approach directs scarce federal resources to where they are needed most. Professional occupations have presented government with some of its most stubborn and persistent recruitment and retention problems. Data from the Office of Personnel Management suggest that the pay gaps for that group average about 40 percent.

This approach addresses only some recruitment and retention problems, however, and other problems would remain. Professionals, after all, make up only 22 percent of the white-collar workforce. Singling out only one group of workers for raises, moreover, would inevitably cause morale problems and raise questions of fairness. Targeting raises toward professional workers in particular would be cause for concern given that women and minorities are heavily represented in occupations that would not receive raises. Finally, if the government recommended locality raises for all workers at a later date, this option would represent merely a postponement of costs.

APPENDIX A

OTHER WHITE-COLLAR PAY PLANS

In addition to the General Schedule (GS), dozens of other pay plans cover civilian white-collar workers of the federal government. Many of those plans have links to the General Schedule. Pay for employees at the highest levels is governed mainly by the Executive Schedule or by rates set for members of the Senior Executive Service. Other significant white-collar pay plans include those covering the Foreign Service and medical personnel at the Veterans Health Administration of the Department of Veterans Affairs.

EXECUTIVE PAY AND EMPLOYMENT

Two plans govern the pay of most executives in government. The Executive Schedule and the rates set for the Senior Executive Service together cover about 8,200 employees with payroll representing about 1 percent of the total for all workers.

Employees at the very highest levels of government, such as cabinet secretaries, agency administrators, and chairs of boards and commissions, are paid according to the Executive Schedule. Most of those positions require appointment by the President. Executive Schedule employment totaled about 410 as of March 1994. Payroll for the group amounted to $49 million as of the same date.

The Executive Schedule consists of five levels. Salaries range from $108,200 for administrators, deputy directors, commissioners, and others at level V to $148,400 for cabinet-level positions at level I. Under authority of the Ethics Reform Act of 1989, pay for positions covered by the Executive Schedule and for Members of Congress and judges increases in January of each year. The first such adjustment occurred in January 1991. The adjustment equals the change in private-sector wages and salaries, as measured by the employment cost index (ECI), minus one-half of a percentage point. (The relevant measure for the January adjustment is how the ECI level for the October-through-December quarter ending 12 months earlier compares with the level of the corresponding quarter one year before that. The calculation for GS employees differs in that its reference point is the July-through-September quarter.) Employees on the Executive Schedule did not receive a raise in pay in 1994 or 1995.

Adjustments in pay for federal executives may also occur as a result of recommendations by the Citizens' Commission on Public Service and Compensation, a group that may be appointed every four years for the purpose of reviewing top salaries in government. After considering the commission's report, the President submits recommendations for changes in executive and other salaries for approval by the Congress.

Just below the agency heads and others covered by the Executive Schedule are members of the Senior Executive Service. The SES was established in 1979 under the authority of the Civil Service Reform Act of 1978. It covers managers and supervisors at the top of the career Civil Service. In fact, the SES was formed largely from positions once graded 16, 17, and 18 on the General Schedule. Most members of the SES are career employees who competed on merit for admission; the rest are political appointees. As of March 1994, SES employees numbered 7,800, with payroll totaling about $850 million.

Pay for members of the SES is set at one of six basic rates, depending on individual qualifications. That approach contrasts with the practice for employees covered by the General Schedule, whose pay primarily reflects the duties and responsibilities of the job assigned. Systems such as the SES that instead weight personal qualifications more heavily are often referred to as rank-in-person systems. The primary advantage of such systems is the flexibility they afford in assigning work. As the need arises, managers can assign employees at a given rank and pay to a variety of tasks.

The minimum basic rate of pay for the SES is the salary rate at grade 15, step 1, of the General Schedule times a factor of 1.20. The maximum rate may not exceed level IV of the Executive Schedule. Those basic rates of pay range from $92,900 at level 1 to $115,700 at level 6. The President may adjust the basic rates each January. In recent years, the adjustments have equaled those made to the Executive Schedule. No adjustment to basic rates was made in 1994 or 1995.

The government has, however, extended to the SES the locality adjustments granted to GS employees. Accordingly, the actual salary SES members receive varies from area to area. Pay with locality adjustments in Washington, D.C., for example, ranges from $97,991 at level 1 to $122,040 at level 6. Adjusted salaries may not exceed the salary at level III of the Executive Schedule. That limit has served to cap top SES pay in areas such as Houston, Texas, where locality raises were high.

