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before the

SUBCOMMITTEE ON OVERSIGHT OF GOVERNMENT MANAGEMENT, THE
FEDERAL WORKFORCE, AND THE DISTRICT OF COLUMBIA

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UNITED STATES SENATE

on

ALTERNATIVE PERSONNEL SYSTEMS:
ASSESSING PROGRESS IN THE FEDERAL GOVERNMENT

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Good morning, Mr. Chairman and Members of the Subcommittee. On behalf of Director

Springer, I want to thank you for the opportunity to appear before you today to discuss

alternative personnel systems in the Federal Government. We are pleased to share that record

with you because we believe these systems have successfully established work places and

cultures where "performance matters" and where high and low performers are distinguished and

rewarded accordingly.

The concept of "alternative personnel systems" is most clearly connected with the

demonstration projects Congress authorized the Office of Personnel Management (OPM) to

establish as part of the Civil Service Reform Act of 1978. That authority provided a means for

the Government to try out alternative merit-based approaches to specific personnel management

tasks and processes before making them more generally applicable.

The demonstration projects that established alternative personnel systems over the years

since 1978 have covered several different areas of human resources management policy,

including recruitment, examining, employee relations, and, of course, classification and pay.

These projects have consistently pursued the goals of better managing, developing, and rewarding employees to better serve the American people.

Many successful efforts have already led to Congress enacting permanent changes to title 5 for the entire Federal Government, as the architects of the demonstration authority intended. As early as 1990, the pay system changes enacted in the Federal Employees Pay Comparability Act, or FEPCA, included authorities for flexibilities like recruitment and retention incentives that had been successfully tested in demonstration projects.

More recently, the Chief Human Capital Officers Act of 2002, which you, Mr. Chairman, shepherded as part of the Homeland Security Act of 2002, authorized a significant alternative examining method known as "category rating." This method had originally been developed in a demonstration project at the Department of Agriculture. Now any Federal agency is free to use that method as a standard hiring practice, and we continue to see an increase in its successful adoption across Government.

These successes illustrate the original intent of the demonstration project authority – develop and refine alternatives under OPM supervision and oversight and then make them available throughout Government.

That brings us to the largest – and oldest – set of alternative personnel systems I would like to focus on today. By far, agencies have most often sought flexibilities to use alternatives to the General Schedule classification and pay system. Agencies determined to pursue improvements to the strategic management of their human capital and achieve success in the heated competition for talent continually seek opportunities to move beyond the General Schedule. They seek to leave behind our 50-year-old 15-grade pay structure of fixed steps with

its automatic and longevity-based pay increases. They want to advance to job evaluation and pay designs that emphasize and reinforce performance and results.

By now, we have substantial experience with using alternative pay systems that cover over 90,000 Federal employees in a wide variety of agencies, occupations, and work settings. More than half these employees are in systems established under the title 5 demonstration project authority. Another third are in independent systems that their agencies established using separate, agency-specific authorities. And another 9 percent are covered in executive pay systems that have recently become true pay-for-performance systems where all pay increases are driven by measured performance.

Although each of these alternative pay systems is unique in some respects, common design features emerge. They use open ranges of pay rates rather than fixed steps. Any pay increase is usually contingent on an assessment that the employee's performance is at least fully successful. The pay increases that move employees through their pay ranges are directly – and differentially – linked to performance assessments, rather than the passage of time. Position classification is streamlined and pay ranges cover more broadly defined levels of work than the narrow General Schedule grades. Overall these alternative pay systems emphasize and reward strategic value and contributions over simply encumbering a position and meeting minimum acceptable standards.

The positive results and trends across these systems are clear. We do not have to wonder whether they work. We know they work based on a range of widely accepted effectiveness benchmarks.

- The highest rated performers are paid the most, and rewards can vary significantly based on performance. Annual pay increases ranged from 0% for low performers to

as much as 20% for top performers. At China Lake, the first demonstration project, there was a 40 percent difference in pay between the average and high performers after 10 years.

