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HUMAN CAPITAL

Preliminary Observations
on Proposed DHS Human
Capital Regulations

Statement of David M. Walker
Comptroller General of the United States



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Highlights

Highlights of [GAO-04-479T](#), testimony before subcommittees of the Senate Committee on Governmental Affairs and the House Committee on Government Reform

Why GAO Did This Study

The creation of the Department of Homeland Security (DHS) almost one year ago represents an historic moment for the federal government to fundamentally transform how the nation will protect itself from terrorism. DHS is continuing to transform and integrate a disparate group of agencies with multiple missions, values, and cultures into a strong and effective cabinet department. Together with this unique opportunity, however, also comes significant risk to the nation that could occur if this transformation is not implemented successfully. In fact, GAO designated this implementation and transformation as high risk in January 2003.

Congress provided DHS with significant flexibility to design a modern human capital management system. GAO reported in September 2003 that the design effort to develop the system was collaborative and consistent with positive elements of transformation. Last Friday, the Secretary of DHS and the Director of the Office of Personnel Management (OPM) released for public comment draft regulations for DHS's new human capital system. This testimony provides preliminary observations on selected major provisions of the proposed system. The subcommittees are also releasing *Human Capital: Implementing Pay for Performance at Selected Personnel Demonstration Projects* (GAO-04-83) at today's hearing.

www.gao.gov/cgi-bin/getrpt?GAO-04-479T.

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

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Preliminary Observations on Proposed DHS Human Capital Regulations

What GAO Found

The proposed human capital system is designed to be aligned with the department's mission requirements and is intended to protect the civil service rights of DHS employees. Many of the basic principles underlying the DHS regulations are consistent with proven approaches to strategic human capital management, including several approaches pioneered by GAO, and deserve serious consideration. However, some parts of the system raise questions that DHS, OPM, and Congress should consider.

- **Pay and performance management:** The proposal takes another valuable step towards results-oriented pay reform and modern performance management. For effective performance management, DHS should use validated core competencies as a key part of evaluating individual contributions to departmental results and transformation efforts.
- **Adverse actions and appeals:** The proposal would retain an avenue for employees to appeal adverse actions to an independent third party. However, the process to identify mandatory removal offenses must be collaborative and transparent. DHS needs to be cautious about defining specific actions requiring employee removal and learn from the Internal Revenue Service's implementation of its mandatory removal provisions.
- **Labor relations:** The regulations recognize employees' right to organize and bargain collectively, but reduce areas subject to bargaining. Continuing to involve employees in a meaningful manner is critical to effective human capital management.

Once DHS issues final regulations for the human capital system, the department will be faced with multiple implementation challenges:

- DHS plans to implement the system using a phased approach, however, nearly half of DHS civilian employees are not covered by these regulations, including more than 50,000 Transportation Security Administration screeners. To help build a unified culture, DHS should consider moving all of its employees under a single performance management system framework.
- DHS noted that it estimates that \$110 million will be needed to implement the new system in its first year. While adequate resources for program implementation is critical to program success, DHS is requesting a substantial amount of funding that warrants close scrutiny by Congress.
- The proposed regulations call for comprehensive, ongoing evaluations. Continued evaluation and adjustments will help to ensure an effective and credible human capital system.
- DHS has begun to develop a strategic workforce plan. Such a plan can be used as a tool for identifying core competencies for staff for attracting, developing, evaluating, and rewarding contributions to mission accomplishment.

The analysis of DHS's effort to develop a strategic human capital management system can be instructive as other agencies request and implement new strategic human capital management authorities.

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

It is a pleasure to appear before you today to provide our preliminary observations on the Department of Homeland Security's (DHS) proposed regulations on its new human capital system.¹ The creation of DHS almost 1 year ago represents an historic moment for the federal government to fundamentally transform how the nation will protect itself from terrorism. DHS is continuing to transform and integrate a disparate group of agencies with multiple missions, values, and cultures into a strong and effective cabinet department. However, this unique opportunity also brings significant risk to the nation if this transformation is not implemented successfully. In fact, we designated this implementation and transformation as high risk in January 2003.²

Last Friday, the Secretary of DHS and the Director of the Office of Personnel Management (OPM) released for public comment proposed regulations for DHS's new human capital system. The regulations are intended to provide the broad outline of the DHS proposed system and are not, nor were they intended to be, a comprehensive presentation of the details of how the new system will be implemented. As the system evolves, critical issues such as how DHS will link individual performance expectations to DHS's mission and goals, how it will define performance expectations to promote individual accountability, and how it will continue to incorporate adequate safeguards to ensure fairness, will need to be addressed. Such detailed implementation policies and procedures will need to be developed in a transparent and inclusive manner as the system evolves. Although we are still reviewing these extensive regulations issued last week, this morning I will provide some preliminary observations on selected provisions that in our view are most in need of close scrutiny as Congress considers the DHS proposal.

The proposed DHS regulations have both significant precedent-setting implications for the executive branch and far-reaching implications on how the department is managed. In my view, many of the basic principles underlying the proposed DHS regulations are consistent with proven approaches to strategic human capital management, including several approaches pioneered by GAO, and deserve serious consideration. In designing the proposed system, DHS and OPM met with a wide range of individuals and organizations with expertise in human capital. At the request of DHS and OPM, we were pleased to share the results of our work looking at leading human capital practices as well as our own experiences with performance management at GAO. My statement today is based on our ongoing review of DHS's design and implementation of its human capital system, recent work on strategic human capital management, including performance management, and our own experience.

