




OFFICE OF THE DIRECTOR

UNITED STATES
OFFICE OF PERSONNEL MANAGEMENT
WASHINGTON, DC 20415-0001

JUL 26 2004

MEMORANDUM FOR HEADS OF EXECUTIVE DEPARTMENTS AND AGENCIES

FROM: Kay Coles James
Director 

SUBJECT: Certification of Performance Appraisal Systems for Senior Employees

I am pleased to inform you that the Office of Personnel Management (OPM) and the Office of Management and Budget (OMB) have jointly issued interim final regulations setting forth the criteria for obtaining certification of performance appraisal systems for members of the Senior Executive Service (SES) and employees in senior-level (SL) and scientific or professional (ST) positions. These regulations are designed to assist Federal agencies in assuring that their senior employee performance management systems make meaningful distinctions based on relative performance, thereby strengthening the linkage between performance and pay. The attached guidance is designed to assist you in submitting requests for full or provisional certification in keeping with the interim final regulations.

The interim final regulations establishing certification requirements and procedures for senior employee appraisal systems incorporate a number of changes received in response to a request for your informal comments on an early draft of these regulatory provisions. The regulations governing the certification of appraisal systems are being issued as interim final regulations with an immediate effective date so that Federal agencies will be able to submit formal requests for full or provisional certification as soon as possible. At the same time, OPM has issued proposed regulations to implement the basic pay and pay administration features of the new SES pay-for-performance system. The SES pay administration regulations, which were also distributed to Federal agencies for informal review, are being issued as proposed regulations so that all interested parties will have an opportunity to provide comments before the new SES pay-for-performance system is fully implemented.

Once you have received certification of your performance appraisal systems for senior employees and OPM's **final** regulations on SES pay administration are issued, you will be permitted to (1) pay your highest-performing SES members above the rate for level III of the Executive Schedule—up to the rate for level II of the Executive Schedule—and (2) apply a higher aggregate limitation—up to the Vice President's salary—to both SES members and SL/ST employees. These are important steps in reforming the Federal pay and performance systems. They will enhance your ability to recruit and retain employees who can make vital contributions to your agency's mission and organizational goals.

You will find the interim final certification regulations at <http://www.opm.gov/oca/compmemo/2004/2004-13-SESCertRegs.pdf> and the proposed SES pay regulations at <http://www.opm.gov/oca/compmemo/2004/2004-13-SESPay.pdf>. These regulations describe the criteria that appraisal systems must meet in order to receive provisional or full certification, the documentation that must be included with certification requests, and the proposed pay administration rules necessary to make pay decisions under the new SES pay system.

The attached implementing guidance provides detailed instructions on how to submit requests for either full or provisional certification. Some of the required documentation is quite straightforward and builds upon materials that agencies already should have readily available. Among the documentation requirements is a requirement to provide OPM with a sample of individual senior employee performance plans. Agencies must provide either a 10 percent sample of covered employee performance plans or a total of 20 plans, whichever is greater. For agencies with fewer than 20 covered employees, all employee performance plans must be submitted. For agencies applying for full certification, the documentation requirements include ratings data for each senior employee for the last two appraisal periods. OPM will also provide an electronic template for this data submission at a later date. The attachments include the following materials:

- Attachment 1: Submission requirements for full certification.
- Attachment 2: Sample cover letter requesting full certification.
- Attachment 3: Submission requirements for provisional certification.
- Attachment 4: Sample cover letter requesting provisional certification.

Agency heads or their designees may submit a single cover letter requesting certification of several SES and/or SL/ST appraisal systems or separate letters requesting certification of each system. For additional guidance or assistance in submitting certification requests, agency Chief Human Capital Officers and Human Resources Directors may contact their assigned OPM Human Capital Officers. Employees should contact their agency human resources offices for information.

We look forward to working with you to implement this critical initiative, which is an important component of the President's Management Agenda and a vital step toward reforming pay and performance systems throughout the Federal Government.

Attachments

cc: Chief Human Capital Officers
Human Resources Directors

SUBMISSION REQUIREMENTS FOR FULL CERTIFICATION OF PERFORMANCE APPRAISAL SYSTEMS

The regulations allowing agencies to implement a pay-for-performance system for members of the Senior Executive Service (SES) and apply a higher aggregate compensation limitation to both senior executives and senior professionals (i.e., employees in senior-level (SL) and scientific or professional (ST) positions) implement significant features of a Federal compensation system that gives the highest pay to agencies' highest performing employees. In order to access the flexibilities offered by these regulations, agencies must first obtain certification of their applicable performance appraisal system(s) under subpart D of 5 CFR part 430. To obtain certification, agencies must demonstrate that their appraisal system(s) makes meaningful distinctions based on relative performance.

This document provides guidance to Federal agencies interested in applying for performance appraisal system certification. The following table lists the documents an agency must submit to fulfill the regulatory requirements for **full certification**.

Please use the fourth (blank) column in the table below to indicate which document(s) the agency is submitting to fulfill the regulatory requirement shown in the first two columns. In addition, please use the fourth column to indicate the location in the cited document where the required information can be found.

Where multiple documents are listed, please submit the document(s) needed to meet the regulatory requirement. For example, if you have two documents that can demonstrate how your agency uses rating levels to differentiate senior employee performance, please select the document that best illustrates this differentiation.

For agencies subject to 5 U.S.C. chapter 43, the performance appraisal system must be approved by OPM. If your agency does not have an approved system, or if your agency has revised its system, please submit a request for system approval concurrently with your certification request.

If you have questions on certification or which documents to submit, please contact your Human Capital Officer.

NOTE: For certification purposes, *performance appraisal system* means the policies, practices, and procedures an agency establishes under 5 U.S.C. chapter 43 and subparts B and C of 5 CFR part 430, or other applicable legal authority, for planning, monitoring, developing, evaluating, and rewarding employee performance. This includes appraisal systems and appraisal programs for senior professionals as defined at 5 CFR 430.203 and performance management systems for senior executives as defined at 5 CFR 430.303. Senior professionals may be covered by a program under their agency's umbrella appraisal system approved by OPM or may be covered by a separate appraisal system approved by OPM.

SUBMISSION REQUIREMENTS FOR FULL CERTIFICATION OF PERFORMANCE APPRAISAL SYSTEMS

REGULATORY REQUIREMENT	LEGAL CITATION (5 CFR)	DOCUMENTS TO SUBMIT Where given a choice of multiple documents, please submit the document(s) needed to meet the regulatory requirement.	AGENCY DOCUMENTATION Please use this column to indicate which document the agency is submitting to fulfill the regulatory requirement and where the specific information can be found.
1. Written request for full certification	430.405(b)	<ul style="list-style-type: none"> • Letter to the Director of OPM from the head of the agency or designee. The letter must specify that the agency requests full certification. 	
2. Full description of the appraisal system(s)	430.405(b)(1)	<ul style="list-style-type: none"> • Performance appraisal system description 	
3. Organizational and employee coverage information	430.405(b)(1)(i)	<ul style="list-style-type: none"> • Performance appraisal system description • Operating manual • Memoranda to employees 	
4. Applicable administrative instructions and implementing guidance	430.405(b)(1)(ii)	<ul style="list-style-type: none"> • Performance appraisal system description • Operating manual • Blank appraisal form • Memoranda to employees • Written instructions for raters or reviewers 	
5. Rating levels that differentiate senior employee performance	430.405(b)(1)(iii)	<ul style="list-style-type: none"> • Performance appraisal system description • Senior employee performance 	

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		<p>plans that show performance level distinctions*</p> <ul style="list-style-type: none"> • The rating level pattern used for reporting data to the Central Personnel Data File — <ul style="list-style-type: none"> ○ for senior executives, pattern F (Levels 1, 2, 3, 5) or pattern H (Levels 1, 2, 3, 4, 5) ○ for senior professionals, pattern B (Levels 1, 3, 5), pattern E (Levels 1, 3, 4, 5), pattern F (Levels 1, 2, 3, 5), or pattern H (Levels 1, 2, 3, 4, 5) 	
<p>6. Clearly defined process for reviewing the initial summary ratings and ratings of record of senior employees to ensure ratings are not given arbitrarily or on a rotational basis</p>	<p>430.405(b)(2)(i)</p>	<ul style="list-style-type: none"> • Performance appraisal system description • Operating manual • Memoranda or written instructions for raters, reviewers, or Performance Review Board members • Narrative attachment 	

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7. Clearly defined process for reviewing the expectations of the subordinates of supervisory senior employees to verify that supervisory senior employees clearly link subordinates' performance expectations to organizational goals	430.405(b)(2)(ii)(A)	<ul style="list-style-type: none"> • Performance appraisal system description • Operating manual • Narrative attachment 	
8. Clearly defined process for reviewing the expectations and ratings of the subordinates of supervisory senior employees to verify that supervisory senior employees make performance distinctions in the appraisal of their subordinates that reflect individual and organizational performance	430.405(b)(2)(ii)(B)	<ul style="list-style-type: none"> • Performance appraisal system description • Operating manual • Narrative attachment 	

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<p>9. The appraisal system(s) meets the certification criteria set forth in 5 CFR 430.404(a)(1)-(9)</p>	<p>430.405(b)(3)(ii) 430.404(a)(1)-(9)</p>	<p>1) Alignment</p> <ul style="list-style-type: none"> • Agency’s strategic plan, annual performance plan, or applicable strategic planning document(s) to establish alignment with employee performance plans • Performance appraisal system description that explains how the agency links senior employee performance plans to strategic planning initiatives • Senior employee performance plans that show expectations are linked to strategic planning initiatives* • Narrative attachment that describes how the agency’s senior employee performance plans link to the agency’s mission and goals <p>2) Consultation</p> <ul style="list-style-type: none"> • Performance appraisal system description that explains how employees are involved in developing performance plans and how performance plans are 	

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		<p>communicated to senior employees at the beginning of the appraisal period</p> <ul style="list-style-type: none"> • Senior employee performance plans that show employees were provided their plans at the beginning of the appraisal period and show that employees were involved in developing the performance plans* • Narrative attachment that describes how the agency involves its employees, individually or in the aggregate, in developing employee performance plans <p>3) Results</p> <ul style="list-style-type: none"> • Performance appraisal system description that explains how performance expectations are written to reflect organizational and individual results and are observable, measurable, and/or demonstrable 	

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		<ul style="list-style-type: none"> • Senior employee performance plans that show expectations include organizational and individual results and requirements/standards that are observable, measurable, and/or demonstrable* • Narrative attachment that describes how the agency ensures expectations include organizational and individual results and are observable, measurable, and/or demonstrable <p>4) Balance</p> <ul style="list-style-type: none"> • Performance appraisal system description that explains how performance expectations include balanced measures • Senior employee performance plans that show appropriate measures such as employee and/or customer/stakeholder feedback; quality, quantity, timeliness, and cost effectiveness; 	

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		<p>technical, leadership, and/or managerial competencies*</p> <ul style="list-style-type: none"> • Narrative attachment that describes how the agency identifies critical competencies and behaviors for the appraisal process and how it measures or observes them • Narrative attachment that describes how the agency incorporates customer satisfaction and employee perspectives into its senior employee performance plans <p>5) Assessments and Guidelines</p> <ul style="list-style-type: none"> • Agency head or designee’s guidance to rating and reviewing officials and Performance Review Board members <p>6) Oversight</p> <ul style="list-style-type: none"> • Narrative attachment that describes how the senior employee ratings and awards take into account, as appropriate, the 	

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		<p>assessment of the agency's performance</p> <ul style="list-style-type: none"> • Documentation the agency used to assess organizational performance <p>7) Accountability</p> <ul style="list-style-type: none"> • Senior employee performance plans that show how senior employees are accountable for rigorous performance management and for aligning their subordinate employees' performance plans to organizational goals* • Performance appraisal system description that explains how senior employees are accountable for rigorous performance management and for aligning their subordinate employees' performance plans to organizational goals <p>8) Performance Differentiation</p> <ul style="list-style-type: none"> • Performance appraisal system 	

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		<p>description that provides for an outstanding summary level</p> <ul style="list-style-type: none"> • Same documents listed under regulatory requirement #10, below <p>9) Pay Differentiation</p> <ul style="list-style-type: none"> • Awards program description • Narrative attachment that describes how the agency determines pay adjustments • Same documents listed under regulatory requirement #11, below 	
10. Data on senior employees' ratings	430.405(b)(4)	<ul style="list-style-type: none"> • Ratings data for the two appraisal periods preceding the certification request for all senior employees covered by the appraisal system(s) to be certified— <ul style="list-style-type: none"> ○ Distribution of ratings and ○ Ratings for each covered employee <p>Note: An electronic template for data submission will be provided by OPM at a later date.</p>	

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11. Data on senior employees' pay and cash awards	430.405(b)(4)	<ul style="list-style-type: none"> • Pay and awards data for the two fiscal years preceding the certification request for all senior employees covered by the appraisal system(s) to be certified, as applicable — <ul style="list-style-type: none"> ○ Levels of pay for new appointees, ○ Performance-based pay adjustments, ○ Salaries before and after pay adjustments, and ○ Cash awards <p>Note: An electronic template for data submission will be provided by OPM at a later date.</p>	

*For senior employee performance plans, agencies must provide either a 10 percent sample of covered employee performance plans or a total of 20 plans, whichever is greater. For agencies with fewer than 20 covered employees, all employee performance plans must be submitted.

SAMPLE COVER LETTER REQUESTING FULL CERTIFICATION

The Honorable Kay Coles James
Director
Office of Personnel Management
Washington, DC 20415

Dear Ms. James:

This is to request full certification of the [Senior Executive Service (SES) and/or senior professional] appraisal system for [Insert name of agency or component]. We understand that upon receiving certification, we will be permitted to pay our highest performing SES members above the rate for level III of the Executive Schedule, up to the rate for level II of the Executive Schedule. We further understand that this certification is required in order to apply a higher aggregate limitation on pay, equivalent to the rate payable to the Vice President, for SES members who are paid under 5 U.S.C. 5383 and employees in senior-level (SL) and scientific or professional (ST) positions paid under 5 U.S.C. 5376.

The documentation accompanying this certification request demonstrates that the design, application, and administration of the system meet all regulatory requirements for certification. We have included data on [senior executive annual summary ratings or senior professional ratings of record, as applicable] for the two appraisal periods preceding this request, as well as corresponding pay adjustments, cash awards, and levels of pay provided to those senior employees.

If you have any questions regarding our submission, please contact

_____ .

Sincerely,

[Agency head or designee]

Enclosures

SUBMISSION REQUIREMENTS FOR PROVISIONAL CERTIFICATION OF PERFORMANCE APPRAISAL SYSTEMS

The regulations allowing agencies to implement a pay-for-performance system for members of the Senior Executive Service (SES) and apply a higher aggregate compensation limitation to both senior executives and senior professionals (i.e., employees in senior-level (SL) and scientific or professional (ST) positions) implement significant features of a Federal compensation system that gives the highest pay to agencies' highest performing employees. In order to access the flexibilities offered by these regulations, agencies must first obtain certification of their applicable performance appraisal system(s) under subpart D of 5 CFR part 430. To obtain certification, agencies must demonstrate that their appraisal system(s) makes meaningful distinctions based on relative performance.