In addition to salary, members of the SES may receive awards and bonuses based on performance. Total annual compensation--pay and bonuses--may not exceed the pay at level I of the Executive Schedule.

PAY AND EMPLOYMENT IN THE FOREIGN SERVICE

By tradition, the Congress has recognized the need in the conduct of foreign relations for a separate, flexible personnel system designed to ensure a highly trained and stable workforce. Current procedures for paying employees in the Foreign Service were established primarily by the Foreign Service Act of 1980. As described here, the Foreign Service covers chiefs of mission, members of the Senior Foreign Service (SFS), Foreign Service officers, and Foreign Service support personnel. Those employees, the majority of whom work for the Department of State, numbered about 13,500 as of March 1994, with payroll totaling about $790 million. Separate pay policies govern the various subgroups of the Foreign Service listed above and have links to policies in other pay systems.

Chiefs of mission, many of whom hold the title of ambassador, stand at the top levels of the Foreign Service. The President appoints them, and they may be chosen from the ranks of the career Foreign Service or from elsewhere. The current salaries of chiefs of mission are tied to levels III and IV of the Executive Schedule.

Management-level experts and others in foreign relations may belong to the Senior Foreign Service. Like the Senior Executive Service, the SFS is a rank-in-person system that bases pay primarily on individual qualifications. Basic salary rates for the SFS lie between the minimum and maximum rates for the SES. Employees stationed in the United States may also receive locality pay adjustments. In addition to salary, members of the SFS may receive awards and bonuses based on performance.

Almost 90 percent of the employees in the Foreign Service are either Foreign Service officers, who hold jobs such as personnel administrator and information analyst, or support personnel, who hold jobs such as secretary and clerk. Pay rates for this group of employees are set out in the Foreign Service Schedule. Similar to the General Schedule with its grades and steps, the Foreign Service Schedule consists of nine classes, each with 14 steps. The maximum salary for the highest class (class 1) is the same as that for a GS 15. The lowest pay for class 9 is linked to the minimum pay at GS 5. The Foreign Service, like the SES and the SFS, is a rank-in-person system in contrast to the General Schedule system.

PAY AND EMPLOYMENT FOR MEDICAL PERSONNEL AT THE DEPARTMENT OF VETERANS AFFAIRS

Doctors, dentists, optometrists, nurses, and other medical professionals at the Veterans Health Administration of the Department of Veterans Affairs (VA) also

have separate pay systems. As of March 1994, those employees numbered 42,200, with payroll totaling $2.2 billion.

The creation of an independent personnel system for this group dates back to 1946. Before that, medical personnel at the VA were included in the regular Civil Service with other employees. Supporters of a separate system for health professionals, like those who argued for a separate plan for the Foreign Service, hoped for more flexible policies and practices that would aid the recruitment and retention of better personnel. Though separate, the system at the VA has maintained some links to the General Schedule.

The system at the VA consists of a number of separate pay plans, each covering a different group of occupations. Policies and practices vary somewhat from plan to plan. All plans, however, share certain characteristics. The VA system, like the Foreign Service and the SES, determines pay primarily on the basis of individual accomplishment rather than duties and responsibilities. In addition, each plan in the system incorporates some element that adapts pay to conditions in local labor markets.

Doctors and dentists are paid according to a schedule consisting of seven grades, each with a minimum and maximum salary. The pay range at the lowest, or associate, grade corresponds to the pay at grade 11 of the General Schedule. The pay at the highest grade ranges from $79,684 to $98,960, which corresponds to the former grade 16 of the General Schedule (grades 16, 17, and 18 no longer exist). Rates rise with ECI adjustments to the General Schedule.

In addition to these basic salaries, doctors and dentists at the VA may receive special pay amounting to tens of thousands of dollars based on a variety of factors such as geographic location, length of service, and medical specialty. Special pay is intended to help to recruit and retain high-quality staff.

Optometrists, podiatrists, and physicians' assistants also have a graded pay schedule with minimum and maximum salaries. For podiatrists and optometrists the pay at the lowest and highest grades is linked to GS grades 11 and 15, respectively. For physicians' assistants, the linkage is to grades 6 and 15. These basic rates, like those for doctors and dentists, rise with ECI adjustments to the General Schedule.