¹Senate Committee on Governmental Affairs, Subcommittee on Oversight of Government Management, the Federal Workforce, and the District of Columbia and House Committee on Government Reform, Subcommittee on Civil Service and Agency Organization.

²U.S. General Accounting Office, *Major Management Challenges and Program Risks: Department of Homeland Security*, GAO-03-102 (Washington, D.C.: January 2003).

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Preliminary Observations on the Proposed Human Capital Regulations

DHS's and OPM's proposed regulations would establish a new human resources management system within DHS that covers pay, classification, performance management, labor relations, adverse action, and employee appeals. These changes are designed to ensure that the system aligns individual performance and pay with the department's critical mission requirements and to protect the civil service rights of its employees. However, it is important to note at the outset that the proposed regulations do not apply to nearly half of all DHS civilian employees, including nearly 50,000 screeners in the Transportation Security Administration (TSA). DHS officials have noted that additional employees can be included through further administrative action, but that legislation would be needed to include other employees such as the screeners and the uniformed division of the Secret Service.³ We have found that having one performance management system framework facilitates unifying an organizational culture and is a key practice to a successful merger and transformation. Based on the department's progress in implementing the system and any appropriate modifications made based on their experience, DHS should consider moving all of its employees under the new human capital system.

Pay and Performance Management

Today, Mr. Chairman and Madam Chairwoman, you are releasing a report that we prepared at your request that shows the variety of approaches that OPM's personnel demonstration projects took to design and implement their pay for performance systems.⁴ Their experiences provide insights into how some organizations in the federal government are implementing pay for performance and thus can guide DHS as it develops and implements its own approach. These demonstration projects illustrate that understanding how to link pay to performance is very much a work in progress in the federal government and that additional work is needed to ensure that performance management systems are tools to help them manage on a day-to-day basis and achieve external results.

As we testified last spring when the Department of Defense (DOD) proposed its civilian personnel reform, from a conceptual standpoint, we strongly support the need to expand pay for performance in the federal government.⁵ Establishing a better link between individual pay and performance is essential if we expect to maximize the performance and ensure the accountability of the federal government for the benefit of the American

³The Homeland Security Act of 2002 gave DHS authority to waive or modify parts of civil service law in Title 5 of the U.S. Code. However, not all employees of DHS are covered under Title 5. According to DHS officials, this impacts coverage of TSA, part of the Coast Guard, the Uniformed Division of the Secret Service, and part of the Emergency Preparedness and Response Directorate. These same DHS officials indicated that DHS can administratively extend the new human capital system to many of these employees. However, they said that legislation would be required to move TSA screeners and Secret Service uniformed employees completely into the new system.

⁴U.S. General Accounting Office, *Human Capital: Implementing Pay for Performance at Selected Personnel Demonstration Projects*, GAO-04-83 (Washington, D.C.: Jan. 23, 2004).

⁵U.S. General Accounting Office, *Defense Transformation: Preliminary Observations on DOD's Proposed Civilian Personnel Reforms*, GAO-03-717T (Washington, D.C.: April 29, 2003).

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people. However, how it is done, when it is done, and the basis on which it is done can make all the difference in whether such efforts are successful. The DHS proposal reflects a growing understanding that the federal government needs to fundamentally rethink its current approach to pay and better link pay to individual and organization performance. To this end, the DHS proposal takes another valuable step towards results-oriented pay reform and modern performance management. My comments on specific provisions follow.

Linking Organizational Goals to Individual Performance

Under the proposed regulations, the DHS performance management system must, among other things, align individual performance expectations with the mission, strategic goals, or a range of other objectives of the department or of the DHS components. The proposed guidelines do not detail how such an alignment is to be achieved, a vital issue that will need to be addressed as DHS's efforts move forward. Our work looking at public sector performance management efforts here in the United States as well as abroad have underscored the importance of aligning daily operations and activities with organizational results. We have found that organizations often struggle with clearly understanding how what they do on a day-to-day basis contributes to overall organizational results. High performing organizations, on the other hand, understand how the products and services they deliver contribute to results by aligning performance expectations of top leadership with organizational goals and then cascading those expectations to lower levels.

As an organization undergoing its own merger and transformation, DHS's revised performance management system can be a vital tool for aligning the organization with desired results and creating a "line of sight" showing how team, unit, and individual performance can contribute to overall organizational results. To help DHS merge its various originating components into a unified department and transform its culture to be more results oriented, customer focused, and collaborative in nature, we reported at your request, Mr. Chairman and Madam Chairwoman, how a performance management system that defines responsibility and assures accountability for change can be key to a successful merger and transformation.⁶ While aligning individual performance expectations with DHS's mission and strategic goals will be key to DHS's effective performance management, it is important to note that DHS has not yet released its strategic plan which may hamper creating the formal linkage to the performance management system and make it difficult to ensure that the proposed regulations support and facilitate the accomplishment of the department's strategic goals and objectives.

Establishing Pay Bands

Under the proposed regulations, DHS would create broad pay bands for much of the department in place of the fifteen-grade General Schedule (GS) system now in place for

⁶U.S. General Accounting Office, *Results-Oriented Cultures: Implementation Steps to Assist Mergers and Organizational Transformations*, GAO-03-669 (Washington, D.C.: July 2, 2003).