This document provides guidance to Federal agencies interested in applying for performance appraisal system certification. The following table lists the documents an agency must submit to fulfill the regulatory requirements for **provisional certification**.

Please use the fourth (blank) column in the table below to indicate which document(s) the agency is submitting to fulfill the regulatory requirement shown in the first two columns. In addition, please use the fourth column to indicate the location in the cited document where the required information can be found.

Where multiple documents are listed, please submit the document(s) needed to meet the regulatory requirement. For example, if you have two documents that can demonstrate how your agency uses rating levels to differentiate senior employee performance, please select the document that best illustrates this differentiation.

For agencies subject to 5 U.S.C. chapter 43, the performance appraisal system must be approved by OPM. If your agency does not have an approved system, or if your agency has revised its system, please submit a request for system approval concurrently with your certification request.

If you have questions on certification or which documents to submit, please contact your Human Capital Officer.

NOTE: For certification purposes, *performance appraisal system* means the policies, practices, and procedures an agency establishes under 5 U.S.C. chapter 43 and subparts B and C of 5 CFR part 430, or other applicable legal authority, for planning, monitoring, developing, evaluating, and rewarding employee performance. This includes appraisal systems and appraisal programs for senior professionals as defined at 5 CFR 430.203 and performance management systems for senior executives as defined at 5 CFR 430.303. Senior professionals may be covered by a program under their agency's umbrella appraisal system approved by OPM or may be covered by a separate appraisal system approved by OPM.

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2. Full description of the appraisal system(s)	430.405(b)(1)	<ul style="list-style-type: none"> • Performance appraisal system description 	
3. Organizational and employee coverage information	430.405(b)(1)(i)	<ul style="list-style-type: none"> • Performance appraisal system description • Operating manual • Memoranda to employees 	
4. Applicable administrative instructions and implementing guidance	430.405(b)(1)(ii)	<ul style="list-style-type: none"> • Performance appraisal system description • Operating manual • Blank appraisal form • Memoranda to employees • Written instructions for raters or reviewers 	
5. Rating levels that differentiate senior employee performance	430.405(b)(1)(iii)	<ul style="list-style-type: none"> • Performance appraisal system description • Senior employee performance 	

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		<p>plans that show performance level distinctions*</p> <ul style="list-style-type: none"> • The rating level pattern used for reporting data to the Central Personnel Data File — <ul style="list-style-type: none"> ○ for senior executives, pattern F (Levels 1, 2, 3, 5) or pattern H (Levels 1, 2, 3, 4, 5) ○ for senior professionals, pattern B (Levels 1, 3, 5), pattern E (Levels 1, 3, 4, 5), pattern F (Levels 1, 2, 3, 5), or pattern H (Levels 1, 2, 3, 4, 5) 	
<p>6. Clearly defined process for reviewing the initial summary ratings and ratings of record of senior employees to ensure ratings are not given arbitrarily or on a rotational basis</p>	<p>430.405(b)(2)(i)</p>	<ul style="list-style-type: none"> • Performance appraisal system description • Operating manual • Memoranda or written instructions for raters, reviewers, or Performance Review Board members • Narrative attachment 	

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7. Clearly defined process for reviewing the expectations of the subordinates of supervisory senior employees to verify that supervisory senior employees clearly link subordinates' performance expectations to organizational goals	430.405(b)(2)(ii)(A)	<ul style="list-style-type: none"> • Performance appraisal system description • Operating manual • Narrative attachment 	
8. Clearly defined process for reviewing the expectations and ratings of the subordinates of supervisory senior employees to verify that supervisory senior employees make performance distinctions in the appraisal of their subordinates that reflect individual and organizational performance	430.405(b)(2)(ii)(B)	<ul style="list-style-type: none"> • Performance appraisal system description • Operating manual • Narrative attachment 	

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9. The appraisal system(s) meets the certification criteria set forth in 5 CFR 430.404(a)(1)-(4)	430.405(b)(3)(i) 430.404(a)(1)-(4)	1) Alignment <ul style="list-style-type: none"> • Agency’s strategic plan, annual performance plan, or applicable strategic planning document(s) to establish alignment with employee performance plans • Performance appraisal system description that explains how the agency links senior employee performance plans to strategic planning initiatives • Senior employee performance plans that show expectations are linked to strategic planning initiatives* • Narrative attachment that describes how the agency’s senior employee performance plans link to the agency’s mission and goals 2) Consultation <ul style="list-style-type: none"> • Performance appraisal system description that explains how employees are involved in developing performance plans and how performance plans are 	

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		<p>communicated to senior employees at the beginning of the appraisal period</p> <ul style="list-style-type: none"> • Senior employee performance plans that show employees were provided their plans at the beginning of the appraisal period and show that employees were involved in developing the performance plans* • Narrative attachment that describes how the agency involves its employees, individually or in the aggregate, in developing employee performance plans <p>3) Results</p> <ul style="list-style-type: none"> • Performance appraisal system description that explains how performance expectations are written to reflect organizational and individual results and are observable, measurable, and/or demonstrable 	

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		<p>technical, leadership, and/or managerial competencies*</p> <ul style="list-style-type: none"> • Narrative attachment that describes how the agency identifies critical competencies and behaviors for the appraisal process and how it measures or observes them • Narrative attachment that describes how the agency incorporates customer satisfaction and employee perspectives into its senior employee performance plans 	

*For senior employee performance plans, agencies must provide either a 10 percent sample of covered employee performance plans or a total of 20 plans, whichever is greater. For agencies with fewer than 20 covered employees, all employee performance plans must be submitted.

SAMPLE COVER LETTER REQUESTING PROVISIONAL CERTIFICATION

The Honorable Kay Coles James
Director
Office of Personnel Management
Washington, DC 20415

Dear Ms. James:

This is to request provisional certification of the [Senior Executive Service (SES) and/or senior professional] appraisal system for [Insert name of agency or component]. We understand that upon receiving certification, we will be permitted to pay our highest performing Senior Executive Service (SES) members above the rate for level III of the Executive Schedule, up to the rate for level II of the Executive Schedule. We further understand that this certification is required in order to apply a higher aggregate limitation on pay, equivalent to the rate payable to the Vice President, for SES members who are paid under 5 U.S.C. 5383 and employees in senior-level (SL) and scientific or professional (ST) positions paid under 5 U.S.C. 5376.

This request for provisional certification shows that the design of our appraisal system(s) [for senior executives or senior professionals, as applicable] meets all regulatory requirements set forth in regulations.

If you have any questions regarding our submission, please contact

_____ .

Sincerely,

[Agency head or designee]

Enclosures

Publication Date July 28, 2004

6325-39

OFFICE OF PERSONNEL MANAGEMENT

5 CFR PART 430

OFFICE OF MANAGEMENT AND BUDGET

5 CFR PART 1330

RIN: 3206-AJ86

Executive Performance and Accountability

AGENCY: Office of Personnel Management and Office of Management and Budget.

ACTION: Interim rule with request for comments

SUMMARY: The Office of Personnel Management (OPM) is issuing interim regulations jointly with the Office of Management and Budget (OMB) to implement a statutory provision that strengthens the relationship between the performance and pay of senior employees of the Federal Government. These regulations establish rigorous conditions regarding an agency's performance appraisal systems for senior employees which, if met, would allow its appraisal systems to be certified. These regulations set forth the criteria and procedural requirements for such certification.

DATES: *Effective Date:* The regulations are effective on July 28, 2004.

Comment Date: Comments must be received by OPM on or before August 27, 2004.

ADDRESSES: Send or deliver comments to Donald J. Winstead, Deputy Associate Director for Pay and Performance Policy, Office of Personnel Management, Room 7H31, 1900 E Street, NW., Washington, DC 20415-8200; by FAX at (202) 606-0824; or by

e-mail at pay-performance-policy@opm.gov.

FOR FURTHER INFORMATION CONTACT: Barbara Colchao by telephone at (202) 606-2720; by FAX at (202) 606-2395; or by email at pay-performance-policy@opm.gov.

SUPPLEMENTARY INFORMATION: The President holds the head of each agency accountable for the performance of that agency. Because an agency's success depends in large part on the effective leadership provided by its senior executives and senior professionals, the President also holds each agency head accountable for effectively managing the performance of those key members of the agency's top management team. The Office of Personnel Management (OPM) is issuing interim regulations jointly with the Office of Management and Budget (OMB) to implement section 1322 of the Chief Human Capital Officers Act of 2002 (Title XIII of Public Law 107-296, the Homeland Security Act of 2002; November 25, 2002). This new statutory provision, as implemented by the regulations set forth below, will assist an agency head in assuring that the agency's senior employee performance management systems make meaningful distinctions based on relative performance for an agency's Senior Executive Service (SES), senior-level (SL), and scientific or professional (ST) employees, thereby strengthening the linkage between their performance and their pay.

Section 1322 of the Chief Human Capital Officers Act of 2002, added a new paragraph (d) to 5 U.S.C. 5307 establishing conditions that, if met, would permit an agency to apply a higher aggregate limitation on pay, equivalent to the rate payable to the Vice President, for certain SES members who are paid under 5 U.S.C. 5383 and employees in senior-level and scientific or professional positions paid under 5 U.S.C.

5376. However, in order to apply this higher aggregate pay limitation, the statute requires that an agency first demonstrate that it has developed and implemented performance appraisal systems for these employees that make meaningful distinctions based on relative performance, as certified by OPM, with OMB concurrence.

As a separate but related matter, OPM is issuing under separate cover regulations to implement section 1125 of the National Defense Authorization Act for Fiscal Year 2004 (Public Law 108-136, November 24, 2003) which (1) amends 5 U.S.C. 5382 and 5383 by replacing a six-level pay system for SES members with a single, open-range “payband” with only the minimum and maximum rates of pay set by law and (2) requires certification under 5 U.S.C. 5307 to allow an increase in the maximum rate of basic pay, from level III to level II of the Executive Schedule, for SES members.

In these regulations, we provide the criteria an agency must meet and the procedures it must follow to obtain certification of its appraisal system(s). These regulations refer to SES members as “senior executives” and SL and ST employees as “senior professionals.” When a distinction between executives and professionals is irrelevant or unnecessary, the regulations refer to them as “senior employees.”

Certification of Performance Appraisal Systems

These regulations establish a new subpart D in part 430 of title 5, Code of Federal Regulations, and a new subpart D in a newly established part 1330 of title 5, Code of Federal Regulations. This new subpart includes the criteria and procedural requirements for certifying an agency’s performance appraisal system(s). Agencies may seek certification of their OPM-approved appraisal systems for their senior employees. Note that under subchapters I and II of 5 U.S.C. chapter 43, an agency must establish separate

performance appraisal systems for its senior professionals and its senior executives.

However, such systems are subject to the same certification criteria, and an agency may choose to establish systems for these groups of employees that are essentially identical.

In some agencies, the performance appraisal system(s) covers employees in many organizations and/or components, and their ability to meet the criteria required by these regulations may vary significantly. In such cases, an agency, at its discretion, may establish separate performance appraisal systems for these distinct organizations and/or components to ensure timely certification of their performance appraisal system(s) for those organizations or components that meet the criteria. New appraisal systems established for this purpose must be approved by OPM. However, when an agency establishes a new appraisal system specifically for the purpose of seeking certification under these regulations, the agency may submit that system for certification even if it has not yet been approved by OPM. OPM, with OMB concurrence, will certify only those systems that OPM approves under subpart B or C of 5 CFR part 430. In addition, when an agency with a certified appraisal system(s) fails to maintain such system approval or is subjected to OPM-mandated corrective action relating to its application of the provisions of 5 U.S.C. chapter 43 or 5 CFR part 430, its system certification under these regulations is suspended automatically without the need for further action by OPM or OMB.

An agency that has not received appraisal system certification may adjust the rate of basic pay for its SES members only up to the rate for level III of the Executive Schedule and must apply an aggregate limitation on pay of level I of the Executive Schedule to its senior employees. Section 5307(d) of title 5, United States Code, requires that agencies design and apply performance appraisal systems for their senior executives

and senior professionals that “make meaningful distinctions based on relative performance” in order to receive appraisal system certification. As provided below, an agency’s appraisal system(s) for its senior executives and senior professionals, as applicable, will be certified only if the agency meets the certification criteria and procedures for certifying appraisal systems set forth in these regulations. (Note that agencies not subject to the provisions and requirements of 5 U.S.C. chapter 43 and 5 CFR part 430 must still meet these criteria and procedural requirements to obtain certification of their appraisal systems.)

Certification Criteria. The following nine certification criteria constitute broad principles designed to guide agencies in the strategic use of their senior employee performance appraisal system(s) to support the development of a strong performance culture and the attainment of the agency’s mission, goals, and objectives. The criteria place requirements on the design and application of agency appraisal systems that must be met to be certified. Although we have specified one particular criterion that derives from 5 U.S.C. chapter 43 (i.e., consultation), all other requirements of chapter 43 must also be met by agencies subject to its provisions. Agency systems will differ in how they are designed and implemented and in how they meet these criteria. In applying these guidelines, agencies must rate performance in accordance with performance expectations, as appropriate and as defined and provided for in these regulations. The regulations define performance expectations as the critical and other performance elements and performance requirements established for senior executives, the performance elements and standards established for senior professionals, and other appropriate means

authorized under performance appraisal systems not covered by chapter 43 for communicating work requirements to senior employees.

- **Alignment**—Performance expectations are linked to or derived from the agency’s mission, strategic goals, program/policy objectives, and/or annual performance plan.
- **Consultation**—Performance expectations are based on senior employee involvement and input that are communicated at the beginning of the appraisal period and appropriate times thereafter, consistent with 5 CFR part 430, subparts B and C.
- **Results**—Performance expectations for senior employees apply to their respective areas of responsibility; reflect expected agency or organizational performance; clearly describe performance that is measurable, demonstrable, or observable; and focus on tangible outputs, outcomes, milestones, or other deliverables.
- **Balance**—Performance expectations for senior employees include appropriate measures or indicators of results; customer/stakeholder feedback; quality, quantity, timeliness, and cost effectiveness, as applicable; and competencies or behaviors that contribute to and are necessary to distinguish outstanding performance.
- **Assessments and guidelines**—The agency head, or an individual specifically designated for such purpose, provides assessments of performance of the agency overall, as well as each of its major program and functional areas, such as reports of the agency’s Government Performance and Results Act (GPRA)

goals and other program performance measures and indicators, and evaluation guidelines based, in part, upon those assessments to senior employees, appropriate senior employee rating and reviewing officials, and Performance Review Board members. These assessments and guidelines are to be provided at the conclusion of the appraisal period but before ratings are recommended, so that they may serve as a basis for individual performance evaluations, as appropriate. The guidance provided may not take the form of quantitative limitations on the number of ratings at any given rating level, and must conform to subpart B or C of 5 CFR part 430, as applicable.

