PARTNERSHIP FOR PUBLIC SERVICE

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Federal Agencies with Human Resources Flexibilities: An Assessment and Recommendations

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Chairman Davis, Representative Marchant, Members of the Subcommittee, thank you very much for the opportunity to appear before you today. I am Kevin Simpson, Executive Vice President and General Counsel of the Partnership for Public Service, a nonpartisan, nonprofit organization dedicated to revitalizing the federal civil service by inspiring a new generation to serve and transforming the way the federal government works. We appreciate your invitation to discuss the human resources (HR) management flexibilities currently available in statute for the Departments of Defense and Homeland Security, the Transportation Security Agency, the Government Accountability Office, and a variety of other federal departments, agencies, and agency subcomponents.

The Partnership has two principal areas of focus. First, we work to inspire new talent to join federal service. Second, we work with government leaders to help transform government so that the best and brightest will enter, stay and succeed in meeting the challenges of our nation. That includes all aspects of how the federal government manages people, from attracting them to government, leading them, supporting their development and managing performance; in short, all the essential ingredients for forming and keeping a world-class workforce.

An Urgent Need for Action

Americans need effective government, and the key to good government is good people. The report of the 9/11 Commission said it best: "[T]he quality of the people is more important than the quality of the wiring diagrams." Every day, we rely on our federal government to deliver vital services, from protecting the homeland to promoting a competitive economy to preserving our natural resources. Today, our nation faces challenges of unprecedented complexity – from combating terrorism and competing in a global marketplace to dealing with an aging population at home.

These new challenges require new skills from our federal workforce. Yet, at this critical time, a record number of experienced federal workers will soon retire, resign or otherwise leave the government, and insufficient interest in and knowledge about federal service leaves us with an inadequate pipeline of talent to replace these losses. Aggressive and immediate action is needed to strengthen the federal civil service, match new skills to current challenges, and build a government that the public deserves and the times demand.

The federal government's human capital crisis defies easy solutions and will require a comprehensive strategy. The federal government will live up to its potential in serving the American people only when our best and brightest answer the call to federal service and enjoy a work environment that empowers them to perform at their best. There are significant human capital challenges facing the federal government regarding its ability (or inability) to attract and recruit the talent it needs and to manage the federal workforce so that talented employees stay and succeed in achieving desired results.

The federal agencies and organizations that have been granted special HR authorities by Congress all, in one way or another, made a business case for change. One major theme in almost all of these organizations is that the current General Schedule (GS) pay and

classification system established in 1949 is no longer sufficient to attract and retain the best and brightest. Another common complaint fueling the drive for special HR authorities is the federal hiring process, which has become increasingly unwieldy for agencies and applicants alike.

An Overview of Civil Service Reform Efforts

For much of its history, the federal civil service and the underlying HR laws, policies, and practices intended to guide federal workforce management were remarkably uniform across agencies. However, as the demands upon government grew over the past several decades in response to a growing population and a more complex and technologically advanced world, it became clear that some civil service reforms were needed.

Perhaps the largest civil service reform effort in recent memory was the Civil Service Reform Act of 1978. The 1978 Act made some significant changes to the civil service, such as the creation of the U.S. Office of Personnel Management and the Senior Executive Service. It provided, for the first time, statutory recognition of labor-management relations. When the law was passed, Congress recognized that the specific government-wide reforms being authorized were unlikely to be sufficient, and it established a research and demonstration project authority (title 5 U.S.C. § 4703) to help guide future reform efforts. Over time, several of the demonstration projects undertaken were allowed to become permanent alternative personnel systems.

Congress has also recognized for quite some time that "one size doesn't necessarily fit all" when it comes to HR systems. For example, the U.S. Post Office became the U.S. Postal Service in 1970 with significant changes in its HR policies and systems that had previously been guided by Title 5. Earlier, in creating the Tennessee Valley Authority, Congress gave it wide discretion in the development of its HR systems. Similarly, the Veterans Administration (now the Department of Veterans Affairs) was given authority to manage its medical personnel under a different legal framework, Title 38 of the U.S. Code. The National Nuclear Security Administration in the Department of Energy is the latest federal organization to announce plans to become a demonstration project.