- Performance – not time – drives pay. The alternative systems replace statutory waiting periods for within-grade step increases and career-ladder promotions. In the majority of systems, the annual general increase is at risk and not granted to poor performers.

- Agencies implement these systems within their existing budgets, and costs can be controlled. As we have applied lessons learned from the earliest demonstration projects, we have developed effective cost management techniques built around pre-determined salary increase budgets. Training and implementation costs are generally absorbed as necessary business expenses.

- Managers are trained to manage performance more effectively and are held accountable for that and for making meaningful distinctions across levels of performance. Clearly, taking the time to make sure managers understand the new systems and how to use them effectively and transparently is key to achieving acceptance and support for the systems. Rating reconsideration processes are built in to these systems to ensure procedural justice. Techniques like calibration discussions help ensure meaningful distinctions among levels of performance are made across organizational units. Performance ratings distributions in most locations clearly demonstrate that distinctions are being made.

- Turnover among the better performers is significantly reduced. Among employees rated Outstanding in four Department of Defense laboratory demonstration projects

(DoD Lab Demos) where this measure was tracked most carefully, the annual turnover rates were reduced by 64 percent, 51 percent, 48 percent, and even 11 percent in a lab where external competition was particularly pronounced.

Of course, employee perceptions of how well these alternative systems are working are critical. The various program evaluation efforts that are an integral part of demonstration projects have produced a rich store of employee survey data from before and after implementing systems and as comparisons to control sites.

- Employees report seeing a direct link between their performance and their pay. In the Lab Demos, that link was reported by two out of three employees, compared with only one out of three employees in control sites under the General Schedule.

- Pay satisfaction is higher after the systems are implemented. Bearing in mind that pay satisfaction starts out at fairly high levels in our traditional Federal pay systems, the fact that pay satisfaction measures showed increases in the 19 to 48 percent range is encouraging.

- Teamwork is supported and not destroyed. LabDemo survey results showed not only that teamwork was not negatively affected, but it increased more in the demonstration sites than in control sites.

- Employees can and do come to understand and accept these alternative pay systems. Measures of support for the demonstration projects range as high as 80 percent. Even where the explicit support is more temperate (e.g., 26 percent, 48 percent), the largest proportion of employees are undecided (e.g., 44 percent, 41 percent) rather than opposed, and other data in those settings suggest some standard implementation efforts require better attention and monitoring.

- Procedural justice is addressed and reinforced. The procedures governing appraisal and pay decisions are crucial, particularly those that give employees a chance to seek reconsideration or redress. Employees in the LabDemos report they understand how their appraisal systems work (72 to 89 percent agreement) and how pay decisions are made (58 to 70 percent agreement). Further they generally agree adequate reconsideration procedures are available. Such results are key to achieving an overall perception of fairness and transparency.

- The trust that leads to success can be earned through good communication and fair administration. Demonstration projects showed significant improvements in communication from management and across organizational units. And, in turn, the already high correlations between communication and procedural justice, as well as between communication and trust, remain strong.

Of course achieving this success does entail significant culture change. Such change requires commitment and communication and training and followthrough, but agencies have proven willing to make the investment. OPM is careful to check for that commitment and ensure it is in place and well founded before encouraging an agency to proceed with any alternatives.

When such commitments are present, the results are definitely encouraging. By the standard benchmarks discussed above, these alternative pay systems are successful. We can indeed devise and operate fair, credible and transparent pay systems in the Federal Government that shift the value proposition.

Generally speaking, under an alternative pay system the money distributed as salary increases is comparable to what would have been distributed under the General Schedule. The important difference lies in the basis used to make pay determinations and the value that basis

represents. For the General Schedule, time is the overwhelming basis for distributing increases, so the message to employees is "Time matters." In the alternative pay systems tested in demonstration projects in the Departments of Defense and Commerce and in other independent systems, pay increases differ based on differences in appraisal outcomes. By making performance much more clearly the basis for distributing pay increases, the message to employees becomes "Performance matters."

Particularly in the war for talent, establishing the right value proposition – that performance is what we value and what makes a difference – can be critical. It definitely has been worth pursuing.