- **Oversight**—Rigorous oversight of the appraisal process is provided by the agency head or designee, who certifies that (1) the senior employee appraisal process makes meaningful distinctions based on relative performance; (2) the results of that process take into account, as appropriate, the agency's assessment of its performance against program performance measures; and (3) pay adjustments, cash awards, and levels of pay accurately reflect and recognize both individual and organizational performance. The agency head or designee need not perform these duties personally, but does bear responsibility for seeing to it that they are done. Furthermore, the organizational performance assessment described in this criterion need not be a separate assessment done for the purposes of these interim final regulations, but may be any official or formal organizational assessment done for the purpose of determining how well the agency and its individual components have performed during the appraisal period.

- **Accountability**—Senior employee ratings (as well as subordinate employees’ performance expectations and ratings for those with supervisory responsibilities) appropriately reflect the employee’s performance expectations, relevant program performance measures, and any other relevant factors.
- **Performance Differentiation**—(1) The appraisal system includes a rating level that reflects outstanding performance or, for equivalent systems that do not use summary ratings, provides for clear differentiation of outstanding performance, as defined in these regulations; and (2) the appraisal process results in meaningful distinctions in relative performance based on senior employees’ actual performance against rigorous performance expectations. “Relative performance” in this context has the meaning given that term in §§ 430.402 and 1330.402. It does not require ranking senior employees against each other. Indeed, such ranking is prohibited for the purpose of determining performance ratings. For the agency’s senior executives covered by 5 CFR part 430 subpart C, appraisal systems must include at least four, but not more than five, summary rating levels—an outstanding level, a fully successful level, an optional level between outstanding and fully successful, a minimally satisfactory level, and an unacceptable level. For the agency’s senior professionals covered by 5 CFR part 430 subpart B, appraisal systems must include at least three, but not more than five, summary rating levels—an outstanding level, a fully successful level, an optional level between

outstanding and fully successful, an unacceptable level, and an optional level between fully successful and unacceptable.

- **Pay Differentiation**—Individual pay rates and pay adjustments, as well as their overall distribution, reflect meaningful distinctions among executives based on their relative contribution to agency performance. An agency's highest performing senior employees should receive the largest pay adjustments and/or highest pay levels (including both basic pay and performance awards), particularly above the rate for level III of the Executive Schedule. Agencies must provide for transparency in the processes for making pay decisions. For example, agencies should consider communicating the overall results of performance management decisions to senior employees, if individual confidentiality can be assured.

Certification Procedures. To receive appraisal system certification, an agency must provide documentation, including its performance ratings history where summary ratings are used, to demonstrate that its appraisal system(s) meets the criteria and procedural requirements of the regulations. Based on that documentation and any additional information that OPM and OMB deem necessary, OPM, with OMB concurrence, may grant the agency's system(s) full certification for 2 calendar years.

Alternatively, in the case of an agency that has designed, but not yet fully implemented an appraisal system(s) for its senior executives and/or senior professionals, as applicable, and which may not have a history of performance ratings that meets the certification criteria and procedural requirements, OPM, with OMB concurrence, may grant provisional certification for 1 calendar year. OPM may extend provisional

certification into the following calendar year in order to permit an agency to take any actions needed to adjust pay based on annual summary ratings, ratings of record, or other performance appraisal results determined during the calendar year for which the system was certified.

Agencies with fully or provisionally certified systems may set a senior executive's rate of basic pay up to the rate for level II of the Executive Schedule, consistent with 5 CFR part 534, subpart D, as and when such subpart is put into effect. In addition, such agencies' senior employees who are covered by a fully or provisionally certified appraisal system may receive aggregate compensation in a calendar year up to an amount equivalent to the total annual compensation payable to the Vice President (consistent with 5 CFR part 530, subpart B, as and when regulations relevant to the higher aggregate limitation on pay are put into effect).

A senior executive whose rate of basic pay is higher than the rate for level III of the Executive Schedule may not suffer a reduction in pay because his or her agency's applicable performance appraisal system certification is suspended under 5 CFR 430.405(h) and 1330.405(h). The senior executive will continue to receive his or her current SES rate and is not eligible for a pay adjustment until the senior executive is assigned to a position that would allow the employee to receive a pay adjustment or until certification of the employing agency's applicable performance appraisal system is reinstated under 5 CFR part 430, subpart D, and part 1330, subpart D.

Agencies with provisionally certified appraisal systems must reapply for certification in order to continue setting the rate of basic pay for senior executives up to the rate for level II of the Executive Schedule and applying the higher aggregate

limitation on pay to its senior employees. OPM expects that most agencies granted provisional certification for 2 consecutive years will qualify for full certification. However, these agencies must request full certification by following the procedures contained in these regulations. OPM, with OMB concurrence, also may suspend (with appropriate advance notice) an agency's appraisal system certification if it determines that the agency is not in compliance with applicable certification requirements.

Regulatory Flexibility Act

I certify that these regulations will not have a significant economic impact on a substantial number of small entities, because they will apply only to Federal agencies and employees.

Waiver of Notice of Proposed Rulemaking and Delayed Effective Date

Pursuant to section 553(b)(3)(B) of title 5 of the United States Code, I find that good cause exists for waiving the general notice of proposed rule making. Also, pursuant to 5 U.S.C. 553(d)(3), I find that good cause exists for making this rule effective in less than 30 days. These regulations implement section 1322 of the Chief Human Capital Officers Act, which became effective on January 25, 2003, and permits the application of higher pay rates for members of the Senior Executive Service up to the rate for level II of the Executive Schedule as well as access to a higher aggregate limitation on pay up to the salary of the Vice President for certain employees. The waiver of the requirements for proposed rulemaking and a delay in the effective date are necessary to ensure timely implementation of the law as intended by Congress and to activate an important tool for the retention of high-performing senior executives that provides some relief for pay

compression and provides for paying executives based on their individual performance and contribution to agency performance.

E.O. 12866, Regulatory Review

This rule has been reviewed by the Office of Management and Budget in accordance with E.O. 12866.

List of Subjects in 5 CFR Part 430 and 5 CFR Part 1330

Government Employees.

Office of Management and Budget

Office of Personnel Management

Joshua B. Bolten
Director

Kay Coles James
Director

Accordingly, OPM and OMB are amending title 5 of the Code of Federal Regulations as follows:

5 CFR Chapter I – Office of Personnel Management

PART 430—PERFORMANCE MANAGEMENT

1. The authority citation for part 430 is revised to read as follows:

Authority: 5 U.S.C. chapter 43 and 5307(d).

2. In part 430, a new subpart D is added to read as follows. The text of the subpart is the same as the common rule text set out at the end of this document.

Subpart D—Performance Appraisal Certification for Pay Purposes

Sec.
430.401 Purpose.
430.402 Definitions.
430.403 System certification.

430.404 Certification criteria.

430.405 Procedures for certifying agency appraisal systems.

3. The text of the new subpart is the same as the common rule text set out at the end of this document, with the following amendments:

a. In § 430.403, the references to “§ ____.402,” “§ ____.404,” and “§ ____.405 are revised to read “§ 430.402,” “§ 430.404,” and “§ 430.405,” respectively.

b. In § 430.404, the reference to “§ ____.402” is revised to read “§ 430.402.”

c. In § 430.405, the references to “§ ____.402,” “§ ____.403,” and “§ ____.404” are revised to read “§ 430.402,” “§ 430.403,” and “§ 430.404,” respectively.

d. Add the following note to subpart D:

Note to Subpart D: Regulations identical to this subpart appear at 5 CFR part 1330, subpart D.

5 CFR Chapter III – Office of Management and Budget

1. 5 CFR chapter III is amended by establishing a new subchapter C consisting of part 1330, subpart D, to read as follows:

Subchapter C—Joint Regulations with the Office of Personnel Management

PART 1330—HUMAN RESOURCES MANAGEMENT

Subparts A—C [Reserved]

Subpart D—Performance Appraisal Certification for Pay Purposes

Sec.

1330.401 Purpose.

1330.402 Definitions.

1330.403 System certification.

1330.404 Certification criteria.

1330.405 Procedures for certifying agency appraisal systems.

Authority: 5 U.S.C. 5307(d).

2. The text of the new subpart is the same as the common rule text set out at the end of this document, with the following amendments:

a. In § 1330.403, the references to “§ ____.402,” “§ ____.404,” and “§ ____.405” are revised to read “§ 1330.402,” “§ 1330.404,” and “§ 1330.405,” respectively.

b. In § 1330.404, the reference to “§ ____.402” is revised to read “§ 1330.402.”

c. In § 1330.405, the references to “§ ____.402,” “§ ____.403,” and “§ ____.404” are revised to read “§ 1330.402,” “§ 1330.403,” and “§ 1330.404,” respectively.

d. Add the following note to subpart D:

Note to Subpart D: Regulations identical to this subpart appear at 5 CFR part 430, subpart D.

Text of the Common Rule

The text of the common rule for 5 CFR part 430, subpart D, and 5 CFR part 1330, subpart D, adopted as set forth above, reads as follows:

Subpart D—Performance Appraisal Certification for Pay Purposes

Sec.

____.401 Purpose.

____.402 Definitions.

____.403 System certification.

____.404 Certification criteria.

____.405 Procedures for certifying agency appraisal systems.

§ ____.401 Purpose.

(a) This subpart implements 5 U.S.C. 5307(d), as added by section 1322 of the Chief Human Capital Officers Act of 2002 (Title XIII of Public Law 107-296, the Homeland Security Act of 2002; November 25, 2002), which provides a higher aggregate limitation on pay for certain members of the Senior Executive Service (SES) under

5 U.S.C. 5382 and 5383 and employees in senior-level (SL) and scientific or professional (ST) positions paid under 5 U.S.C. 5376. In addition, this subpart is necessary to administer rates of basic pay for members of the SES under 5 U.S.C. 5382, as amended by section 1125 of the National Defense Authorization Act for Fiscal Year 2004. The regulations in this subpart strengthen the application of pay-for-performance principles to senior executives and senior professionals. Specifically, the statutory provisions authorize an agency to apply a higher maximum rate of basic pay for senior executives (consistent with 5 CFR part 534, subpart D, when effective) and apply a higher aggregate limitation on pay (consistent with 5 CFR part 530, subpart B) to its senior employees, but only after OPM, with OMB concurrence, has certified that the design and application of the agency's appraisal systems for these employees make meaningful distinctions based on relative performance. This subpart establishes the certification criteria and procedures that OPM will apply in considering agency requests for such certification.

(b) Senior executives generally may receive an annual rate of basic pay up to the rate for level III of the Executive Schedule under 5 U.S.C. 5382 and 5 CFR part 534, subpart D, when effective. Senior employees generally may receive total compensation in a calendar year up to the rate for level I of the Executive Schedule under 5 U.S.C. 5307(a) and 5 CFR 530.203(a). Only employees covered by an appraisal system that OPM, with OMB concurrence, certifies under this subpart are eligible for a maximum annual rate of basic pay for senior executives up to the rate for level II of the Executive Schedule (consistent with 5 U.S.C. 5382 and 5 CFR part 534, subpart D, when effective) and a higher aggregate pay limitation equivalent to the total annual compensation payable to the Vice President (consistent with 5 U.S.C. 5307(d) and 5 CFR 530.203(b)).

§ __.402 **Definitions.**

In this subpart—

Appraisal system means the policies, practices, and procedures an agency establishes under 5 U.S.C. chapter 43 and 5 CFR part 430, subparts B and C, or other applicable legal authority, for planning, monitoring, developing, evaluating, and rewarding employee performance. This includes appraisal systems and appraisal programs as defined at § 430.203 and performance management systems as defined at § 430.303.

GPRA means the Government Performance and Results Act of 1993.

OMB means the Office of Management and Budget.

OPM means the Office of Personnel Management.

Outstanding performance means performance that substantially exceeds the normally high performance expected of any senior employee, as evidenced by exceptional accomplishments or contributions to the agency's performance.

Performance evaluation means the comparison of the actual performance of senior employees against their performance expectations and may take into account their contribution to agency performance, where appropriate.

Performance expectations means critical and other performance elements and performance requirements that constitute the senior executive performance plans (as defined in § 430.303) established for senior executives, the performance elements and standards that constitute the performance plans (as defined in § 430.203) established for senior professionals, or other appropriate means authorized under performance appraisal systems not covered by 5 U.S.C. chapter 43 for communicating what a senior employee

is expected to do and the manner in which he/she is expected to do it, and may include contribution to agency performance, where appropriate.

Program performance measures means results-oriented measures of performance, whether at the agency, component, or function level, which include, for example, measures under the Government Performance and Results Act.

PRB means Performance Review Board, as described at § 430.310.

Relative performance means the performance of a senior employee with respect to the performance of other senior employees, including their contribution to agency performance, where appropriate, as determined by the application of a certified appraisal system.

Senior employee means a senior executive or a senior professional.

Senior executive means a member of the Senior Executive Service (SES) paid under 5 U.S.C. 5383.

Senior professional means an employee in a senior-level (SL) or scientific or professional position (ST) paid under 5 U.S.C. 5376.

§ __.403 System certification.

(a) The performance appraisal system(s) covering senior employees must be certified by OPM, with OMB concurrence, as making meaningful distinctions based on relative performance before an agency may apply a maximum annual rate of basic pay for senior executives equal to the rate for level II of the Executive Schedule or apply an annual aggregate limitation on payments to senior employees equal to the salary of the Vice President under 5 U.S.C. 5307(d)). OPM, with OMB concurrence, will certify an agency's appraisal system(s) only when a review of that system's design, application, and

administration reveals that the agency meets the certification criteria established in § ____.404 and has followed the procedures for certifying agency appraisal systems in § ____.405.

(b) Except as provided in paragraph (c) of this section, agencies subject to 5 U.S.C. chapter 43 and 5 CFR part 430 seeking certification of their appraisal systems must submit systems that have been approved by OPM under § 430.312 or § 430.210, as applicable. In some agencies, the performance appraisal system(s) covers employees in many organizations and/or components, and their ability to meet the certification criteria in § ____.404 may vary significantly. In such cases, an agency may establish and/or submit separate performance appraisal systems for each of these distinct organizations and/or components to ensure timely certification of those performance appraisal system(s) that meet the criteria. New appraisal systems established under 5 CFR part 430, subpart B or C, as applicable based on the employees covered, must be approved by OPM.

(c) When an agency establishes a new appraisal system for the purpose of seeking certification under this subpart, the agency may submit that system for certification even if it has not yet been approved by OPM under § 430.312 or § 430.210, as applicable. OPM will certify, with OMB concurrence, only those systems that OPM determines meet the approval requirements of 5 CFR part 430, subpart B or C, as applicable.

(d) An agency must establish an appraisal system(s), as defined in § ____.402, for its senior professionals that meets the requirements of 5 CFR part 430, subpart B, and is separate from the system(s) established to cover its SES members under 5 CFR part 430, subpart C. For the purpose of certification under this subpart, such senior professional

appraisal system(s) must meet the certification criteria set forth in § ____404. At its discretion, an agency may include system features in its senior professional appraisal system(s) that are the same as, or similar to, the features of its SES appraisal system(s), as appropriate, including procedures that correspond to the higher level review procedures under § 430.308(b) and PRB reviews of summary ratings under § 430.308(c).