Nurses have an independent locality pay system with rates and adjustments based on comparisons with nonfederal nurses in more than 150 localities. The surveys for those comparisons must be conducted at least once a year. Rates in 1994 ranged from a low of $20,400 for nurses at grade 1 stationed in the Philippines and other areas to a high of $135,200 for nurses at the top of grade 5 in Bedford, Massachusetts.

APPENDIX B

PAY BANDING AND REFORM OF THE CLASSIFICATION SYSTEM

Fundamental reform of the classification system offers an alternative to addressing specific incidents of incorrect grading. One approach consolidates the grades of the General Schedule (GS) into broad ranges of pay, or pay bands. Such a system involves fewer distinctions between types and levels of work. It therefore offers the advantages of simplicity and flexibility.

The report of Vice President Gore's National Performance Review urged that agencies adopt pay-banding systems. A 1991 report by the National Academy of Public Administration set out a design for such a system that could serve as a model for federal agencies.[1] In addition, the government is testing pay banding at a number of agency demonstration projects.

PAY BANDING AT THE NAVY DEMONSTRATION PROJECT

One of the longest running and most thoroughly evaluated pay-banding demonstration projects is being conducted by the Navy. The project, started in 1980, involves four naval laboratories. Two laboratories in California--the Naval Command, Control and Ocean Surveillance Center in San Diego and the Naval Air Warfare Center in China Lake--have adopted the new personnel system. Two others--the Naval Air Development Center in Warminster, Pennsylvania, and the Naval Surface Warfare Center in Dahlgren, Virginia, and White Oak, Maryland--made no changes, serving as controls for purposes of comparison.

At the Navy demonstration laboratories, which have 12,000 employees, pay bands substitute for more narrowly defined GS grades, and career paths of related occupations substitute for more specific GS occupational designations. Scientists, engineers, and others, for example, make up a career path consisting of several pay bands that cover a number of GS grades. Advancement up the salary range covered by each pay band depends on good performance on the job. (By contrast, length of satisfactory service determines progress up the pay range of the General Schedule.)

Classification at the demonstration laboratories involves assigning positions to a pay band representing a broadly defined level of difficulty rather than to a more

1. National Academy of Public Administration, *Modernizing Federal Classification: An Opportunity for Excellence* (Washington, D.C.: NAPA, 1991).

narrowly defined General Schedule grade. As such, the decisions involved in classifying work become less complex, and the potential for error and disagreement drops. Classifiers, for example, no longer have to concern themselves with the often subtle distinction between professional work at grades 12 and 13. The broad pay bands not only increase the range of salaries a laboratory can offer to new recruits but also afford employees the opportunity for greater growth in pay. Moreover, compared with the GS system, the broad pay bands provide a wider range of salaries within which to make performance-based pay distinctions. All those advantages offer the potential for agencies to improve recruitment and retention.

SOME RESULTS OF THE DEMONSTRATION PROJECT

The Navy demonstration project has simplified personnel administration and improved employees' attitudes. Results for the project's other objectives are less clear. For example, evaluators collected no data for either the productivity of lab operations or the quality of lab work on which to base an assessment of organizational effectiveness. No analysis, however, has identified any serious problems with the experimental personnel system. And the project's accomplishments appear to have been gained at negligible cost.

In considering the effects of the demonstration project, one must recognize that the Navy designed its experimental system to meet the specific recruitment and retention needs for two specialized facilities--laboratories employing large numbers of scientists and engineers. Generally, the work at the laboratories is more technical, the workforce more homogenous and professional, and the organizational structure less hierarchical than for other government operations. Pay-banding systems appropriate for other operations may vary from the one examined here and therefore have different outcomes. Some people argue that pay banding may not be appropriate for all government operations. From that perspective, such systems would represent an optional arrangement for selective application by agencies.

The Office of Personnel Management (OPM) has conducted extensive evaluations of pay banding and the Navy demonstration project.[2] Among other findings, OPM's analysis indicates that personnel administration has become simpler. Evaluators noted fewer complaints about classification. The hours that both supervisors and personnel staff spent on each classification action dropped, as did the number of classification actions and the rate of classification errors. (OPM compared the performance of the demonstration labs with their performance before installing the new personnel practices and with the performance of the control laboratories.)