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much of the civil service. Specifically, DHS officials have indicated that they will form ten to fifteen occupational pay clusters of similar job types, such as a management or science and technology cluster. Most of these occupational clusters would have four pay bands ranging from entry level to supervisor. Within each occupational cluster, promotion to another band (such as from full performance to senior expert) would require an assessment and/or competition. Under the proposed regulations, DHS is not to reduce employees' basic rate of pay when converting to pay bands. In addition, the proposed regulations would allow DHS to establish a "control point" within a band, beyond which basic pay increases may be granted only for meeting criteria established by DHS, such as an outstanding performance rating.

The use of control points can be a valuable tool because managing progression through the bands can help to ensure that employees' performance coincides with their salaries and can help to prevent all employees from eventually migrating to the top of the band and thus increasing salary costs. Both China Lake and the Naval Sea Systems Command Warfare Center's (NAVSEA) Dahlgren Division have checkpoints or "speed bumps" in their pay bands designed to ensure that only the highest performers move into the upper half of the pay band. For example, when employees' salaries at China Lake reach the midpoint of the pay band, they must receive a performance rating equivalent to exceeding expectations, before they can receive additional salary increases.

Pay banding and movement to broader occupational clusters can both facilitate DHS's movement to a pay for performance system, and help DHS to better define occupations, which can improve the hiring process. We have reported that the current GS system as defined in the Classification Act of 1949 is a key barrier to comprehensive human capital reform and the creation of broader occupational job clusters and pay bands would aid other agencies as they seek to modernize their personnel systems.⁷ The standards and process of the current classification system is a key problem in federal hiring efforts because they are outdated and not applicable to the occupations and work of today. Many employees in agencies that are now a part of DHS responding to OPM's 2002 Federal Human Capital Survey (FHCS) believe that recruiting is a problem – only 36 percent believe their work unit is able to recruit people with the right skills.⁸

Setting Employee Performance Expectations

The DHS performance management system is intended to promote individual accountability by communicating performance expectations and holding employees responsible for accomplishing them and by holding supervisors and managers responsible for effectively managing the performance of employees under their supervision. While supervisors are to involve employees as far as practicable in

⁷U.S. General Accounting Office, *Human Capital: Opportunities to Improve Executive Agencies' Hiring Processes*, GAO-03-450 (Washington, D.C.: May 30, 2003).

⁸The DHS responses reported by the OPM FHCS approximate the views of some, but not all, employees now at DHS. For example, the Transportation Security Administration (TSA) screeners were not hired at the time of the survey. Also, though the Animal and Plant Health Inspection Services (APHIS) employees were divided between DHS and the U.S. Department of Agriculture (USDA), the APHIS respondents included those remaining at USDA. Details on the objective, scope, and methodology for the OPM FHCS are described in more detail in Appendix 1.

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developing their performance expectations and employees seek clarification if they do not understand them, the final decision on an employee's expectations is the supervisor's sole and exclusive discretion. Supervisors must monitor the performance of their employees and provide periodic feedback, including one or more formal interim performance reviews during the appraisal period.

The proposed regulations provide a general description of DHS's performance management system with many important details to be determined. Under the proposed regulations, performance expectations may take the form of goals or objectives that set general or specific performance targets at the individual, team, and/or organizational level; a particular work assignment, including characteristics such as quality, accuracy, or timeliness; or competencies an employee is expected to demonstrate on the job; and/or the contributions an employee is expected to make, among other things. As DHS's system design efforts move forward, it will need to define in further detail than currently provided how performance expectations will be established, including the degree to which DHS components, managers, and supervisors will have flexibility in setting those expectations.

Nevertheless, the range of expectations that DHS will consider in setting individual employee performance expectations are generally consistent with those we see used by leading organizations. In addition, DHS appropriately recognizes that given the vast diversity of work done in the Department, managers and employees need flexibility in crafting specific expectations. However, the experiences of leading organizations suggest that DHS should reconsider its position to merely allow, rather than require the use of core employee competencies as a central feature of DHS'S performance management efforts.⁹ Based on our review of others' efforts and our own experience at GAO, core competencies can help reinforce employee behaviors and actions that support the department's mission, goals, and values and can provide a consistent message to employees about how they are expected to achieve results. For example, the Civilian Acquisition Workforce Personnel Demonstration Project (AcqDemo), which covers various organizational units of the Air Force, Army, Navy, Marine Corps, and the Office of the Under Secretary of Defense, applies organizationwide competencies for all employees such as teamwork/cooperation, customer relations, leadership/supervision, and communication.

More specifically and consistent with leading practices for successful mergers and organizational transformation, DHS should use its performance management system to serve as the basis for setting expectations for individual roles in its transformation process.¹⁰ To be successful, transformation efforts, such as the one underway at DHS, must have leaders, managers, and employees who have the individual competencies to integrate and create synergy among multiple organizations involved in the transformation effort. Individual performance and contributions can be evaluated on competencies such as change management, cultural sensitivity, teamwork and

⁹U.S. General Accounting Office, *Creating a Clear Linkage between Individual Performance and Organizational Success*, GAO-03-488 (Washington, D.C.: March 14, 2003).

¹⁰GAO-03-669.

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collaboration, and information sharing. Leaders, managers, and employees who demonstrate these competencies are rewarded for their success in contributing to the achievement of the transformation process. DHS, by including such competencies throughout its revised performance management system, would create a shared responsibility for organizational success and help assure accountability for change.