(e) For agencies subject to 5 U.S.C. chapter 43 and 5 CFR part 430, OPM approval of the agency performance appraisal system(s) is a prerequisite to certification. Agencies not subject to the appraisal provisions of 5 U.S.C. chapter 43 and 5 CFR part 430 and which are seeking certification of their appraisal system(s) under this subpart must submit appropriate documentation to demonstrate that each system complies with the appropriate legal authority that governs the establishment, application, and administration of that system.

§ ____404 Certification criteria.

(a) To be certified, an agency's applicable appraisal system(s) for senior executives or senior professionals must make meaningful distinctions based on relative performance and meet the other requirements of 5 U.S.C. chapter 43, as applicable, in addition to the particular criterion cited here (i.e., consultation). Such system(s) must provide for the following:

(1) Alignment, so that the performance expectations for individual senior employees derive from, and clearly link to, the agency's mission, GPRAs strategic goals, program and policy objectives, and/or annual performance plans and budget priorities;

(2) Consultation, so that the performance expectations for senior employees meet the requirements of 5 CFR part 430, subparts B and C, as applicable, and/or other

applicable legal authority; are developed with the input and involvement of the individual senior employees who are covered thereby; and are communicated to them at the beginning of the applicable appraisal period, and/or at appropriate times thereafter;

(3) Results, so that the performance expectations for individual senior employees apply to their respective areas of responsibility; reflect expected agency and/or organizational outcomes and outputs, performance targets or metrics, policy/program objectives, and/or milestones; identify specific programmatic crosscutting, external, and partnership-oriented goals or objectives, as applicable; and are stated in terms of observable, measurable, and/or demonstrable performance;

(4) Balance, so that in addition to expected results, the performance expectations for individual senior employees include appropriate measures or indicators of employee and/or customer/stakeholder feedback; quality, quantity, timeliness, and cost effectiveness, as applicable; and those technical, leadership and/or managerial competencies or behaviors that contribute to and are necessary to distinguish outstanding performance;

(5) Appropriate assessments of the agency's performance—overall and with respect to each of its particular missions, components, programs, policy areas, and support functions—such as reports of the agency's GPRA goals, annual performance plans and targets, program performance measures, and other appropriate indicators, as well as evaluation guidelines based, in part, upon those assessments, that are communicated by the agency head, or an individual specifically designated by the agency head for such purpose, to senior employees, appropriate senior employee rating and reviewing officials, and PRB members. These assessments and guidelines are to be

provided at the conclusion of the appraisal period but before individual senior employee performance ratings are recommended, so that they may serve as a basis for individual performance evaluations, as appropriate. The guidance provided may not take the form of quantitative limitations on the number of ratings at any given rating level, and must conform to 5 CFR part 430, subpart B or C, as applicable;

(6) Oversight by the agency head or the individual specifically designated under paragraph (a)(5) of this section, who certifies, for a particular senior employee appraisal system, that—

(i) The senior employee appraisal process makes meaningful distinctions based on relative performance;

(ii) The results of the senior employee appraisal process take into account, as appropriate, the agency's assessment of its performance against program performance measures, as well as other relevant considerations; and

(iii) Pay adjustments, cash awards, and levels of pay based on the results of the appraisal process accurately reflect and recognize individual performance and/or contribution to the agency's performance;

(7) Accountability, so that final agency head decisions and any PRB recommendations regarding senior employee ratings consistent with 5 CFR part 430, subparts B and C, individually and overall, appropriately reflect the employee's performance expectations, relevant program performance measures, and such other relevant factors as the PRB may find appropriate; in the case of supervisory senior employees, ratings must reflect the degree to which performance standards, requirements, or expectations for individual subordinate employees clearly link to organizational

mission, GPRA strategic goals, or other program or policy objectives and take into account the degree of rigor in the appraisal of their subordinate employees;

(8) Performance differentiation, so that the system(s) includes at least one summary level of performance above fully successful, including a summary level that reflects outstanding performance, as defined in § ____402, and so that its annual administration results in meaningful distinctions based on relative performance that take into account the assessment of the agency's performance against relevant program performance measures, as described in paragraph (a)(6) of this section, employee performance expectations, and such other relevant factors as may be appropriate.

Relative performance does not require ranking senior employees against each other; such ranking is prohibited for the purpose of determining performance ratings. For equivalent systems that do not use summary ratings, the appraisal system must provide for clear differentiation of performance at the outstanding level; and

(9) Pay differentiation, so that those senior employees who have demonstrated the highest levels of individual performance and/or contribution to the agency's performance receive the highest annual summary ratings or ratings of record, as applicable, as well as the largest corresponding pay adjustments, cash awards, and levels of pay, particularly above the rate for level III of the Executive Schedule. Agencies must provide for transparency in the processes for making pay decisions, while assuring confidentiality.

(b) Consistent with the requirements in section 3(a) of the Inspector General Act of 1978, an agency's Inspector General or an official he or she designates must perform the functions listed in paragraphs (a)(5) and (6) of this section for senior employees in the Office of the Inspector General.

§ ____.405 **Procedures for certifying agency appraisal systems.**

(a) *General.* To receive system certification, an agency must provide documentation demonstrating that its appraisal system(s), in design, application, and administration, meets the certification criteria in § ____.404 as well as the procedural requirements set forth in this section.

(b) *Certification requests.* In order for an agency's appraisal system to be certified, the head of the agency or designee must submit a written request for full or provisional certification of its appraisal system(s) to OPM. Certification requests may cover an agencywide system or a system that applies to one or more agency organizations or components and must include—

(1) A full description of the appraisal system(s) to be certified, including—

- (i) Organizational and employee coverage information;
- (ii) Applicable administrative instructions and implementing guidance; and
- (iii) The system's use of rating levels that are capable of clearly differentiating among senior employees based on appraisals of their relative performance against performance expectations in any given appraisal period reflecting performance evaluation results that make meaningful distinctions based on relative performance, and which include—

(A) For the agency's senior executives covered by 5 CFR part 430, subpart C, at least four, but not more than five, summary rating levels—an outstanding level, a fully successful level, an optional level between outstanding and fully successful, a minimally satisfactory level, and an unsatisfactory level;

(B) For the agency's senior professionals covered by 5 CFR part 430, subpart B, at least three, but not more than five, summary levels—an outstanding level, a fully successful level, an optional level between outstanding and fully successful, an unacceptable level, and an optional level between fully successful and unacceptable; and

(C) For agencies not subject to 5 CFR part 430, subparts B and C, a summary rating level that reflects outstanding performance or a methodology that clearly differentiates outstanding performance, as defined in § ____.402;

(2) A clearly defined process for reviewing—

(i) The initial summary ratings and ratings of record, as applicable, of senior employees to ensure that annual summary ratings or ratings of record are not distributed arbitrarily or on a rotational basis, and

(ii) In the case of senior employees with supervisory responsibilities—

(A) The performance standards, requirements, or expectations for the employees they supervise to ensure that they clearly link to organizational mission, GPRA strategic goals, or other program and policy objectives, as appropriate, and

(B) The performance standards, requirements, or expectations and the performance ratings of the employees they supervise to ensure that they reflect distinctions in individual and organizational performance, as appropriate;

(3) Documentation showing that the appraisal system(s) meets the applicable certification criteria, as follows:

(i) For provisional certification, the requirements in § ____.404(a)(1)-(4); and

(ii) For full certification, all of the requirements in § ____.404.

(4) For full certification, data on senior executive annual summary ratings and senior professional ratings of record, as applicable (or other documentation for agencies that do not use summary ratings), for the two appraisal periods preceding the request, as well as corresponding pay adjustments, cash awards, and levels of pay provided to those senior employees; and

(5) Any additional information that OPM and OMB may require to make a determination regarding certification.

(c) *Certification actions.* At the request of an agency, the Director of OPM, at his or her discretion and in accordance with the requirements of this subpart and with OMB concurrence, may grant full or provisional certification of the agency's appraisal system(s). OPM, with OMB concurrence, may—

(1) Grant full certification of an agency's senior employee appraisal system(s) for 2 calendar years when an agency has demonstrated that it has designed and fully implemented and applied an appraisal system(s) for its senior executives or senior professionals, as applicable, that meets the certification criteria in § ____.404 and the documentation requirements of this section.

(2) Grant provisional certification of an agency's senior employee appraisal system(s) for 1 calendar year when an agency has designed, but not yet fully implemented or applied, an appraisal system(s) for its senior executives or senior professionals, as applicable, that meets the certification criteria in § ____.404. OPM may extend provisional certification into the following calendar year in order to permit an agency to take any actions needed to adjust pay based on annual summary ratings, ratings

of record, or other performance appraisal results determined during the calendar year for which the system was certified; or

(3) Suspend certification under paragraph (h) of this section if, at any time during the certification period, OPM, with OMB concurrence, determines that the agency appraisal system is not in compliance with certification criteria.

(d) Pay limitations. Absent full or provisional certification of its appraisal system(s), an agency must—

(1) Set a senior executive's rate of basic pay at a rate that does not exceed the rate for level III of the Executive Schedule, consistent with 5 CFR part 534, subpart D, when effective; and

(2) Limit aggregate compensation paid to senior employees in a calendar year to the rate for level I of the Executive Schedule, consistent with 5 CFR 530.203(b).

(e) Full Certification. (1) OPM, with OMB concurrence, may grant full certification when a review of the agency's request and accompanying documentation demonstrates that the design, application, and administration of the agency's appraisal system(s) meet the criteria in § ____.404 and the documentation requirements of this section.

(2) An agency with a fully-certified appraisal system(s) may set the rate of basic pay under 5 CFR part 534, subpart D, when effective, for a senior executive covered by a certified system at a rate that does not exceed the rate for level II of the Executive Schedule and pay senior employees covered by certified system(s) aggregate compensation in a certified calendar year in an amount up to the Vice President's salary under 3 U.S.C. 104.

(3) Full certification of an agency's appraisal system will be renewed automatically for an additional 2 calendar years, if—

(i) The agency meets the annual reporting requirements in paragraph (g) of this section; and

(ii) Based on those annual reports, OPM determines, and OMB concurs, that the appraisal system(s) continues to meet the certification criteria and procedural requirements set forth in this subpart.

(f) *Provisional certification.* (1) OPM, with OMB concurrence, may grant provisional certification when the design of an agency's appraisal system(s) for senior executives or senior professionals, as applicable, meets the requirements set forth in this subpart, but insufficient documentation exists to determine whether the actual application and administration of the appraisal system(s) meet the requirements for full certification. OPM, with OMB concurrence, may grant provisional certification to an agency more than once.

(2) During the 1-year period of provisional certification, an agency may set the rate of basic pay for a senior executive covered by the provisionally certified system at a rate that does not exceed the rate for level II of the Executive Schedule (consistent with 5 CFR part 534, subpart D, when effective) and pay senior employees covered by provisionally certified systems aggregate compensation in the certified calendar year in an amount up to the Vice President's salary under 3 U.S.C. 104 (consistent with 5 CFR part 530, subpart B).

(3) An agency must resubmit an application requesting provisional certification for every calendar year for which it intends to maintain provisional certification. An

agency with a provisionally certified appraisal system(s) may request that OPM, with OMB concurrence, grant full certification upon a showing that its performance appraisal systems for senior executives and senior professionals, as applicable, meet the certification criteria in § ____.404 and the documentation requirements in this section, particularly with respect to the implementation and administration of the system(s) over at least two consecutive performance appraisal periods.

(g) *Annual reporting requirement.* Agencies with certified appraisal systems must provide OPM with a general summary of the annual summary ratings and ratings of record, as applicable, and rates of basic pay, pay adjustments, cash awards, and aggregate total compensation (including any lump-sum payments in excess of the applicable aggregate limitation on pay that were paid in the current calendar year as required by § 530.204) for their senior employees covered by a certified appraisal system at the conclusion of each appraisal period that ends during a calendar year for which the certification is in effect, in accordance with OPM instructions.

(h) *Suspension of Certification.* (1) When OPM determines that an agency's certified appraisal system is no longer in compliance with certification criteria, OPM, with OMB concurrence, may suspend such certification, as provided in paragraph (c)(3) of this section.

(2) An agency's system certification is automatically suspended when OPM withdraws performance appraisal system approval or mandates corrective action because of misapplication of the system as authorized under §§ 430.210(c), 430.312(c), and _____.403(e).

(3) OPM will notify the head of the agency at least 30 calendar days in advance of the suspension and the reason(s) for the suspension, as well as any expected corrective action. Upon such notice, and until its system certification is reinstated, the agency must set a senior executive's rate of basic pay under 5 CFR part 534, subpart D, when effective, at a rate that does not exceed the rate for level III of the Executive Schedule. While certification is suspended, an agency must limit aggregate compensation received in a calendar year by a senior employee to the rate for level I of the Executive Schedule. Pay adjustments, cash awards, and levels of pay in effect prior to that notice will remain in effect unless OPM finds that any such decision and subsequent action was in violation of law, rule, or regulation.

(4) OPM, with OMB concurrence, may reinstate an agency's suspended certification only after the agency has taken appropriate corrective action.

(5) OPM may reinstate the certification of an appraisal system that has been automatically suspended under paragraph (h)(2) of this section upon the agency's compliance with the applicable OPM-mandated corrective action(s).

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OFFICE OF PERSONNEL MANAGEMENT

5 CFR PARTS 451, 530, 534, and 575

RIN: 3206-AK34

**Senior Executive Service Pay and Performance Awards and
Aggregate Limitation on Pay**

AGENCY: Office of Personnel Management.

ACTION: Proposed rule.

SUMMARY: The Office of Personnel Management (OPM) is issuing proposed regulations to implement statutory provisions that establish a new performance-based pay system for the Senior Executive Service (SES) and a higher aggregate limitation on pay for SES members and employees in senior-level (SL) and scientific or professional (ST) positions. These regulations prescribe the criteria for the administration of rates of basic pay and performance awards under the SES performance-based pay system and the rules for applying the aggregate limitation on pay.

DATE: Comments must be received on or before [INSERT DATE 30 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER].

ADDRESSES: Send or deliver comments to Donald J. Winstead, Deputy Associate Director for Pay and Performance Policy, Office of Personnel Management, Room 7H31, 1900 E Street,

NW., Washington, DC 20415-8200; by FAX at (202) 606-0824; or by e-mail at pay-performance-policy@opm.gov.

FOR FURTHER INFORMATION CONTACT: Jo Ann Perrini by telephone at (202) 606-2858; by FAX at (202) 606-0824; or by email at pay-performance-policy@opm.gov.

SUPPLEMENTARY INFORMATION: The Office of Personnel Management (OPM) is issuing proposed regulations to implement two statutory provisions that strengthen the linkage between the performance and pay of an agency's Senior Executive Service (SES), senior-level (SL), and scientific or professional (ST) employees. The new SES performance-based pay system requires agencies to make decisions on setting and adjusting rates of basic pay for SES members based on individual performance and/or contribution to the agency's performance as determined under a rigorous performance management system. OPM, jointly with the Office of Management and Budget (OMB), also is issuing regulations to prescribe the criteria and procedures for obtaining certification of an agency's performance appraisal system(s) for SES members and SL/ST employees. Agencies must receive certification of their performance appraisal systems to use the higher base pay limitation for SES members and to use the higher aggregate limitation on pay for SES and SL/ST employees. In these regulations, we interchangeably use the terms "SES members" and "senior executives" to mean members of the Senior Executive Service. In addition, we refer to SL/ST employees as "senior professionals."