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) gave special pay-setting authority to agencies such as the National Credit Union Administration (NCUA) and the Federal Deposit Insurance Corporation (FDIC). The Securities and Exchange Commission (SEC) was recently given comparable authorities. The Internal Revenue Service (IRS), Federal Aviation Administration (FAA), NASA, the Transportation Security Administration (TSA), and Congress's own Government Accountability Office (GAO) have all been granted special HR authorities by Congress. The Departments of Defense and Homeland Security, which together employ over 42 percent of all civilian employees in the executive branch, are only the most recent federal departments granted relief from parts of Title 5 of the U.S. Code that were deemed too inflexible or counter-productive.

A Current Assessment

So, how well have these department and agency-specific personnel systems been implemented and have the desired end-results been achieved? In summary, here are our perspectives on a selected number of those agencies:

- **Demonstration Projects:** The federal organizations and subcomponents with special HR authorities established as demonstration projects (5 U.S.C. § 4703) were carefully vetted as to their readiness to "test" alternative personnel systems. A detailed project plan was developed; employees under union bargaining agreements were not included without prior consultation or negotiation, as appropriate; and a rigorous external evaluation of the demonstration project was conducted.

  While many of the demonstration projects were subjected to refinements over time and at least one attempt at gain-sharing (Pacer Share at McClellan Air Force Base) expired with a finding that it did not meet expectations, most demonstration projects were ultimately judged to be superior to the systems they replaced. This was the case even when a majority of federal employees were initially resistant to the changes being made since, over time, employee acceptance typically improved.

  A January 2004 GAO report (GAO-04-83) based on an examination of "pay for performance" approaches at six established demonstration projects found, for example, that the pay-banded, pay-for-performance demonstration project started in 1980 at the Department of the Navy's China Lake Naval Weapons Center was initially favored by only 29 percent of employees, but by 1998 that number had grown to 71 percent. GAO concluded that it "strongly supports the need to expand pay-for-performance in the federal government. 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 Government Accountability Office** (GAO) presents another interesting example of an alternative personnel system. The GAO, of course, operates as part of the legislative branch. Until the mid-1970s, GAO followed many of the same Title 5 HR rules and regulations as the executive branch. For a number of years, however, GAO has operated under a pay-banded, pay-for-performance approach. Most recently, that has included a move to market-based pay. This latter move came with a determination that at least some jobs in GAO were being paid "above-market."

  GAO employees, based on published media accounts, have expressed unhappiness with the most recent changes. However, since GAO has shared some of its annual employee survey results with the Partnership for Public Service in order to be included in our "Best Places to Work in the Federal Government" rankings, we know that while overall employee satisfaction did decline by approximately three percentage points between 2004 and 2006, GAO's own employees still rate it among the top five "best places to work" compared to other large departments and agencies.

- **The Federal Aviation Administration** (FAA) was unique in that Congress effectively removed FAA from almost all of the restrictions of Title 5 and gave them great latitude to design a more effective HR system. After a series of false starts, during which FAA found it necessary to proclaim that it would adhere to the basic merit principles and veterans preference and was ultimately directed by Congress to grant their employees appeal rights to the Merit Systems Protection Board which they had replaced with an internal review board, the FAA completed the design and implemented the system. While FAA has now had time to achieve a better balance, for a time, the main change for FAA seemed to be the negotiation of higher wages for employees. The lesson learned here is that some guidance from Congress and clearer expectations are beneficial in reform efforts.

- **FIRREA agencies.** Those agencies covered by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) benefited largely from the ability to set higher, more market-sensitive wages for their employees. The law also requires that the pay levels be comparable to that of one another for comparable jobs, lest they simply compete with one another. Clearly, the ability to set higher, more competitive salaries has benefited the ability of the FIERRA agencies to hire and retain needed talent. It should be noted, however, that higher salaries alone do not translate into a better work environment. Two FIRREA agencies, the National Credit Union Administration (NCUA) and the Federal Deposit Insurance Corporation (FDIC) both pay similar wages and both operate under a pay-for-performance approach. However, the NCUA has consistently ranked substantially higher than the FDIC in the "Best Places to Work" rankings.