Translating Employee Performance Ratings into Pay Increases and Awards

A stated purpose of DHS's performance management system is to provide for meaningful distinctions in performance to support adjustments in pay, awards, and promotions. All employees who meet organizational expectations are to receive pay adjustments, generally to be made on an annual basis. In coordination with OPM, the pay adjustment is to be based on considerations of mission requirements, labor market conditions, availability of funds, pay adjustments received by other federal employees, and other factors. The pay adjustment may vary by occupational cluster or band. Employees that meet or exceed expectations are also eligible to receive a performance-based pay increase, either as an increase to base pay or a one-time award, depending on the employee's performance rating. Employees with unacceptable ratings are not to receive the pay adjustment or a performance-based pay increase. The proposed regulations provide managers with a range of options for dealing with poor performance, such as remedial training, reassignment, an improvement period, among other things.

In coordination with OPM, DHS may additionally set the boundaries of locality pay areas. Participants in the DHS focus groups expressed concerns regarding the shortcomings of the current locality pay system, including its impact on recruitment and retention.¹¹

While the DHS proposal does not provide additional detail on how it would consider labor market conditions, its proposed approach is broadly consistent with the experiences of some of the demonstration projects that considered the labor market or the fiscal condition of the organization in determining how much to budget for pay increases. For example, NAVSEA's Newport Division considers the labor market and uses regional and industry salary information compiled by the American Association of Engineering Societies when determining how much to set aside for pay increases and awards. In addition, the Newport Division is financed in part through a working capital fund and thus must take into account fiscal condition when budgeting for pay increases and awards. Responding to higher salaries in the labor market, the Newport Division funded pay increases at a higher rate in fiscal year 2001 than in 2000. Conversely, in fiscal year 2002, the performance pay increase and award pools were funded at lower levels than in 2001 because of fiscal constraints.

Under the proposed regulations, DHS would establish performance pay pools by occupational cluster and by band within each cluster, and may further divide them by unit and/or location. Performance-based pay would be based on "performance points" whereby points correspond to a rating level. In an example used by DHS, for a four-level system, the point value pattern may be 4-2-1-0, where 4 points are assigned to the highest

¹¹Details on the objective, scope, and methodology for the DHS focus groups are described in more detail in Appendix 1.

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rating and 0 points to an unacceptable rating. While each pay pool has the option to use this point value pattern or another, DHS is to determine the value of a performance point. The proposed regulations do not provide more detailed information on how ratings will be used for pay and promotions.

Under the proposed regulations, DHS may not impose a quota on any rating level or a mandatory distribution of ratings. DHS would create a Performance Review Board (PRB) to review ratings in order to promote consistency and provide general oversight of the performance management system to ensure it is administered in a fair, credible, and transparent manner. DHS may, in turn, appoint as many review boards within the departmental components as it deems necessary to effectively carry out these intended functions and, when practicable, may include employees outside the organizational unit, occupation, and/or location of employees subject to review by the PRB. The proposed regulations do not offer additional details on other matters such as the selection process for the members nor their qualifications. Where circumstances warrant, the PRB may remand individual ratings for additional review and/or modify a rating.

While much remains to be determined about how the DHS PRB will operate, we believe that the effective implementation of such a board is important to assuring that predecisional internal safeguards exist to help achieve consistency and equity, and assure nondiscrimination and nonpoliticization of the performance management process. The key will be to create a PRB that is independent of line management and review such matters as the establishment and implementation of the performance appraisal system and later, performance rating decisions, pay determinations, and promotion actions before they are finalized to ensure they are merit based.

Several of the OPM pay for performance demonstration projects consider an employee's current salary when making decisions on permanent pay increases and one-time awards – a procedure that is worth additional consideration in the proposed DHS regulations. By considering salary in such decisions, the projects intend to make a better match between an employee's compensation and his or her contribution to the organization. Thus, two employees with comparable contributions could receive different pay increases and awards depending on their current salaries. For example, at AcqDemo, supervisors recommend and pay pool managers approve employees' "contribution scores." Pay pool managers then plot contribution scores against the employees' current salaries and a "standard pay line" to determine if employees are "appropriately compensated," "under-compensated" or "over-compensated," given their contributions.

As a result of this system, AcqDemo has reported that it has made progress in matching employees' compensation to their contributions to the organization. From 1999 to 2002, appropriately compensated employees increased from about 63 percent to about 72 percent, under-compensated employees decreased from about 30 percent to about 27 percent and over-compensated employees decreased from nearly 7 percent to less than 2 percent. A recent evaluation of AcqDemo by Cubic Applications, Inc. by Cubic Applications, Inc. found that employees' perceptions of the link between pay and contribution increased, from 20 percent reporting that pay raises depend on their contribution to the organization's mission in 1998 to 59 percent in 2003.