You asked us to discuss the role OPM has played in developing and overseeing these alternative systems. Congress clearly gave OPM a key role in the demonstration projects because we establish them only after carefully considering a proposed design for conceptual and technical soundness. We take very seriously the requirement that demonstration projects include a thorough evaluation. The information those evaluations produce has been a rich source of best practices and lessons learned to apply as designs evolve further both within the demos specifically and wherever possible, Governmentwide. For example, effective cost control techniques like salary increase budgets, the value of balancing base pay adjustments and lump-sum bonuses to recognize performance, and the clear impact of communications and effective manager training on understanding and acceptance of system changes have all been recognized and applied more generally as a result of the demonstration projects.

In that respect, OPM is leveraging its leadership of the Human Capital Initiative of the President's Management Agenda. Using a "beta site" or piloting approach, we are establishing goals for agencies that will further the development of robust performance management systems.

For a particular site within the agency, evidence must be clear that managers are effectively setting expectations, providing employees ongoing feedback, appraising employee performance, and using awards programs to reward results. In other words, we will require evidence that the site is ready to link pay to performance appraisal systems, with the expectation that such improvements will expand and continue throughout the agency.

Even where Congress has granted an agency some independent authority, OPM still plays a role. In some instances, Congress assigns us a specific role, as with the Internal Revenue Service broadbanding authority which requires OPM to issue criteria the Secretary of the Treasury must follow in establishing any broadbanded system at IRS.

Beyond that, however, OPM has its normal oversight and accountability responsibilities. Of course we are always mindful of those responsibilities, but especially when alternatives to the standard title 5 provisions are being used. When OPM observes or even foresees difficulties in implementing a system feature, our experts step right in to notify the agency and assist in making appropriate design corrections or otherwise address emerging issues.

OPM's leadership role is also essential to making these alternative pay systems work successfully. In particular, we try to anticipate unintended consequences, to act on lessons learned, and to articulate and share best practices. OPM provides expert guidance which the agencies find invaluable in tailoring sensible approaches to meet their unique needs and avoiding problems.

Improvements in implementation and cost management strategies have evolved over time with the more recent projects. For example, after recognizing the cost consequences of certain design features in some early demonstration projects, OPM ensured they would not be duplicated in subsequent systems. We take particular care in reviewing which General Schedule grades an

agency is proposing to band together because that can have a significant impact on overall system costs.

In that sense, OPM's role as a gatekeeper is well-placed. The Congress understood that the freedom to do different things meant the consideration of some options that might be ineffective or inefficient, and has looked to OPM to keep agencies on course and not let them steer into harm's way.

OPM and the Federal Government have already learned and applied important lessons through these alternative pay systems. We believe the time has come to allow these alternatives to achieve the same permanence other successful demonstration projects like category rating have earned. The ideas the Administration is incorporating into our Working for America legislation are the legacy of these successful projects and systems. We are convinced these ideas work. And we are convinced these and other agencies are ready to be given carefully controlled access to making these ideas a permanent part of their human capital management systems.

The Working for America Act would give OPM a central leadership role and the responsibility to establish core classification and pay systems. We believe Congress should authorize core systems for two main reasons. First, applying a basic principle of leveraging scale to achieve efficiency makes it more sensible to assign the task and resources necessary to set up, adjust, and maintain market-sensitive pay schedules to one lead agency with well-established expertise. Second, we have enough evidence from recent experience with independent systems and authorities to agree concerns about dysfunctional inter-agency competition are well placed and are best addressed through common pay structures and pay rules.

As a step toward transitioning to alternative systems, by using the President's Management Agenda and Executive Branch Management Scorecard, the Administration has

been hard at work readying agencies to demonstrate they use robust performance management systems. Agencies are preparing themselves to embrace a truly results-oriented performance culture through the use of more performance- and market-sensitive classification and pay systems. Already the performance management systems in some agency settings are ready to support making stronger links between pay and performance, and elsewhere significant progress is being made. OPM is determined to ensure their success and we look forward to your continued support as we do so.

That concludes my testimony, Mr. Chairman. I would be happy to answer any questions you may have.