- **National Security Personnel System.** The Department of Defense designed a comprehensive set of proposed regulations to implement the NSPS that drew heavily from its experience with alternative HR systems under the 1978 demonstration project authority (Title 5 U.S.C. § 4703). DOD proposed a pay-banded approach to compensation that would be more market-sensitive as well as more performance-sensitive than the GS system. Other changes proposed by DOD and authorized in the NSPS involve additional flexibilities in the areas of hiring and some new "workforce shaping" provisions to address current or anticipated skills gaps.

  DOD also designed some alternatives to its labor-management relations policies and to the process by which employees could appeal a proposed adverse personnel action. Those proposed changes had <u>not</u> been previously tested through demonstration projects or in other federal organizations. When these latter changes were challenged in court by employee unions, the D.C. District Court enjoined those parts of the regulations as inconsistent with the legal requirements of the NSPS. A decision on a DOD appeal of the lower court ruling is expected from the D.C. Circuit Court of Appeals in the next several weeks. In the meantime, DOD has started implementation of their proposed changes for selected non-bargaining unit employees only. This latter implementation is being done in "Spirals" with the first of three initial roll-outs (Spiral 1.1) implemented in 2006. The first performance management cycle and payouts under Spiral 1.1 were completed in January 2007.

While a full evaluation of the impact of the NSPS is premature, we note that many of the principles -- other than those proposed in the areas of employee due process and labor-management relations -- have been thoroughly tested in DOD and a number of other federal agencies over the past 25 years. It will take a period of time before the effects and potential benefits of the NSPS can be fully assessed. However, we believe that many (but not all) aspects of NSPS – if implemented with employee involvement and strong congressional oversight – have the potential to make a positive difference and to gain acceptance by the DOD civilian workforce.

- **Department of Homeland Security.** Similar to and preceding the NSPS, the Department of Homeland Security (DHS) was granted major exemptions from Title 5 requirements, including in the areas of pay and performance, when it was created under the Homeland Security Act of 2002. DHS went through an extended consultation period with employees and other stakeholders while designing their new HR systems, dubbed "MaxHR," that included a pay-banded approach to pay and was intended to be more sensitive to performance than the GS system. DHS, however, also designed new approaches to labor-management relations and employee appeals. As with the NSPS, the latter were challenged in court by employee unions. In the case of DHS, the final court ruling that the planned labor-relations provisions are inconsistent with the law has not been appealed further.

  Most recently, DHS has announced their intent to "move beyond MaxHR" and to focus on broader HR issues and initiatives under a "Human Capital Operational Plan." The plan will focus on improved hiring and retention, creating a "culture of performance" based on well-thought out and implemented performance management plans, and enhanced training and development. While there are still plans to move toward a more market and performance-sensitive pay system, DHS is moving at a slower pace than originally planned. It is, of course, much too early to assess the results of the alternative personnel systems authorized by Congress for DHS since they have largely remained in the planning stages. However, the current direction and more deliberate pace of change within DHS is a promising development.

In short, well over half of the 1.8 million civilian employees in the executive branch work in agencies whose HR systems are no longer tied by statute to the General Schedule (GS) pay and classification system. Most of the latter agencies also have additional flexibilities in the areas of performance management and hiring.

It's clear that the process of making major changes in federal HR systems, especially in pay and performance management, involves culture change and well as system change. Such change is inevitably slow and iterative. The changes that have occurred in the aforementioned agencies have a mixed track record, to be sure, especially in terms of employee acceptance. We note, however, that a number of the federal agencies that have been allowed to operate under alternative personnel systems such as SEC, NASA and GAO have consistently been rated by their employees as among the top ranked "Best Places to Work."

In summary, we believe that movement back to the 1949-era General Schedule or a roll back of the authorities discussed above would likely have greater costs than benefits. None of the alternative personnel systems have been "magic bullets," but over time most have been improvements over what existed previously and the affected organizations would be loathe to return to the previous state. The challenge, therefore, is to effectively move forward from here and to ultimately bring all federal department and agencies onto a level playing field to the extent practicable.