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Providing Adequate Safeguards to Ensure Fairness and Guard against Abuse

According to the proposed regulations, the DHS performance management system must comply with the merit system principles and avoid prohibited personnel practices; provide a means for employee involvement in the design and implementation of the system; and overall, be fair, credible, and transparent. Last spring, when commenting on the DOD civilian personnel reforms, we testified that Congress should consider establishing statutory standards that an agency must have in place before it can implement a more performance-based pay program and developed an initial list of possible safeguards to help ensure that pay for performance systems in the government are fair, effective, and credible.¹²

While much remains to be defined, DHS is proposing taking actions that are generally consistent with these proposed safeguards. For example, as I noted previously, DHS plans to align individual performance management with organizational goals and provide for reasonableness reviews of performance management decisions through its PRB. Moreover, employees and their union representatives played a role in shaping the design of the proposed systems, as we previously reported.¹³

DHS should continue to build in safeguards into its revised performance management system. For example, we noted that agencies need to assure reasonable transparency and provide appropriate accountability mechanisms in connection with the results of the performance management process. This can include publishing overall results of performance management and individual pay decisions while protecting individual confidentiality and reporting periodically on internal assessments and employee survey results relating to the performance management system. DHS should commit to publishing the results of the performance management process. Publishing the results in a manner that protects individual confidentiality can provide employees with the information they need to better understand the performance management system. Several of the demonstration projects publish information for employees on internal Web sites about the results of performance appraisal and pay decisions, such as the average performance rating, the average pay increase, and the average award for the organization and for each individual unit.

Adverse Actions And Appeals

The DHS proposal is intended to streamline the employee adverse action process, while maintaining an independent third-party review of most adverse actions. It is designed to create a single process for both performance-based and conduct-based actions,¹⁴ and shortens the adverse action process by removing the requirement for a performance-improvement-plan and reducing other timeframes. The proposed regulations also adopt

¹²GAO-03-717T.

¹³U.S. General Accounting Office, *Human Capital: DHS Personnel System Design Effort Provides for Collaboration and Employee Participation*, GAO-03-1099 (Washington, D.C.: Sept. 30, 2003).

¹⁴Title 5 has a process for performance-based actions in Chapter 43 and a different process in Chapter 75 which can be used for conduct or performance-based actions.

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the lower standard of proof for adverse actions in DHS, requiring the agency to meet a standard of “substantial evidence” instead of a “preponderance of the evidence.” An independent review is to be retained by allowing employees to appeal to the Merit Systems Protection Board (MSPB). The appeals process at MSPB is however, to be streamlined by shortening the time for filing and processing appeals. The proposal also encourages the use of Alternative Dispute Resolution (ADR).

The proposal authorizes the Secretary of DHS to identify specific offenses for which removal is mandatory. Employees alleged to have committed these offenses will have the right to a review by an adjudicating official and a further appeal to an independent DHS panel to be formed. Members of this three-person panel are to be appointed by the Secretary for three-year terms and qualifications for these members are articulated in the proposed regulations. Members of the panel may be removed by the Secretary “only for inefficiency, neglect of duty, or malfeasance.” Qualifications for the adjudicating officials, who are designated by the panel, are not specified.

Retention of a qualified and independent third-party to address employee appeals may be especially important in light of OPM’s FHCS results. Specifically,

- 38 percent of DHS respondents believe that complaints, disputes, or grievances are resolved fairly –lower than the governmentwide response of 44 percent;¹⁵ and
- 38 percent of DHS respondents perceive that arbitrary action, personal favoritism and coercion for partisan political purposes are not tolerated –lower than the governmentwide response of 45 percent.

Providing an avenue for an independent appeal can enhance employee trust of the entire human capital system. A similar theme was echoed during the DHS focus groups, in which employees and managers believed it was important to maintain a neutral third-party reviewer in the appeals process. In a separate survey that we administered (GAO survey), members of the field team identified the presence of a neutral third party in the process as the most critical challenge in terms of the discipline and appeals system, while others identified options retaining a third party reviewer as most likely to address the department’s challenges in discipline and appeals.¹⁶

DHS’s commitment to use ADR is also a very positive development. To resolve disputes in a more efficient, timely, and less adversarial manner, federal agencies have been expanding their human capital programs to include ADR approaches. These approaches include mediation, dispute resolution boards and ombudsmen. Ombudsmen are typically used to provide an informal alternative to addressing conflicts. We reported on common approaches used in ombudsman offices, including 1) broad responsibility and authority to address almost any workplace issue, 2) their ability to bring systemic issues to management’s attention, and 3) the manner in which they work with other agency offices

¹⁵In all instances comparing DHS’s results to the OPM FHCS governmentwide average, DHS results are lower by a statistically significant amount according to OPM data.

¹⁶Field team participants served as a key source of information during the design process. The field team consisted of DHS managers and staff. Details on the objective, scope, and methodology for the GAO-administered survey of the field team are described in more detail in Appendix 1.

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in providing assistance to employees.¹⁷ The proposed regulations note that the department will use ADR, including an ombudsman, where appropriate.

One potential area of caution is the authority given to the Secretary to identify specific offenses for which removal is mandatory. I believe that the process for determining and communicating which types of offenses require mandatory removal should be explicit and transparent and involve a member of key players. Such a process should include an employee notice and comment period before implementation, collaboration with relevant Congressional stakeholders, and collaboration with employee representatives.

We also would suggest that DHS exercise caution when identifying specific removable offenses and the specific punishment. When developing these proposed regulations, DHS should learn from the experience of the Internal Revenue Service's (IRS) implementation of its mandatory removal provisions.¹⁸ We reported that IRS officials believed this provision had a negative impact on employee morale and effectiveness and had a "chilling" effect on IRS frontline enforcement employees who are afraid to take certain appropriate enforcement actions.¹⁹ Careful drafting of each removable offense is critical to ensure that the provision does not have unintended consequences.

Moreover, the independence of the panel that will hear appeals of mandatory removal actions deserves further consideration. Removal of the panel members by the Secretary may potentially compromise the real or perceived independence of the panel's decisions. As an alternative, the department should consider having members of the panel removed only by a majority decision of the panel.