2. See, for example, Office of Personnel Management, *Broad-Banding in the Federal Government*, Technical Report (1992).

Employees' satisfaction with work and pay also seems to have improved under the demonstration project. In 1989, for example, 49 percent of employees at the demonstration laboratories reported they were satisfied with their pay compared with only 32 percent at the control labs. Consistent with the demonstration project, the rates at which employees separated at the demonstration labs were generally lower and less erratic than at the control labs. The OPM data also offer some evidence that demonstration labs were more successful than the control labs at retaining employees who performed well on the job.

EFFECTS OF THE NAVY'S SYSTEM ON COST

Given the limited scope of the demonstration projects, estimates of the cost of more widespread use of pay banding in government would amount to speculation. The Navy's experience suggests that the potential benefits of pay banding are achieved at modest cost and that costs would not necessarily have to rise. The demonstration project has indicated where management and design can limit the costs of pay-banding systems.

Salary Growth at the Navy Demonstration Project

Data show that, overall, salaries at the demonstration labs grew faster than salaries at the control labs between 1979 and 1990--64 percent compared with 60 percent. Consequently, the average salary at the demonstration labs, which in 1979 was 0.15 percent higher than at the control labs, was about 2.5 percent higher in 1990.

Most of the extra growth in salaries at the demonstration labs, however, reflects an initial employee buyout--an increase in base salaries designed to make the transition to the new system easier for employees. Comparison of salary growth for the period after the buyout--1980 through 1990--shows an almost identical change in salary. Salary growth varied by occupational group; scientists and engineers at the demonstration labs showed the clearest advantages regardless of the period considered.

Of course, a variety of factors that may or may not have anything to do with the experimental pay-banding system could have influenced the results described above. Employment at the demonstration labs, for example, grew much faster than at the control labs. All else being equal, a large increase in new employees at entry-level salaries will limit any increase in average salary in an organization.

In an effort to account for such factors and to obtain a clearer picture of the effects of pay banding on salary growth, OPM also tracked the salaries of a group of

new employees hired in 1985. That analysis showed slower pay growth at the demonstration laboratories. For most of the occupational groups examined, salaries at the demonstration laboratories started out higher than those at the control laboratories but eventually fell behind because of smaller annual increases. For example, the salary for one group of professionals hired by the demonstration laboratories in 1985 was more than 20 percent higher than the salary for a similar group of new employees at the control laboratories. By 1990, salaries at the demonstration laboratories for this group had fallen 1 percent behind the salaries of the comparison group at the control laboratories. According to OPM, the demonstration laboratories have traded the more rapid increases that characterize the GS system for a system that offers higher starting salaries and, by virtue of banding grades together, the potential for greater, albeit slower, growth in pay. Higher starting salaries offer the opportunity to attract better candidates, and the promise of greater long-term career development raises the chance of keeping them.

Controlling the Costs of Pay-Banding Systems

The Navy's experience indicates how the management and design of pay-banding systems can influence costs. Such information offers a useful guide to any future expansion of the use of pay banding in government.

The structure of the transition to a pay-banding system, for example, appears to influence costs. OPM's analysis indicates that the Navy could have avoided some of the observed increase in average salaries at the demonstration labs by offering to buy out employees with one-time cash bonuses rather than granting permanent increases in base pay. In general, allowing the option of offering bonuses rather than increases in base pay will limit the costs of any pay-banding system. In addition, using a fixed pool of funds for pay increases, according to OPM, can serve to limit the rating inflation observed in other pay systems that base raises on performance. For example, OPM notes that in most years managers at the demonstration labs rated about half of all workers at the mean of a five-point performance rating scale. By contrast, 80 percent of employees under the former Performance Management and Recognition System received ratings above the mean in 1990.[3] Finally, managers can limit the costs of pay-banding systems when they use the flexibility inherent in such systems to make better use of staff. They could, for example, use temporary workers where appropriate, or they could substitute technical assistants for professional staff.

3. The Performance Management and Recognition System based federal pay raises on performance and covered General Schedule employees in grades 13, 14, and 15. The system was terminated in October 1993.