On January 13, 2004, OPM issued interim regulations to establish the new SES performance-based pay system (69 FR 2048). In those interim regulations, OPM established the structure of the SES rate range, rules for conversion to the new pay system, and the criteria for providing pay adjustments to SES members on or after the first applicable pay period beginning on or after January 1, 2004 (January 11, 2004, for most employees). OPM has issued additional

guidance on the SES pay system at <http://www.opm.gov/oca/compmemo/index.asp>. In these proposed regulations, we are prescribing rules for establishing and adjusting SES rates of basic pay, paying performance awards to senior executives, and applying the aggregate limitation on pay if an agency receives certification of an applicable performance appraisal system under 5 U.S.C. 5307(d).

New SES Performance-Based Pay System

Section 1125 of Public Law 108-136 (November 24, 2003) amended 5 U.S.C. 5382 to establish a new performance-based pay system for the SES that has an “open-range” pay band. Each member of the SES will be paid at one of the rates within the SES rate range. In the interim regulations issued on January 13, 2004, OPM established the minimum rate of basic pay for the SES rate range at the rate of basic pay (excluding locality payments) payable under 5 U.S.C. 5376 for senior-level positions (\$104,927 in 2004). OPM established the maximum rate of basic pay for the SES rate range at the rate for level III of the Executive Schedule (\$145,600 in 2004). These proposed regulations establish the maximum rate of basic pay for the SES rate range at the rate for level II of the Executive Schedule (\$158,100 in 2004) for those agency senior executive performance appraisal systems that have been certified by OPM, with OMB concurrence, in accordance with 5 U.S.C. 5307 and OPM’s regulations at 5 CFR part 430, subpart D. To receive certification, an agency must demonstrate that the applicable performance appraisal system makes meaningful distinctions based on relative performance.

The minimum rate of basic pay for the SES rate range will increase consistent with any increase in the minimum rate of basic pay for senior-level positions under 5 U.S.C. 5376, and the maximum rate of basic pay for the SES rate range will increase with any increase in the rates for levels II and III of the Executive Schedule. Section 534.404(f) allows agencies to review an

initial determination to adjust a rate of basic pay and grant an additional increase, if warranted, to a senior executive if there is an additional increase in the rates for the Executive Schedule that is made effective on the first day of the first pay period beginning on or after January 1 of that year. Such additional adjustments in pay must be made effective as of the effective date of the initial determination to adjust the senior executive's rate of basic pay.

Conversion to the new SES Pay System

On January 13, 2004, OPM issued interim regulations on conversion to the new SES pay system. In these proposed regulations, we have revised § 534.406 to further clarify the rules for converting senior executives to the new system. Generally, upon conversion to the new SES pay system, an SES member was entitled to a new rate of basic pay equal to the existing rate of basic pay plus any applicable locality payment to which the employee was entitled immediately before the first day of the first applicable pay period beginning on or after January 1, 2004 (January 10, 2004, for most employees). However, under section 1125(c)(2) of Public Law 108-136, an SES member's rate of basic pay, plus any applicable locality-based comparability payment under 5 U.S.C. 5304 to which the employee was entitled on November 24, 2003, may not be reduced for 1 year after the first day of the first applicable pay period beginning on or after January 1, 2004 (January 11, 2004, for most employees). If an SES member's rate of basic pay, plus any applicable locality-based comparability payment under 5 U.S.C. 5304 to which the employee was entitled on November 24, 2003, is higher than the rate in effect on January 10, 2004, the agency must use the higher rate for the purpose of converting the SES member to the SES pay system.

On January 11, 2004, certain SES members who were assigned to positions that have geographic mobility requirements and who were assigned outside the 48 contiguous States and

the District of Columbia continued to receive their rate of basic pay in effect on January 10, 2004, or, if higher, the rate of basic pay in effect on November 23, 2003. However, upon reassignment to a position in the 48 contiguous States or the District of Columbia, these employees are entitled to have their rates of basic pay converted to a new SES rate of basic pay that equals their current rate of basic pay, plus the amount of locality pay authorized under 5 U.S.C. 5304 for the applicable locality pay area. A senior executive who is reassigned to a locality pay area is not automatically entitled to a rate of basic pay that is higher than the rate for level III of the Executive Schedule. If the senior executive's rate of basic pay did not exceed the rate for level III of the Executive Schedule while assigned to a position outside the 48 contiguous States or the District of Columbia, the senior executive's converted rate of basic pay may not exceed the rate for level III of the Executive Schedule upon reassignment to a locality pay area. Of course, an agency may choose to consider the applicable locality payment when setting or adjusting the rate of basic pay of a senior executive who transfers to a position within the 48 contiguous States, but whose position is not subject to a geographic mobility requirement.

On January 11, 2004, an SES law enforcement officer (LEO) continued to receive his or her rate of basic pay, plus any applicable special geographic pay adjustment established for LEOs under section 404(a) of the Federal Employees Pay Comparability Act of 1990 (Public Law 101-509) to which he or she was entitled on January 10, 2004, or, if higher, his or her rate of basic pay plus the LEO special geographic pay adjustment in effect on November 23, 2003. On March 3, 2004, the President issued Executive Order 13332, which increased General Schedule rates of pay and locality-based comparability payments effective on the first day of the first applicable pay period beginning on or after January 1, 2004 (January 11, 2004, for most employees). As a result, the remaining LEO special geographic pay adjustment in Boston was

terminated as of January 11, 2004, because a higher locality pay percentage now applies to LEOs. Agencies must correct the rate of basic pay for SES law enforcement officers in Boston and base any pay adjustments approved on or after January 11, 2004, on the senior executive's newly reconstructed rate of basic pay. (See <http://www.opm.gov/oca/compmemo/2004/2004-05.asp>.) The newly reconstructed rate is the senior executive LEO's rate of basic pay.

Setting and Adjusting Rates of Pay for SES Members

The new subpart D in 5 CFR part 534 prescribes the rules for setting and adjusting rates of basic pay and granting awards to SES members. Section 534.404(g) requires agencies to establish a plan for setting and adjusting rates of basic pay for their senior executives. The agencies' plans may establish policies on the minimum increase in pay that may be offered to current employees upon initial appointment to the SES. An agency may set and adjust a senior executive's rate of basic pay at any rate within the applicable SES rate range, based on individual performance and/or contribution to the agency's performance, as determined under a rigorous performance management system. In this regard, agencies may consider any unique skills, qualifications, or competencies that the individual possesses, and their significance to the agency's mission, as well as the individual's current responsibilities. Agencies must ensure that only those senior executives who have demonstrated the highest levels of individual performance and/or made the greatest contributions to the agency's performance or, in the case of newly-appointed senior executives, those who possess superior leadership or other competencies, receive the highest rates of basic pay and pay adjustments.

Setting rates of basic pay higher than level III of the Executive Schedule. Rates of basic pay higher than the rate for level III of the Executive Schedule but less than or equal to the rate

for level II of the Executive Schedule generally should be reserved for those senior executives who have demonstrated the highest levels of individual performance and/or made the greatest contributions to agency performance, as determined by the agency through the administration of its applicable performance appraisal system for senior executives, or, in the case of newly-appointed senior executives, those who possess superior leadership or other competencies, consistent with the agency's strategic human capital plan. For example, rates of pay higher than the rate for level III of the Executive Schedule should be reserved for a senior executive with an exceptionally meritorious accomplishment, for a senior executive who is assigned to a position with substantially greater scope and responsibility, or for a senior executive who is critical to the mission of the agency. In all cases, setting pay above the rate for level III of the Executive Schedule must be approved by the agency head or designee who performs the functions described in 5 CFR 430.404(a)(5) and (6) (oversight of senior executive appraisal process and communication of performance assessment and evaluation guidelines).

Setting pay upon initial appointment to the SES. Upon initial appointment to an SES position, an authorized agency official may set an SES member's rate of basic pay at any rate within the SES rate range consistent with the restrictions on setting pay above the rate for level III of the Executive Schedule. The authorized agency official must determine the new senior executive's appropriate rate of basic pay based on the nature and quality of the individual's experience, qualifications, and accomplishments as they relate to the requirements of the SES position, as well as the individual's current responsibilities.

Adjusting SES rates of basic pay. A senior executive who receives an annual summary rating of outstanding must be considered for an annual pay increase. A senior executive who receives a summary performance rating of less than fully successful may not receive an increase

in pay for the current performance appraisal period. Subject to the 1-year prohibition in 5 U.S.C 5382(c) on reducing a senior executive's rate of basic pay (see § 534.406(b)), an authorized agency official may reduce a senior executive's rate of basic pay for performance and/or disciplinary reasons. Such a reduction in pay for a career senior executive may not exceed 10 percent (compared to the former limitation on reductions in pay of one SES rate, or approximately 5 percent of basic pay). Any pay reduction may be appealed to the head of the agency. The agency head's decision is final and non-reviewable.

12-Month rule. Generally, an authorized agency official may adjust (i.e., increase or reduce) the rate of basic pay of a senior executive not more than once in any 12-month period. The setting of pay upon initial appointment or reappointment to the SES and adjusting an SES rate of basic pay are considered pay adjustments for this purpose. However, under § 534.404(c)(4), an authorized agency official may approve an increase in a senior executive's rate of basic pay more than once during a 12-month period where the head of an agency or designee who performs the functions described in 5 CFR 430.404(a)(5) and (6) determines that an additional increase is warranted (1) for an exceptionally meritorious accomplishment, (2) for a senior executive who is reassigned to a position with substantially greater scope and responsibility, (3) for a senior executive who is critical to the mission of the agency and who would be likely to leave the agency in the absence of a pay increase, or (4) to align a senior executive with the agency's senior executive appraisal and pay adjustment cycle (e.g., in the case of a senior executive who was appointed to an SES position within the past 12 months or a senior executive who was transferred to an SES position from an agency with a different senior executive appraisal and pay adjustment cycle within the past 12 months).

OPM recognizes that as the rate of basic pay for levels II and III of the Executive Schedule are increased, the maximum rate of the SES rate range for an SES performance appraisal system also increases, which disadvantages agencies that have already granted pay increases to their senior executives following their SES performance appraisal periods. We therefore solicit the views of commenters on a proposal to establish an additional exception to the 12-month rule that would permit agencies, at their discretion, to grant an additional pay increase to a senior executive whose rate of basic pay is equivalent to the rate for level II or level III when the applicable maximum rate is increased and becomes effective after an agency has already granted a pay increase to the senior executive. An additional pay increase under this circumstance would not be considered a pay adjustment for the purpose of applying the 12-month rule.

Adjustments in pay prior to certification of performance appraisal system(s). Section 534.404(d) authorizes agencies to increase a senior executive's rate of basic pay on the first day of the first applicable pay period beginning on or after January 1, 2004, or on any date thereafter. Prior to obtaining certification of the agency's performance appraisal system(s) for senior executives under 5 CFR part 430, subpart D, an agency may increase a senior executive's rate of basic pay up to the rate for level III of the Executive Schedule where the individual's performance and/or contributions so warrant and the senior executive is otherwise eligible for such a pay increase (i.e., he or she did not receive a pay adjustment during the previous 12-month period). On January 20, 2004, the Director of OPM delegated to the heads of agencies the authority to make limited exceptions to the 12-month rule. (See <http://www.opm.gov/oca/compmemo/2004/2004-04.asp>.) Because we are proposing to provide agencies, in these regulations, with authority to make exceptions to the 12-month rule under

certain conditions, the Director of OPM intends to withdraw this delegated authority upon issuance of final regulations on SES pay and performance awards. An adjustment in pay prior to certification is considered a pay adjustment for the purpose of applying § 534.404(c).

Adjustments in pay after certification of performance appraisal system(s). Section 534.404(e) authorizes an agency that receives certification of its performance appraisal system(s) for senior executives under 5 CFR part 430, subpart D, to increase a senior executive's rate of basic pay up to the rate for level II of the Executive Schedule if warranted and the senior executive is otherwise eligible for such a pay increase (i.e., he or she did not receive a pay adjustment during the previous 12-month period). In § 534.404(c)(4), OPM has provided agencies with authority to make exceptions to the 12-month rule under certain limited conditions. Agencies must comply with the limitations in § 534.403(a)(2) for setting a senior executive's rate of basic pay higher than the rate for level III of the Executive Schedule and reserve these higher rates of pay for those senior executives who have demonstrated the highest levels of individual performance and/or made the greatest contributions to the agency's performance or, in the case of a newly-appointed senior executive, those who possess superior leadership or other competencies. A post-certification adjustment in pay is considered a pay adjustment for the purpose of applying § 534.404(c).

No reduction in pay upon transfer to another agency or suspension of certification. A senior executive whose rate of basic pay is higher than the rate for level III of the Executive Schedule may not suffer a reduction in pay as a result of transfer from an agency with a maximum SES rate of basic pay equal to the rate for level II of the Executive Schedule to an agency with a maximum SES rate of basic pay equal to the rate for level III of the Executive Schedule (§ 534.404(h)(2)) or as the result of a decision to suspend certification of the applicable

performance appraisal system under 5 CFR part 430, subpart D (§ 534.403(b)). The senior executive will continue to receive his or her current SES rate and is not eligible for a pay increase until the employing agency's applicable performance appraisal system is certified.

Setting rates of basic pay following a break in SES service. Upon reappointment to the SES, an agency may set the rate of basic pay of a former senior executive at any rate within the SES rate range if there has been a break in SES service of more than 30 days. If there has been a break in SES service of 30 days or less, the senior executive's rate of basic pay must be set at a rate at least equivalent to the employee's former SES rate of basic pay.

Performance Awards. As a result of the implementation of the new SES performance-based pay system, the limit on the total amount of performance awards that may be granted in a fiscal year and the actual amount of an individual performance award that may be granted will be greater than in the past, since both are derived from an SES rate of basic pay that now includes any applicable locality payment. To determine the total amount of performance awards that may be granted in FY 2004, agencies must include any applicable locality payments in effect at the end of FY 2003 for the purpose of applying the limitations in § 534.405(b)(1) and (2).

Additional Payments. Agencies must review any determination to provide additional payments to a senior executive that are calculated based on the senior executive's rate of basic pay (e.g., retention allowances and extended assignment incentives). As a result of conversion to the new SES pay system, a senior executive's rate of basic pay has increased significantly to include locality payments. Payments that are calculated based on a senior executive's rate of basic pay also may have increased significantly.

Aggregate Limitation on Pay

Higher aggregate limitation on pay for senior executives and senior professionals.