Labor Management Relations

The DHS proposed regulations recognize the right for employees to organize and bargain collectively.²⁰ However, the proposal reduces the scope of bargaining by removing the requirement to bargain on matters traditionally referred to as "impact and implementation," which include the processes used to deploy personnel, assign work, and use new technology, for example, and redefining what are traditionally referred to as the "conditions of employment." A DHS Labor Relations Board is proposed that would be responsible for determining appropriate bargaining units, resolving disagreements on the scope of bargaining and the obligation to bargain, and resolving impasses, and would be separate and independent from the Federal Labor Relations Authority (FLRA). The Labor Relations Board would have three members selected by the Secretary. No member could be a current DHS employee and one member would be from FLRA. The

¹⁷U.S. General Accounting Office, *Human Capital: The Role of Ombudsmen in Dispute Resolution*, GAO-01-466 (Washington, D.C.: April 13, 2001).

¹⁸Section 1203 of the IRS Restructuring and Reform Act of 1998 outlines conditions for firing of IRS employees for any of ten acts of misconduct. 26 USC 7804 note.

¹⁹U.S. General Accounting Office, *Tax Administration: IRS and TIGTA Should Evaluate Their Processing of Employee Misconduct Under Section 1203*, GAO-03-394 (Washington, DC: February 2003).

²⁰Under current law, the rights of employees to bargain may be suspended for reasons of national security. 5 U.S.C. Sect. 7103(b), 7112(b)(6).

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FLRA is retained to resolve complaints concerning certain unfair labor practices and to supervise or conduct union elections.

Regardless of whether it is as a part of collective bargaining, involving employees in such important decisions as how they are deployed and how work is assigned is critical to the successful operations of the department. During the course of the design process, DHS has recognized the importance of employee involvement and has been involving multiple organizational components and its three major employee unions in designing the new human capital system.²¹ This is consistent with our finding that leading organizations involve unions and incorporate their input into proposals before finalizing decisions.²² Engaging employee unions in major changes, such as redesigning work processes, changing work rules, or developing new job descriptions, can help achieve consensus on the planned changes, avoid misunderstandings, speed implementation, and more expeditiously resolve problems that occur. These organizations engaged employee unions by developing and maintaining an ongoing working relationship with the unions, documenting formal agreements, building trust over time, and participating jointly in making decisions.

DHS employees' comments can prove instructive when determining the balance in labor management relations. In the DHS focus groups, employees suggested having informal mechanisms in place to resolve issues before the need to escalate them to the formal process and holding supervisors accountable for upholding agreements. Supervisors and employees also expressed a need for increased training in roles and responsibilities in the labor process and an interest in training in ADR. Respondents to the GAO survey said the most critical challenge in terms of labor relations will be to maintain a balance between the mission of the agency and bargaining rights.

DHS Faces Multiple Implementation Challenges

Once DHS issues final regulations for the human capital system, the department will be faced with multiple implementation challenges. While we plan to provide further details to the Congress on some of these challenges in the near future, they include the following.

Implementing the system using a phased approach. The DHS proposed regulations note that the labor relations, adverse actions, and appeals provisions will be effective 30 days after issuance of the interim final regulations later this year. DHS plans to implement the job evaluation, pay, and performance management system in phases to allow time for final design, training, and careful implementation. We strongly support a phased approach to implementing major management reforms. A phased implementation approach recognizes that different organizations will have different levels of readiness and different capabilities to implement new authorities. Moreover, a phased approach

²¹GAO-03-1099.

²²U.S. General Accounting Office. *Human Capital: Practices that Empowered and Involved Employees*, GAO-01-1070 (Washington, D.C.: Sept. 14, 2001).

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allows for learning so that appropriate adjustments and midcourse corrections can be made before the regulations are fully implemented organizationwide.

Providing adequate resources for additional planning, implementation, and evaluation.

The administration recognizes the importance of funding this major reform effort and has requested for fiscal year 2005 over \$10 million for a performance pay fund in the first phase of implementation (affecting about 8,000 employees) to recognize those who meet or exceed expectations and \$100 million to fund training and the development of the performance management and compensation system. In particular, DHS is appropriately anticipating that its revised performance management system will have costs related to both implementation and development – a fact confirmed by the experience of the demonstration projects. In fact, OPM reports that the increased costs of implementing alternative personnel systems should be acknowledged and budgeted for up front.

DHS is recognizing that there are up front costs and that its components are starting from different places regarding the maturity and capabilities of their performance management systems. At the same time, DHS is requesting a substantial amount of funding that warrants close scrutiny by Congress. In addition, certain costs are one-time in nature and therefore should not be built into the base of DHS's budget for future years. Furthermore, presumably most of any performance-based pay will be funded from what otherwise would be used from automatic across the board adjustments and step increases under the existing GS system.

For example, the DHS proposal correctly recognizes that a substantial investment in training is a key aspect of implementing a performance management system. The demonstration projects' experiences show that while training costs are generally higher in the year prior to implementation, the need for in-depth and varied training continues as the system is implemented. We have reported that agencies will need to invest resources, including time and money, to ensure that employees have the information, skills, and competencies they need to work effectively in a rapidly changing and complex environment.²³

Evaluating the impact of the system. High-performing organizations continually review and revise their human capital management systems based on data-driven lessons learned and changing needs in the environment. DHS indicates that it is committed to an ongoing comprehensive evaluation of the effectiveness of the human capital system, including the establishment of human capital metrics and the use of employee surveys. Collecting and analyzing data is the fundamental building block for measuring the effectiveness of these approaches in support of the mission and goals of the agency.

DHS should consider doing evaluations that are broadly modeled on the evaluation requirements of the OPM demonstration projects. Under the demonstration project authority, agencies must evaluate and periodically report on results, implementation of the demonstration project, cost and benefits, impacts on veterans and other equal

²³U.S. General Accounting Office, *Human Capital: A Guide for Assessing Strategic Training and Development Efforts in the Federal Government*, GAO-03-893G (Washington, D.C.: July 2003).

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employment opportunity groups, adherence to merit system principles, and the extent to which the lessons from the project can be applied governmentwide. A set of balanced measures addressing a range of results, customer, employee, and external partner issues may also prove beneficial. An evaluation such as this would facilitate congressional oversight; allow for any midcourse corrections; assist DHS in benchmarking its progress with other efforts; and provide for documenting best practices and sharing lessons learned with employees, stakeholders, other federal agencies, and the public.

Building a DHS-wide workforce plan. DHS has recently begun drafting a departmental workforce plan, using the draft strategic plan as a starting point. Workforce plans of different levels of sophistication are used in the five legacy agencies we studied. Despite the efforts of the DHS legacy agencies we studied, DHS headquarters has not yet been systematic or consistent in gathering relevant data on the successes or shortcomings of legacy human capital approaches or current and future workforce challenges—a deficiency that will make workforce planning more difficult. The strategic workforce plan can be used, among other things, as a tool for identifying core competencies for staff for attracting, developing, and rewarding contributions to mission accomplishment.²⁴

Involving employees and other stakeholders in designing the details of the system. We reported last fall that DHS's and OPM's effort to design a new human capital system were collaborative and facilitated participation of employees from all levels of the department.²⁵ We recommended that the Secretary of DHS build on the progress that has been made and ensure that the communication strategy used to support the human capital system maximize opportunities for employee involvement through the completion of the design process, the release of the system options, and implementation, with special emphasis on seeking the feedback and buy-in of frontline employees.

Moving forward, employee perspectives can provide insights on areas that deserve particular attention while implementing the new performance management system. For example, DHS employees responding to the OPM FHCS reported that

- 37 percent indicated that high-performing employees are recognized or rewarded on a timely basis, which is lower than the governmentwide average of 41 percent;
- 60 percent believe that their appraisals are fair reflections of their performance, which is lower than the governmentwide average of 65 percent;
- 23 percent believe that steps are taken to deal with a poor performer who cannot or will not improve, which is lower than the governmentwide average of 27 percent; and
- 28 percent perceive that selections for promotions in their work units are based on merit, which is lower than the governmentwide average of 37 percent.

In the GAO survey, members of the field team said that the most critical challenge in terms of performance management will be to create a system that is fair. Such data

²⁴U.S. General Accounting Office, *Human Capital: Key Principles for Effective Strategic Workforce Planning*, GAO-04-39 (Washington, D.C.: Dec. 11, 2003).

²⁵GAO-03-1099.

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underscore the continuing need to involve employees in the design and implementation of the new system to obtain their buy-in to the changes being made. More specifically, employee involvement in the validation of core competencies is critical to ensure that the competencies are both appropriate and accepted.

Summary Observations

As we testified on the DOD civilian personnel reforms, the bottom line for additional performance-based pay flexibility is that an agency should have to demonstrate that it has a modern, effective, credible, and as appropriate, validated performance management system in place with adequate safeguards, including reasonable transparency and appropriate accountability mechanisms, to ensure fairness and prevent politicalization and abuse of employees. To this end, DHS's proposed regulations set the foundation for results-oriented pay reform and modern performance management. DHS's performance management system is intended to align individual performance to DHS's success; hold employees responsible for accomplishing performance expectations; provide for meaningful distinctions in performance through performance- and market-based payouts; and be fair, credible, and transparent. However, the experiences of leading organizations suggest that DHS should require core, and as appropriate, validated competencies in its performance management system. The core competencies can serve to reinforce employee behaviors and actions that support the DHS mission, goals, and values and to set expectations for individuals' roles in DHS's transformation, creating a shared responsibility for organizational success and ensuring accountability for change. DHS should also continue to build safeguards into its revised human capital system.

DHS's overall effort to design a strategic human capital management system can be particularly instructive for future human capital management and reorganization efforts within specific units of DHS. Its effort can also prove instructive as other agencies design and implement new authorities for human capital management.

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

Contacts and Acknowledgments

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Appendix I

Methodology

In presenting our preliminary observations on the Department of Homeland Security's (DHS) regulations, we reviewed the proposed human capital regulations issued jointly by DHS and the Office of Personnel Management (OPM) on February 20, 2004, in the *Federal Register*. Additional documents reviewed include relevant laws and regulations, the 52 DHS human capital system options released in October 2003, and testimony presented by leaders of DHS employee unions and the Merit System Protection Board (MSPB). Interviews with experts in federal labor relations and the federal adverse actions and appeals system provided additional insights. The official transcripts and report summarizing the proceedings of the Senior Review Advisory Committee meetings in October 2003 were also examined. A draft of the report summarizing the proceedings of the Senior Review Advisory Committee meetings in October 2003 was reviewed by members of the committee to ensure its reliability. Additionally, we attended the committee's October 2003 meetings. Relevant GAO reports on human capital management were used as criteria against which the proposals were evaluated.