Section 1322 of the Chief Human Capital Officers Act of 2002 (Public Law 107-296, Title XIII, November 25, 2002) added a new paragraph (d) to 5 U.S.C. 5307 that permits agencies with certified appraisal systems for their senior executives and senior professionals, as applicable, to apply a higher annual aggregate limitation on pay to those employees. The higher annual aggregate limitation on pay is equivalent to the total annual compensation payable to the Vice President, under 3 U.S.C. 104, on the last day of the applicable calendar year (\$203,000 in 2004). Agencies that are not covered by the performance appraisal system requirements set forth in 5 U.S.C., chapter 43, but which are subject to the aggregate limitation in 5 U.S.C. 5307, also must have a certified appraisal system in order to apply the higher aggregate limitation on pay to their senior executives and senior professionals.

Agencies without certification must continue to apply an annual aggregate limitation on pay equivalent to the rate for level I of the Executive Schedule (\$174,500 in 2004). The level I aggregate limitation also continues to apply to (1) other employees covered by 5 U.S.C. 5307; (2) employees paid under the Executive Schedule established under 5 U.S.C., chapter 53, subchapter II; and (3) equivalent categories of employees whose pay is linked directly to a rate of pay under the Executive Schedule. In addition, section 1322 of the Act increases the annual aggregate limitation on pay for judicial branch employees paid under 28 U.S.C. 332(f), 603, and 604. It also authorizes the Director of the Administrative Office of the United States Courts to prescribe regulations to implement the higher annual aggregate limitation on pay. The law requires the regulations of the Administrative Office of the United States Courts to be consistent with OPM's and OMB's regulations regarding certification.

Definitions. In § 530.202, we have revised the definition of aggregate compensation to clarify that it excludes student loan repayments under 5 U.S.C. 5379 and nonforeign area cost-of-living allowances under 5 U.S.C. 5941(a)(1). We have added a definition of aggregate limitation to avoid repeated extended references to the two statutory limitations—i.e., the limitation in effect at the end of the calendar year that is equal to the rate for level I of the Executive Schedule or the rate payable to the Vice President, whichever limitation applies to the employee. Finally, we have revised the definition of estimated aggregate compensation to clarify that the term refers to the estimated compensation an employee would receive but for the application of the aggregate limitation to future payments. At any point during a calendar year, an agency may estimate the aggregate compensation that would be received but for application of the aggregate limitation to future payments. Excess amounts already deferred for payment at the beginning of the next calendar year are not considered in computing the current estimate, since those payments are not projected to be received in the current calendar year.

Also in § 530.202, we have added extended assignment incentives authorized under 5 U.S.C. 5757 to the list of payments that are covered by the definition of aggregate compensation and discretionary payments. Extended assignment incentives, which were established by section 207 of Public Law 107-273 (November 2, 2002), permit the head of an Executive agency to pay an extended assignment incentive to certain Federal employees assigned to positions located in a territory or possession of the United States, the Commonwealth of Puerto Rico, or the Commonwealth of the Northern Mariana Islands.

Deferring Discretionary Payments. We have clarified § 530.203(d) to require that a retention allowance must be reduced or terminated before deferring any other discretionary payment, consistent with 5 CFR 575.307(a). However, for a discretionary payment to be

considered deferred, its payment in the current calendar year must be required by a mandatory personnel policy or it must have been officially approved to be paid within the current calendar year. Otherwise, the setting of the payment date for a discretionary payment in the next calendar year is not a deferral under these regulations and has no effect on the payment of retention allowances in the current year.

Overestimating an Employee's Aggregate Compensation. In § 530.203, we have added a new paragraph (h) to address situations where an agency overestimates an employee's aggregate annual compensation for the calendar year at an earlier point in the year and, as a result, unnecessarily defers payments. In this case, an agency may make corrective payments in the current calendar year rather than waiting to make the payments at the beginning of the next calendar year.

Change in Aggregate Limitation on Pay. In § 530.203(g) and (h), we have provided rules for taking corrective actions when the aggregate limitation is increased or decreased during a calendar year as a result of gaining or losing certification of a senior executive performance appraisal system.

Lump-Sum Payments in Excess of Aggregate Limitation on Pay. We have amended § 530.204(c) to require that if an employee transfers to another agency, the gaining agency is responsible for making any lump-sum payment in excess of the aggregate limitation. The previous employing agency must provide the gaining agency with documentation regarding the employee's excess amount. The previous employing agency must provide a fund transfer equal to the total cost of the lump-sum payment to the gaining agency through the Department of the Treasury's Intra-Governmental Payment and Collection System. If an employee leaves Federal

service, the current employing agency is responsible for making the lump-sum payment to the employee as provided in § 530.204(d).

Recordkeeping. In § 530.205, we have added a number of specific recordkeeping requirements that deal with the source and payment of deferred excess amounts, consistent with other provisions in the regulations.

Plain Language. OPM is also taking this opportunity to revise and reorganize part 530, subpart B, Aggregate Limitation on Pay, to improve its readability. We also have made some substantive changes to the regulations to assist agencies in administering them. In addition, we have replaced the verb “shall” with “must” for added clarity and readability. In this regard, any provision using the verb “must” is intended to have the same meaning and effect as previous provisions using “shall.”

Extended Award Authority

The Federal Employees Pay Comparability Act of 1990 established a specific authority to pay performance-based cash awards to employees paid under the General Schedule (GS) (5 U.S.C. 4505a). This law specifies that the President may extend application of this authority to groups of employees not covered by the General Schedule at the request of the agency head. This extension authority was delegated by E.O. 12828 to the Director of OPM. Over the years some agencies have incorrectly cited this law as the authority under which they pay performance-based awards to non-GS employees. OPM is extending by regulation the provisions of 5 U.S.C. 4505a to non-GS employees covered by 5 U.S.C. chapter 45 and 5 CFR part 451 who are not otherwise eligible for performance-based cash awards under another specific statutory authority, including 5 U.S.C. 5384 (SES performance awards). Extending this

authority will avoid incorrect references and citations and provide agencies with a specific authority to grant performance-based cash awards to their SL/ST (and other non-GS) employees.

Recruitment and Relocation Bonuses and Retention Allowances

We have made technical amendments to the regulations on recruitment and relocation bonuses and retention allowances in 5 CFR part 575 to conform to the changes made to the aggregate limitation on pay in 5 CFR part 531, subpart B.

Regulatory Flexibility Act

I certify that these regulations will not have a significant economic impact on a substantial number of small entities because they will apply to only Federal agencies and employees.

E.O. 12866, Regulatory Review

This rule has been reviewed by the Office of Management and Budget in accordance with E.O. 12866.

List of Subjects in parts 451, 530, 534, 575

Decorations, medals, awards, Government employees, Law Enforcement Officers, Reporting and recordkeeping requirements, Hospitals, Students, and Wages.

Office of Personnel Management

Kay Coles James
Director

Accordingly, OPM is proposing to amend parts 451, 530, 534, and 575 of title 5 of the Code of Federal Regulations as follows:

PART 451—EMPLOYEE AWARDS

Subpart A—Agency Awards

1. The authority citation for part 451 continues to read as follows:

Authority: 5 U.S.C. 4302, 4501-4509; E.O. 11438, 12828.

2. In § 451.101 paragraph (d), remove the reference “534.403” and add the reference “534.405” in its place, and add a new paragraph (e) to read as follows:

§ 451.101 Authority and coverage.

* * * * *

(e) An agency may grant performance-based cash awards (i.e., on the basis of a rating of record) under the authority of 5 U.S.C. 4505a and the provisions of this part to eligible non-GS employees who are covered by 5 U.S.C. chapter 45 and this part, and who are not otherwise covered by an explicit statutory authority for the payment of such awards, including 5 U.S.C. 5384 (SES performance awards).

3. In § 451.104(a)(3), remove the reference “534.403” and add the reference “534.405” in its place.

4. Part 530, subpart B, is revised to read as follows:

PART 530 -- PAY RATES AND SYSTEMS (GENERAL)

Subpart B -- Aggregate Limitation on Pay

Sec.

530.201 Purpose.

530.202 Definitions.

530.203 Administration of aggregate limitation on pay.

530.204 Payment of excess amounts.

530.205 Records.

Authority: 5 U.S.C. 5305 and 5307; E.O. 12748, 56 FR 4521, 3 CFR, 1991 Comp., p. 316; subpart B also issued under §§ 302(c) and 404(c) of the Federal Employees Pay Comparability Act of 1990 (Public Law 101-509), 104 Stat. 1462 and 1466, respectively; subpart C also issued under sec. 4 of the Performance Management and Recognition System Termination Act of 1993 (Public Law 103-89), 107 Stat. 981; and sec. 1322 of the Chief Human Capital Officers Act of 2002 (Public Law 107-296, Title XIII, November 25, 2002), 116 Stat. 2135.

Subpart B -- Aggregate Limitation on Pay

§ 530.201 Purpose.

This subpart establishes regulations for limiting an employee's aggregate annual compensation. An employee's aggregate compensation received in any given calendar year may not exceed the rate of pay for level I of the Executive Schedule or the rate payable to the Vice President at the end of the calendar year, whichever is applicable to the employee based on the certification status of the performance appraisal system covering that employee under 5 CFR part 430, subpart D. These regulations must be applied in conjunction with 5 U.S.C. 5307.

§ 530.202 Definitions.

In this subpart:

Agency means an executive agency as defined at 5 U.S.C. 105.

Aggregate compensation means the total of—

(1) Basic pay received as an employee of the executive branch or as an employee outside the executive branch to whom the General Schedule applies;

(2) Locality payments under 5 U.S.C. 5304; continued rate adjustments under 5 CFR part 531, subpart G; or special pay adjustments for law enforcement officers under section 404 of the Federal Employees Pay Comparability Act of 1990 (Public Law 101-509);

- (3) Premium pay under 5 U.S.C. chapter 53, subchapter IV;
- (4) Premium pay under 5 U.S.C. chapter 55, subchapter V;
- (5) Incentive awards and performance-based cash awards under 5 U.S.C. chapters 45 and 53;
- (6) Recruitment and relocation bonuses under 5 U.S.C. 5753;
- (7) Retention allowances under 5 U.S.C. 5754 and extended assignment incentives under 5 U.S.C. 5757;
- (8) Supervisory differentials under 5 U.S.C. 5755;
- (9) Post differentials under 5 U.S.C. 5925;
- (10) Danger pay allowances under 5 U.S.C. 5928;
- (11) Post differentials based on environmental conditions for employees stationed in nonforeign areas under 5 U.S.C. 5941(a)(2);
- (12) Physicians' comparability allowances under 5 U.S.C. 5948;
- (13) Continuation of pay under 5 U.S.C. 8118;
- (14) Lump-sum payments in excess of the aggregate limitation on pay as required by § 530.204; and
- (15) Other similar payments authorized under title 5, United States Code, excluding—
 - (i) Overtime pay under the Fair Labor Standards Act of 1938, as amended, and 5 CFR part 551;
 - (ii) Severance pay under 5 U.S.C. 5595;
 - (iii) Lump-sum payments for accumulated and accrued annual leave upon separation under 5 U.S.C. 5551 or 5552;

(iv) Back pay awarded to an employee under 5 U.S.C. 5596 because of an unjustified personnel action;

(v) Student loan repayments under 5 U.S.C. 5379; and

(vi) Nonforeign area cost-of-living allowances under 5 U.S.C. 5941(a)(1).

Aggregate limitation means the limitation on aggregate compensation received in any given calendar year as established by 5 U.S.C. 5307. For an executive branch employee (including employees in Senior Executive Service positions paid under 5 U.S.C. 5383 and employees in senior-level or scientific or professional positions paid under 5 U.S.C. 5376), a General Schedule employee in the legislative branch, or General Schedule employee in the judicial branch (excluding those paid under 28 U.S.C. 332(f), 603, and 604), the limitation on aggregate compensation is equal to the rate for level I of the Executive Schedule in effect at the end of the applicable calendar year. For an employee in a Senior Executive Service position paid under 5 U.S.C. 5383 and an employee in a senior-level or scientific or professional position paid under 5 U.S.C. 5376 covered by an applicable performance appraisal system that has been certified under 5 CFR part 430, subpart D, the limitation on aggregate compensation is equal to the total annual compensation payable to the Vice President under 3 U.S.C. 104 at the end of a calendar year.

Basic pay means the total amount of pay received at a rate fixed by law or administrative action for the position held by an employee, before any deductions. Basic pay includes night and environmental differentials for prevailing rate employees under 5 U.S.C. 5343(f) and 5 CFR 532.511. Basic pay excludes additional pay of any other kind, including locality payments under 5 U.S.C. 5304.

Discretionary payment means a payment an agency has discretion to make or not to make to an employee. A retention allowance under 5 U.S.C. 5754 and an extended assignment incentive under 5 U.S.C. 5757 are discretionary payments. However, other payments that are preauthorized to be made to an employee at a regular fixed rate each pay period are not discretionary payments.

Employee has the meaning given that term in 5 U.S.C. 2105.

Estimated aggregate compensation means the agency's projection of the aggregate compensation an employee actually would receive during a calendar year but for application of the aggregate limitation to future payments. This projection must be based upon known factors. Estimated aggregate compensation includes—

- (1) The total amount of basic pay the employee will receive during the calendar year;
- (2) Any lump-sum payment of excess amounts from a previous calendar year, as described in § 530.204;
- (3) The total amount of nondiscretionary payments the employee would be entitled to receive during the calendar year; and
- (4) The total amount of discretionary payments the employee would be authorized to receive during the calendar year.

§ 530.203 Administration of aggregate limitation on pay.

(a) Except as provided in paragraph (b) of this section, no executive branch employee or General Schedule employee in the legislative branch (or General Schedule employee in the judicial branch, excluding those paid under 28 U.S.C. 332(f), 603, and 604), may receive any allowance, differential, bonus, award, or other similar cash payment under title 5, United States Code, in any calendar year which, in combination with the employee's basic pay (whether

received under title 5, United States Code, or otherwise), would cause the employee's aggregate compensation to exceed the rate for level I of the Executive Schedule on the last day of that calendar year (i.e., the aggregate limitation).

(b)(i) Subject to paragraph (b)(ii) of this section, an employee in a Senior Executive Service position paid under 5 U.S.C. 5383 and an employee in a senior-level or scientific or professional position paid under 5 U.S.C. 5376 may not receive any allowance, differential, bonus, award, or other similar cash payment under title 5, United States Code, in any calendar year which, in combination with the employee's basic pay, would cause the employee's aggregate compensation to exceed the rate of pay for level I of the Executive Schedule.

(ii) An employee covered by a performance appraisal system that has been certified under 5 CFR part 430, subpart D, may not receive any allowance, differential, bonus, award, or other similar cash payment under title 5, United States Code, in any calendar year which, in combination with the employee's basic pay, would cause the employee's aggregate compensation to exceed the total annual compensation payable to the Vice President under 3 U.S.C. 104 on the last day of that calendar year (i.e., the aggregate limitation).

(iii) An agency must make corrective actions as provided in paragraphs (g) and (h) of this section if the agency underestimated or overestimated an employee's aggregate compensation in a calendar year as a result of receiving or losing certification of its applicable performance appraisal system under 5 CFR part 430, subpart D.