To respond to your particular interest in seeking out and incorporating employee perspectives on the human capital system, we gathered information on employee perceptions from a variety of sources and presented these findings throughout the statement. Insights to employee opinions were gathered from OPM Federal Human Capital Survey (FHCS), a GAO-administered survey of the field team used to inform the human capital system design effort, and a report summarizing findings from the DHS focus groups held during the summer of 2003.

OPM Federal Human Capital Survey

To assess the strengths and weaknesses of selected provisions of DHS's proposed human capital system, we reviewed the analysis of the DHS component agencies' responses to relevant questions on OPM's FHCS of 2002 for those legacy components that are now within DHS: the Animal and Plant Health Inspection Service (APHIS); the U.S. Coast Guard; the U.S. Customs Service; the Federal Emergency Management Agency; the Immigration and Naturalization Service; Federal Law Enforcement Training Center; U.S. Secret Service; Office of Emergency Preparedness and National Disaster Medical System; and the Federal Protective Service. This governmentwide survey was conducted from May through August 2002. It was administered to employees of 24 major agencies represented on the President's Management Council, which constitute 93 percent of the executive branch civilian workforce. There were 189 subelement/organizational components of the 24 agencies that participated. The sample was stratified by employee work status: supervisory, nonsupervisory, and executive. Of the more than 200,000 employees contacted, a little over 100,000 employees responded to the survey, resulting in a 51 percent response rate. OPM reported that the margin of error for the percentages of respondents governmentwide was plus or minus 1 percent at a 95 percent confidence interval. Likewise, it reported that the margin of error for the

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percentages of respondents for individual agencies was somewhat higher but less than plus or minus 5 percent.

The OPM survey was conducted during the same time frame that the administration proposed legislation to form DHS; thus, the opinions expressed by the respondents to the survey were before the formation of DHS. For reporting purposes, OPM compiled the DHS responses by combining the various subentities cited above. The responses approximate the views of some, but not all, employees now at DHS. For example, the Transportation Security Administration (TSA) screeners were not hired at the time of the survey. Also, APHIS employees were divided between DHS and the Department of Agriculture (USDA), so the APHIS respondents included some employees who remained at USDA.

Because OPM did not provide us with a copy of the full survey data set that included all records or the strata weights for any of the records, we could not perform our own analyses of the data or calculate the confidence intervals that would be associated with such analyses. OPM did, however, provide us with access to a Web site that provided reports with weighted data analyses for the FHCS 2002. We addressed the reliability of the survey analyses by (1) reviewing existing information about the survey data collection and analysis processes and (2) interviewing OPM agency officials who were knowledgeable about the data. We determined that the data were sufficiently reliable for the purposes of this testimony. We reviewed the analyses of the DHS component agencies presented on the Web site in four areas (pay and performance management, classification, labor relations, and adverse actions and appeals) that compared the component's data to DHS-wide data and DHS-wide data to governmentwide data.

Field Team Survey

We were interested in obtaining the views of the field team participants who served as a key source of information for DHS's Core Design Team. The field team consisted of DHS managers and staff. Members were selected by departmental management or the three major unions.

From October through December 2003, we surveyed the 31 members of the team to obtain their insights into the DHS design process and proposed human capital system options. The survey, administered by e-mail and fax, contained two parts. The first part addressed their views on how effectively the field team was utilized throughout the design process. The second part addressed their views about human capital challenges and the proposed policy options in four areas: (1) pay and classification, (2) performance management, (3) labor relations, and (4) discipline and appeals. Prior to distribution, the questionnaire was reviewed by DHS and OPM officials and pretested with a field team member to ensure clarity of the questions and determine whether the respondent had the knowledge to answer the questions. The questionnaire was revised based on their input. We received completed questionnaires from 19 of 31 field team members. We aggressively followed up with nonrespondents by telephone and e-mail. Because many of the field team members were either not based in offices, on extensive travel, or

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difficult to reach, we extended our survey through December 2003. The views that we obtained are not representative of all the participants.

DHS Focus Groups

DHS conducted multiple focus groups and Town Hall meetings from the end of May through the beginning of July 2003 in 10 cities across the United States.²⁶ Six focus group sessions were held in each city to obtain employee input and suggestions for the new human resource system. In most cities, five of the six sessions were devoted to hearing employees' views while the remaining sessions heard the views of supervisors and managers. Each focus group was facilitated by a contractor. The contractor used a standard focus group facilitation guide to manage each session. Additionally, the contractor was responsible for recording the issues identified during each focus group session and compiling a summative report on the findings from all the focus groups. We did not attend any focus group sessions and were not able to review any original notes from the sessions to assess the accuracy of the summative report.

Participation in the focus groups was not random nor was it necessarily representative of DHS employees. DHS reports that employee participation generally reflected the population in that location. For example, the level of bargaining unit representation at the focus groups was determined based on OPM data on bargaining unit membership. Bargaining unit employees were selected by union representatives to participate in the focus groups, while nonbargaining unit employees and supervisors were selected by DHS management. Union representatives and DHS managers were asked to select a diverse group of participants based on occupation, work location, gender, ethnicity, and age.

This work was done in accordance with generally accepted government auditing standards from March 2003 through February 2004.

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²⁶The 10 cities were Atlanta, Georgia; Detroit, Michigan; El Paso, Texas; Los Angeles, California; Miami, Florida; New York, New York; Norfolk, Virginia; Seattle, Washington; Washington, D.C.; and Baltimore, Maryland.