(c) The aggregate limitations described in paragraphs (a) and (b) of this section apply to the aggregate compensation an employee actually received during the calendar year without regard to when the compensation was earned.

(d) When an agency authorizes a discretionary payment for an employee, the agency must defer any portion of such payment that, when added to the estimated aggregate compensation the employee is projected to receive, would cause the employee's aggregate compensation during the calendar year to exceed the applicable aggregate limitation. Any portion of a discretionary payment deferred under this paragraph must be available for payment as provided in § 530.204. Special rules apply to the authorization and payment of a retention allowance, which may not be deferred. (See 5 CFR 575.306(b) and 575.307(a).) A retention allowance must be reduced or terminated before deferring any other type of discretionary payment, as long as the other discretionary payment is required to be paid within the current calendar year under a mandatory personnel policy or has been officially approved by an authorized agency official for payment within the current calendar year. When a discretionary payment is authorized but not required to be paid in the current calendar year, an agency official's decision to set the payment date in the next calendar year is not considered a deferral under this paragraph.

(e) An agency may not defer or discontinue nondiscretionary payments for any period of time to make a discretionary payment that would otherwise cause an employee's pay to exceed the applicable aggregate limitation. An agency may not defer or discontinue basic pay under any circumstance.

(f) If, after an agency defers discretionary payments as required by paragraph (d) of this section, the estimated aggregate compensation to which an employee is entitled exceeds the applicable aggregate limitation, the agency must defer all nondiscretionary payments (other than basic pay) as necessary to avoid payments in excess of that limitation. An agency must defer all nondiscretionary payments at the time when otherwise continuing to pay such payments would

cause an employee's estimated aggregate compensation for that calendar year to exceed the applicable aggregate limitation. An agency must pay any portion of a nondiscretionary payment deferred under this paragraph at a later date, as provided in § 530.204.

(g)(1) If an agency determines that it underestimated an employee's aggregate compensation at an earlier date in the calendar year, or the aggregate limitation applicable to the employee is reduced during the calendar year, the sum of the employee's remaining payments of basic pay may exceed the difference between the aggregate compensation the employee has actually received to date in that calendar year and the applicable aggregate limitation. In such cases, the employee will become indebted to the Federal Government for any amount paid in excess of the applicable aggregate limitation. The head of the agency may waive the debt under 5 U.S.C. 5584, if warranted.

(2) To the extent that any excess amount is attributable to amounts that should have been deferred and would have been payable at the beginning of the next calendar year, an agency must extinguish the excess amount on January 1 of the next calendar year. As part of the correction of the error, the agency must deem the excess amount to have been paid on January 1 of the next calendar year (when the debt was extinguished) as if it were a deferred excess payment, as described in § 530.204, and must consider this deemed deferred excess payment to be part of the employee's aggregate compensation for the new calendar year.

(3) To the extent that any excess amount is attributable to retention allowances that the agency inadvertently did not reduce or terminate under 5 CFR 575.307(a), the employee will become indebted to the Federal Government for any amount attributable to retention allowance payments that were paid in excess of the applicable aggregate limitation. The head of the agency may waive the debt under 5 U.S.C. 5584, if warranted.

(h) If an agency determines that it overestimated an employee's aggregate compensation at an earlier date in the calendar year, which caused the agency to defer payments unnecessarily under this section, or the aggregate limitation applicable to the employee is increased during the calendar year, the agency may make appropriate corrective payments to the employee during the calendar year, notwithstanding § 530.204.

§ 530.204 Payment of excess amounts.

(a) An agency must pay the amounts that were deferred because they were in excess of the aggregate limitation (as described in § 530.203) as a lump-sum payment at the beginning of the following calendar year, except as otherwise provided in this section. This payment is part of the employee's aggregate compensation for the new calendar year.

(b) If a lump-sum payment under paragraph (a) of this section causes an employee's estimated aggregate compensation to exceed the aggregate limitation in the current calendar year, an agency must consider only the employee's basic pay that is expected to be paid in the current year in determining the extent to which the lump-sum payment may be paid. An agency must defer all other payments, as provided in § 530.203, in order to pay as much of the lump-sum excess amount as possible. Any payments deferred under this paragraph, including any portion of the lump-sum excess amount that was not payable, are payable at the beginning of the next calendar year, as provided in paragraph (a) of this section.

(c) If an employee transfers to another agency, the gaining agency is responsible for making any lump-sum payment required by paragraph (a) of this section. The previous employing agency must provide the gaining agency with documentation regarding the employee's excess amount, as provided in § 530.205. The previous employing agency must provide a fund transfer equal to the total cost of the lump-sum payment to the gaining agency

through the Department of the Treasury's Intra-Governmental Payment and Collection System. If an employee leaves Federal service, the employing agency is responsible for making the lump-sum payment to the employee as provided in paragraph (d) of this section.

(d) An agency must pay any excess amount regardless of the calendar year limitation under the following conditions:

(1) If an employee dies, the employing agency must pay the entire excess amount as part of the settlement of accounts, in accordance with 5 U.S.C. 5582.

(2) If an employee separates from Federal service, the employing agency must pay the entire excess amount following a 30-day break in service. If the individual is reemployed in the Federal service within the same calendar year as the separation, any previous payment of an excess amount must be considered part of that year's aggregate compensation for the purpose of applying the aggregate limitation for the remainder of the calendar year.

§ 530.205 Records.

An agency must maintain appropriate records to administer this subpart and must transfer such records to any agency to which an employee may transfer. An agency must make such records available to any agency that may employ the employee later during the same calendar year. An agency's records must document the source of any deferred excess amount remaining to the employee's credit at the time of separation from the agency. In the case of an employee who separates from Federal service for at least 30 days, the agency records also must document any payment of a deferred excess amount made by the agency after separation.

PART 534 – PAY UNDER OTHER SYSTEMS

5. The authority citation for part 534 is revised to read as follows:

Authority: 5 U.S.C. 1104, 3161(d), 5307, 5351, 5352, 5353, 5376, 5382, 5383, 5384, 5385, 5541, 5550a, and sec. 1125 of the “National Defense Authorization Act for FY 2004 (Public Law 108-136), 117 Stat. 1392.

Subpart D—Pay and Performance Awards Under the Senior Executive Service

6. Section 534.401 is revised to read as follows:

§ 534.401 Purpose.

This subpart contains the rules for setting and adjusting rates of basic pay and granting performance awards for members of the Senior Executive Service (SES), as provided by 5 U.S.C. 5382, 5383, and 5384. An agency must set and adjust the rate of basic pay for an SES member on the basis of the employee’s performance and/or contribution to the agency’s performance, as determined by the agency through the administration of its performance management systems for senior executives. These regulations must be read in combination with applicable statutes and with the regulations for the approval of an SES performance management system under 5 CFR part 430, subpart C, and certification of an SES performance appraisal system under 5 CFR part 430, subpart D.

7. Section 534.402 is revised to read as follows:

§ 534.402 Definitions.

In this subpart—

Agency means an executive agency or military department, as defined by 5 U.S.C. 105 and 102.

Authorized agency official means the head of an agency or an official who is authorized to act for the head of the agency in the matter concerned. The agency’s Inspector General is the

authorized agency official for senior executive positions in the Office of the Inspector General, consistent with the requirements in section 3(a) of the Inspector General Act of 1978.

Outstanding performance means performance that substantially exceeds the normally high performance expected of any senior executive, as evidenced by exceptional accomplishments or contributions to the agency's performance.

PRB means Performance Review Board, as described in § 430.310.

Rate of basic pay means the rate of pay fixed by law or administrative action for the senior executive, within the established SES rate range or, in the case of a senior executive entitled to pay retention, the employee's retained rate of pay, excluding any applicable locality-based comparability payments under 5 U.S.C. 5304, but before any deductions and exclusive of additional pay of any other kind.

Senior executive means a member of the Senior Executive Service (SES).

SES or ES rate means a rate of basic pay within the SES or ES rate range assigned to a member of the SES under § 534.403(a).

SES or ES rate range means the range of rates of basic pay established for the SES under 5 U.S.C. 5382 and § 534.403(a).

8. Redesignate §§ 534.403 and 534.405 as §§ 534.405 and 534.408 respectively.

9. Add new §534.403 to read as follows:

§ 534.403 SES rate range.

(a) SES rate range. (1) On the first day of the first applicable pay period beginning on or after January 1, 2004, the minimum rate of basic pay of the SES rate range is set at an amount equal to the minimum rate of basic pay under 5 U.S.C. 5376 for senior-level positions (excluding any locality-based comparability payment under 5 U.S.C. 5304). An SES member may not

receive less than the minimum rate of the SES rate range. Except as provided in paragraph (a)(2) of this section, the maximum rate of basic pay of the SES rate range is set at the rate for level III of the Executive Schedule. An SES member's rate of basic pay must be set at one of the rates within the SES rate range based on the senior executive's performance and/or contribution to the agency's performance.

(2) The maximum rate of basic pay of the SES rate range is set at the rate for level II of the Executive Schedule for senior executives in an agency who are covered by a performance appraisal system that makes meaningful distinctions based on relative performance, as certified by the Office of Personnel Management (OPM), with concurrence by the Office of Management and Budget (OMB), under 5 U.S.C. 5307(d) and 5 CFR part 430, subpart D. A senior executive's rate of basic pay may not exceed the maximum rate of the applicable SES rate range, except as provided in § 534.404(h)(2).

(3) Rates of basic pay higher than the rate for level III of the Executive Schedule but less than or equal to the rate for level II of the Executive Schedule generally are reserved for those senior executives who have demonstrated the highest levels of individual performance and/or made the greatest contributions to the agency's performance, as determined by the agency through the administration of its performance appraisal system for senior executives, or, in the case of newly-appointed senior executives, those who possess superior leadership or other competencies, consistent with the agency's strategic human capital plan.

(b) *Suspension of certification of performance appraisal system.* A senior executive whose rate of basic pay is higher than the rate for level III of the Executive Schedule may not suffer a reduction in pay because his or her agency's applicable performance appraisal system certification is suspended under 5 CFR 430.405(h). The senior executive will continue to receive

his or her current SES rate and is not eligible for a pay adjustment until the senior executive is assigned to a position that would allow the employee to receive a pay adjustment or until certification of the employing agency's applicable performance appraisal system is reinstated under 5 CFR part 430, subpart D. The SES rate of pay is not considered a retained rate of pay for the purpose of applying 5 U.S.C. 3594 and 5 CFR part 359, subpart G, or 5 U.S.C. 5363 and 5 CFR 536.104.

10. Section 534.404 is revised to read as follows:

§ 534.404 Setting and adjusting pay for senior executives.

(a) *Setting pay upon initial appointment to the SES.* An authorized agency official may set the rate of basic pay of an individual at any rate within the SES rate range upon initial appointment to the SES, subject to the limitation on the maximum rate of basic pay in § 534.403(a)(2). Rates of basic pay above the rate for level III of the Executive Schedule but less than or equal to the rate for level II of the Executive Schedule generally are reserved for those newly appointed senior executives who possess superior leadership or other competencies, as determined by the agency as part of its strategic human capital plan. In setting a new senior executive's rate of basic pay, an agency must consider the nature and quality of the individual's experience, qualifications, and accomplishments as they relate to the requirements of the SES position, as well as the individual's current responsibilities.

(b) *Adjusting the pay of SES members.* (1) An authorized agency official may adjust (increase or reduce) the rate of basic pay of a senior executive consistent with the agency's plan for setting and adjusting SES rates of basic pay under paragraph (g) of this section.

(2) An agency may provide an increase in pay only upon a determination by the authorized agency official that the senior executive's individual performance and/or

contributions to agency performance so warrant. In assessing a senior executive's performance and/or contribution to the agency's performance, the authorized agency official may consider such things as unique skills, qualifications, or competencies that the individual possesses, and their significance to the agency's performance, as well as the senior executive's current responsibilities. Senior executives who demonstrate the highest levels of individual performance and/or make the greatest contributions to the agency's performance, as determined by the agency through the administration of its performance appraisal system, or, in the case of newly-appointed senior executives, those who possess superior leadership or other competencies, as determined by the agency as part of its strategic human capital plan, must receive the highest rates of basic pay and pay adjustments.

(3) A senior executive who receives an annual summary rating of outstanding performance must be considered for an annual pay increase, subject to the limitation on the maximum rate of basic pay in § 534.403(a)(2).

(4) A senior executive who receives a summary rating of less than fully successful may not receive an increase in pay for the current appraisal period.

(5) An authorized agency official may reduce the rate of basic pay of a senior executive for performance and/or disciplinary reasons, consistent with the restrictions on reducing the rate of basic pay of a career senior executive in paragraph (j) of this section and in § 534.406(b).

(c) 12-month rule. (1) An authorized agency official may adjust (i.e., increase or reduce) the rate of basic pay of a senior executive not more than once during any 12-month period, except as provided in paragraph (c)(4) of this section.

(2) The following pay actions are considered pay adjustments for the purpose of applying this paragraph:

(i) The setting of an individual's rate of basic pay upon initial appointment or reappointment to the SES under paragraphs (a) and (i)(1) of this section and upon reinstatement to the SES under paragraph (i)(2)(ii) of this section; and

(ii) Any adjustment (increase or reduction) in an SES rate of basic pay granted to a senior executive prior to certification of the applicable agency performance appraisal system as provided in paragraph (d) of this section or after certification of the applicable agency performance appraisal system as provided in paragraph (e) of this section.

(3) The following pay actions are not considered pay adjustments for the purpose of applying this paragraph:

(i) The conversion of senior executives to the new SES pay system under § 534.406 and the conversion of other employees to equivalent senior executive positions;

(ii) A determination by an authorized agency official to make a zero adjustment in pay after reviewing a senior executive's annual summary rating; and

(iii) A zero adjustment in pay made during the 12-month period preceding the first day of the first applicable pay period beginning on or after January 1, 2004, caused by the former limitation on basic pay plus locality-based comparability payments under 5 U.S.C. 5304(g)(2) for a senior executive who was granted an increase in his or her rate of basic pay that did not result in an actual increase in pay.

(4) An authorized agency official may approve increases in a senior executive's rate of basic pay more than once during a 12-month period if the agency head or designee who performs the functions described in 5 CFR 430.404(a)(5) or (6) determines that—

(i) The senior executive's exceptionally meritorious accomplishment significantly contributes to the agency's performance;

(ii) The senior executive is reassigned to a position with substantially greater scope and responsibility;

(iii) The retention of the senior executive is critical to the mission of the agency and the senior executive would be likely to leave the agency in the absence of a pay increase; or

(iv) Such action conforms to an otherwise applicable executive appraisal and pay adjustment cycle (e.g., in the case of a senior executive who was appointed to an SES position within the past 12 months or a senior executive who was transferred to an SES position from an agency with a different senior executive appraisal and pay adjustment cycle within the past 12 months).

(5) Any pay adjustment made as a result of a determination under paragraph (b)(4) of this section is considered a pay adjustment for the purpose of applying § 534.404(c) and begins a new 12-month period.

(d) *Adjustments in pay prior to certification of applicable performance appraisal system.*

An authorized agency official may increase a senior executive's rate of basic pay converted under § 534.406 on the first day of the first applicable pay period beginning on or after January 1, 2004, or on any date thereafter prior to obtaining certification under 5 CFR part 430, subpart D, but only up to the rate for level III of the Executive Schedule. The authorized agency

official may provide such an increase if warranted under the conditions prescribed in paragraph (b)(2) of this section and the senior executive is otherwise eligible for such a pay increase (i.e., he or she did not receive a pay adjustment under § 534.404(c) during the previous 12-month period). An adjustment in pay made under this paragraph is considered a pay adjustment for the purpose of applying § 534.404(c).

(e) *Adjustments in pay after certification of applicable performance appraisal system.* In the case of an agency that obtains certification of a performance appraisal system for senior executives under 5 CFR part 430, subpart D, an authorized agency official may increase a covered senior executive's rate of basic pay up to the rate for level II of the Executive Schedule, consistent with the limitation on increasing pay above the rate for level III of the Executive Schedule in § 534.403(a)(2). The authorized agency official may provide an increase in pay if warranted under the conditions prescribed in paragraph (b)(2) of this section if the senior executive is otherwise eligible for such a pay increase (i.e., he or she did not receive a pay adjustment under § 534.404(c) during the previous 12-month period). The agency head or designee who performs the functions described in 5 CFR 430.404(a)(5) and (6) may make exceptions to the 12-month rule in paragraph (c) of this section under certain limited conditions prescribed in paragraph (c)(4) of this section. An increase in pay made under this paragraph is considered a pay adjustment for the purpose of applying § 534.404(c).

(f) *Effect of Additional increases in Executive Schedule rates of pay.* If there is an additional increase in the rates for the Executive Schedule in a calendar year, and if that increase becomes effective on the first day of the first pay period beginning on or after January 1 (i.e., the date prescribed in 5 U.S.C. 5318), an agency may review any previous determination to adjust the pay of a senior executive that was made effective on or after the effective date of the first

increase in the rates for the Executive Schedule to determine whether, and to what extent, an additional pay increase may be warranted for senior executives based on the same criteria used for the previous determination. If the agency determines that an additional pay increase is warranted, that increase must be made effective as of the effective date of the previous pay increase and is not considered a pay adjustment for the purpose of applying § 534.404(c).

(g) *Agency plan for setting and adjusting SES rate of basic pay.* Each agency must establish a plan for setting and adjusting the rates of basic pay for SES members. The agency's plan must require that any decisions to adjust pay must reflect meaningful distinctions among senior executives based on individual performance and/or contribution to agency performance and must include—

(1) The criteria that will be used to set and adjust a senior executive's rate of basic pay;

(2) The criteria that will be used to set and adjust a senior executive's rate of basic pay at a rate that exceeds the rate for level III of the Executive Schedule if the applicable agency performance appraisal system has been certified under 5 CFR part 430, subpart D;

(3) The designation of the authorized agency official who has authority to set and adjust SES rates of pay for individual senior executives, subject to the requirement that the agency head or designee who performs the functions described in 5 CFR 430.404(a)(5) and (6) must approve any determination to set a senior executive's rate of basic pay higher than the rate for level III of the Executive Schedule and must approve any determination to increase a senior executive's rate of basic pay more than once in any 12-month period; and

(4) The administrative and management controls that will be applied to ensure compliance with applicable statutes, OPM's regulations, the agency's plan, and, where

applicable, the certification requirements set forth in 5 CFR 430, subpart D, and the limitation on the maximum rate of basic pay in § 534.403(a)(2).

(h) Setting pay upon transfer. (1) An authorized agency official may set the pay of a senior executive transferring from another agency at any rate within the SES rate range, subject to the limitation on the maximum rate of basic pay in § 534.403(a)(2) and the restrictions on reducing the pay of career senior executives in paragraph (h)(2) of this section (upon transfer to an agency whose applicable performance appraisal system is not certified) and in § 534.406(b) (for 12 months following the effective date of the new SES pay system). If pay is set at the same SES rate the senior executive received in his or her former agency, the action is not considered a pay adjustment for the purpose of applying § 534.404(c).

(2) A senior executive whose rate of basic pay is higher than the rate for level III of the Executive Schedule may not suffer a reduction in pay as a result of transferring from an agency with a maximum SES rate of basic pay equal to the rate for level II of the Executive Schedule to an agency with a maximum SES rate of basic pay equal to the rate for level III of the Executive Schedule. The senior executive will continue to receive his or her current SES rate and is not eligible for a pay adjustment until the senior executive is assigned to a position that would allow the employee to receive a pay adjustment or the employing agency's applicable performance appraisal system is certified under 5 CFR part 430, subpart D. The SES rate of pay is not considered a retained rate of pay for the purpose of applying 5 U.S.C. 3594 and 5 CFR part 359, subpart G, or 5 U.S.C. 5363 and 5 CFR 536.104.

(i) Setting pay following a break in SES service. (1) General. Upon reappointment to the SES, an authorized agency official may set the rate of basic pay of a former senior executive at

any rate within the SES rate range, subject to the limitations in § 534.403(a), if there has been a break in SES service of more than 30 days. If there has been a break in SES service of 30 days or less, the senior executive's rate of basic pay must be set at a rate at least equal to the employee's former SES rate of basic pay. Setting a rate of basic pay upon reappointment to the SES is considered a pay adjustment under § 534.404(c).

(2) Reinstatement from a Presidential appointment requiring Senate confirmation. The following provisions apply to a former career senior executive who is reinstated under 5 CFR 317.703:

(i) If the individual elected to remain subject to the SES pay provisions while serving under a Presidential appointment, his or her SES rate may be adjusted upon reinstatement to the SES, whether in the agency where the individual held the Presidential appointment or in another agency, if at least 12 months have elapsed since the employee's last SES pay adjustment, unless a determination is made under § 534.404(c)(4) that an additional pay increase is warranted. Any pay adjustment must be made in accordance with paragraphs (b), (d), and (e) of this section and the agency's plan for adjusting SES rates of pay in paragraph (g) of this section.

(ii) If the individual did not elect to remain subject to the SES pay provisions while serving under a Presidential appointment, his or her SES rate may be set upon reinstatement to the SES at any rate within the SES rate range, subject to the limitations in § 534.403(a).

(iii) Setting a rate of basic pay upon reinstatement to the SES under paragraphs (i)(2)(i) and (ii) of this section is considered a pay adjustment for the purpose of applying § 534.404(c).

(j) Restrictions on reducing the pay of career senior executives.

(1) An authorized agency official may reduce a career senior executive's SES rate of basic pay by not more than 10 percent for performance or disciplinary reasons, subject to the restriction on reducing the pay of career senior executives in § 534.406(b) or setting pay below the minimum rate of the SES rate range in § 534.403(a).

(2) The SES rate of basic pay of a career senior executive may be reduced without the employee's consent by the senior executive's agency or upon transfer of function to another agency only—

(i) If the senior executive has received a less than fully successful annual summary rating under 5 CFR part 430, subpart C, or has otherwise failed to meet the performance requirements for a critical element as defined in 5 CFR 430.303; or

(ii) As a disciplinary or adverse action resulting from conduct-related activity, including, but not limited to, misconduct, neglect of duty, or malfeasance.

(3) Prior to reducing a career senior executive's rate of basic pay, the agency must provide the senior executive with the following:

(i) Written notice of such reduction at least 15 days in advance of its effective date;

(ii) A reasonable period of time, but not less than 7 days, for the senior executive to respond to such notice orally and/or in writing and to furnish affidavits and other documentary evidence in support of that response;

(iii) An opportunity to be represented in the matter by an attorney or other representative;

(iv) A written decision and specific reasons for the pay reduction at the earliest practicable date after the senior executive's response, if any; and

(v) An opportunity to request, within 7 days after the date of that decision, reconsideration by the head of the agency, whose determination with respect to that request will be final and not subject to further review.

11. In newly redesignated § 534.405, revise paragraphs (a)(2)(i), (b), (c), and (f) to read as follows:

§ 534.405 Performance Awards.

(a) * * *

(2) * * *

(i) A former SES career appointee who elected to retain award eligibility under 5 CFR part 317, subpart H. If the rate of basic pay of the individual is higher than the maximum rate of basic pay for the applicable SES rate range, the maximum rate of that SES rate range is used for crediting the agency award pool under paragraph (b) of this section and the amount the individual may receive under paragraph (c) of this section.

* * * * *

(b)(1) The total amount of performance awards paid during a fiscal year by an agency may not exceed the greater of—

(i) Ten percent of the aggregate career SES rates of basic pay for the agency as of the end of the fiscal year prior to the fiscal year in which the award payments are made; or

(ii) Twenty percent of the average annual rates of basic pay for career SES appointees of the agency as of the end of the fiscal year prior to the fiscal year in which the award payments are made.

(2) In determining the aggregate career SES rates of basic pay and the average annual rate of basic pay as of the end of FY 2003 for the purpose of applying paragraph (b) of this section, agencies must use the annual rate of basic pay, plus any applicable locality-based comparability payment under 5 U.S.C. 5304 or special geographic pay adjustment established for law enforcement officers under section 404(a) of the Federal Employees Pay Comparability Act of 1990 (Public Law 101-509), which the SES appointees were receiving at the end of FY 2003.

(c) The amount of a performance award paid to an individual career appointee may not be less than 5 percent nor more than 20 percent of the appointee's SES rate of basic pay as of the end of the performance appraisal period.

* * * * *

(f) Performance awards must be paid in a lump sum except in those instances when it is not possible to pay the full amount because of the applicable aggregate limitation on pay during a calendar year under 5 CFR part 530, subpart B. In that case, any amount in excess of the applicable aggregate limitation must be paid at the beginning of the following calendar year in accordance with 5 CFR part 530, subpart B. The full performance award, however, is charged against the agency bonus pool under § 534.405(b) for the fiscal year in which the initial payment was made.

12. A new § 534.406 is revised read as follows:

§ 534.406 Conversion to the SES pay system.

(a) On the first day of the first applicable pay period beginning on or after January 1, 2004, agencies must convert an existing SES rate of basic pay for a senior executive to an SES rate of basic pay that is equal to the employee's rate of basic pay, plus any applicable locality-based comparability payment under 5 U.S.C. 5304 which the senior executive was receiving immediately before that date, except as provided in paragraph (b) of this section. The newly converted rate is the senior executive's SES rate of basic pay. An agency's establishment of an SES rate of basic pay for a senior executive under this paragraph is not considered a pay adjustment for the purpose of applying § 534.404(c).

(b) An SES member's rate of basic pay, plus any applicable locality-based comparability payment under 5 U.S.C. 5304 to which the employee was entitled on November 24, 2003, may not be reduced for 1 year after the first day of the first applicable pay period beginning on or after January 1, 2004. If an SES member's rate of basic pay, plus any applicable locality-based comparability payment under 5 U.S.C. 5304 to which the employee was entitled on November 23, 2003, is higher than the rate in effect immediately prior to the first day of the first applicable pay period beginning on or after January 1, 2004, the agency must use the higher rate for the purpose of converting SES members to the SES pay system.

(c) Certain SES members in positions that have geographic mobility requirements and who are assigned outside the 48 contiguous States and the District of Columbia to a position overseas or in Alaska, Hawaii, Guam or the Commonwealth of the Northern Mariana Islands, Puerto Rico, the U.S. Virgin Islands, or other U.S. territories and possessions as of the first day of the first applicable pay period beginning on or after January 1, 2004, will be converted to a

new rate of basic pay that equals their current rate of basic pay, plus the amount of locality pay authorized under 5 U.S.C. 5304 for the applicable locality pay area upon reassignment to a position in the 48 contiguous States or the District of Columbia. The adjustment will be prospective, not retroactive, and it will not be considered a pay adjustment for the purpose of applying § 534.404(c). If the senior executive's rate of basic pay did not exceed the rate for level III of the Executive Schedule while assigned to a position outside the 48 contiguous States or the District of Columbia, upon reassignment to a locality pay area the senior executive's converted rate of basic pay may not exceed the rate for level III of the Executive Schedule consistent with the limitations in § 534.403(a)(2) on increasing a senior executive's rate of basic pay up to the rate for level II of the Executive Schedule. The newly converted rate is the senior executive's SES rate of basic pay.

(d) On the first day of the first applicable pay period beginning on or after January 1, 2004, a law enforcement officer (LEO), as defined in 5 CFR 531.301, who is a member of the SES will have his or her rate of basic pay, plus any applicable special geographic pay adjustment established for LEOs under section 404(a) of the Federal Employees Pay Comparability Act of 1990 (Public Law 101-509) to which he or she was entitled immediately before that date, converted to a new SES rate of basic pay. The newly converted rate is the senior executive's SES rate of basic pay, and any pay adjustments approved on or after January 11, 2004, must be computed based on the senior executive's converted rate of basic pay. Conversion to a new SES rate of basic pay is not considered a pay adjustment for the purpose of applying § 534.404(c).

13. Section 534.407 is added to subpart D to read as follows:

§ 534.407 Pay computation and aggregate compensation.

(a) Except as provided in paragraph (b) of this section, pay for members of the SES must be computed in accordance with 5 U.S.C. 5504(b).

(b) To determine the hourly rate of pay for members of the SES, divide the annual SES rate of basic pay by 2,087 and round to the nearest cent, counting one-half cent and over as a whole cent. To derive the biweekly rate, multiply the hourly rate by 80.

(c) Senior executives are subject to the applicable aggregate limitation on pay in 5 CFR part 530, subpart B.

14. In newly redesignated § 534.408, remove the word “subject” and add in its place the word “subpart” in the last sentence of paragraph (b).

PART 575--RECRUITMENT AND RELOCATION BONUSES; RETENTION ALLOWANCES; SUPERVISORY DIFFERENTIALS

15. The authority citation for part 575 continues to read as follows:

Authority: 5 U.S.C. 1104(a)(2), 5753, 5754, and 5755; secs. 302 and 404 of the Federal Employees Pay Comparability Act of 1990 (FEPCA) (Pub. L. 101-509), 104 Stat. 1462 and 1466, respectively; E.O. 12748, 3 CFR, 1992 Comp. p. 316.

Subpart C--Retention Allowances

16. In § 575.306, paragraph (b) is revised to read as follows:

§ 575.306 Payment of retention allowance.

* * * * *

(b) The head of an agency may not authorize a retention allowance for an employee if or to the extent that such an allowance, when added to the employee's estimated aggregate compensation, as defined in 5 CFR 530.202, would cause the aggregate compensation actually received by the employee during the calendar year to exceed the applicable aggregate limitation on pay under 5 CFR part 530, subpart B, at the end of the calendar year.

* * * * *

17. In § 575.307, paragraph (a) is revised to read as follows:

§ 575.307 Reduction or termination of retention allowance.

(a) The agency must reduce or terminate the authorized amount of a retention allowance to the extent necessary to ensure that the employee's estimated aggregate compensation, as defined in 5 CFR 530.202, does not exceed the applicable aggregate limitation on pay under 5 CFR part 530, subpart B, at the end of the calendar year.

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