Recommendations

In response to the current situation, the Partnership has the following recommendations:

1. Congress should allow federal agencies to continue their pursuit of more market-sensitive pay systems that also allow more flexibility in recognizing employee performance, classifying jobs and setting initial pay – particularly when the features of these alternative systems have been tested previously in a demonstration project.

2. Congress should require that an agency's alternative pay system must meet certain requirements, and be certified by OPM, GAO, or another entity specified by Congress, before it is implemented. The requirements for certification should include (a) a fair, credible and transparent performance appraisal system, (b) a means of ensuring employee involvement and ongoing feedback, and (c) a mechanism for ensuring the system is adequately resourced.

3. A key criterion for the success of any alternative personnel systems will be the presence of highly competent managers, supervisors, and HR professionals. Congress should ensure that federal agencies are making the necessary investment to select, train, and effectively manage the individuals in these key occupations, specifically with regard to their responsibilities under an alternative personnel system.

4. Congress should ensure that any alternative personnel system operate under common government-wide ground rules, and, in fact, Congress has provided such ground rules in most of the recent reform efforts (with FAA and TSA somewhat the exceptions). These ground rules should include:
    a. Adherence to the Merit System Principles in 5 U.S.C. § 2301(b) and the Prohibited Personnel Practices in 5 U.S.C. § 2302(b);
    b. Collaboration with and involvement of employees and managers;
    c. Collective bargaining with employee representatives via negotiated agreements;
    d. Due process rights for employees; and,
    e. Adherence to veterans' preference.

5. To assist agencies in designing a compensation system that conforms to these common ground rules, OPM should design a replacement for the 1949 General Schedule pay system and the associated classification system that is available as a template for all

agencies. The alternative system should be market-sensitive and give greater weight to performance than does the GS system.

6. Congress should carefully review and consider limiting future agency-initiated changes to the employee appeals process and labor-management relations to alleviate employee concerns about (a) fair and equitable treatment and (b) having a workplace in which they can be involved in decisions that affect them or their work.

7. In the case of the NSPS, the Subcommittee should review the process by which employees may appeal adverse personnel actions and consider a larger role for an adjudicatory body outside of, and independent from, DOD. One obvious approach would be to enlarge the role that the current regulations assign to the U.S. Merit Systems Protection Board. Of course, the forthcoming decision by the D.C. Circuit Court of Appeals will strongly influence this area.

8. Again, in the case of the NSPS, the Subcommittee should review the proposed changes to labor-management relations to examine concerns of bargaining unit employees regarding the ability of their union representatives to adequately safeguard their interest in (a) being treated in a fair and equitable manner and (b) having a workplace in which they can be involved in decisions that affect them or their work. Once again, the forthcoming decision by the D.C. Circuit Court of Appeals will strongly influence this area.

9. The Subcommittee should arrange for an ongoing assessment of current and future alternative personnel systems, as would be required if those alternative personnel systems were being designed and implemented under demonstration project authority. This ongoing assessment should be based on established criteria and indicators that will provide Congress with much-needed, objective insight into the impact of alternative personnel systems on agencies' missions and employees.

10. Congress should closely monitor agencies' investments in training and development. Too often, these accounts are among the first to be cut, when the fact is we need to be investing more in training and development, particularly when we are demanding more of managers and implementing a new system.

11. To assist Congress in the exercise of its oversight responsibility and to respond to any concerns that current or future HR reforms might actually detract from the ability of the respective federal agencies to accomplish their mission, the Partnership recommends the development and use of a set of metrics for the specific purpose of evaluating the reforms over time. Such metrics will only be of value if the Congress, the agencies, and other key stakeholders agree on a common set of measures to inform future decision-making. The following principles should apply in this regard:
    a. The key to effective oversight will be looking at the *right* measures, not the *most* measures.
    b. Metrics should include qualitative as well as quantitative measures.
    c. Metrics should not impose an undue collection and analysis burden on DOD.

d. Metrics should be used to inform decision-making and not simply to monitor compliance/non-compliance.

The Partnership has recently completed a thorough review of human capital metrics in federal, state and local governments, as well as the leading practices of top companies in the Partnership's *Private Sector Council (PSC)*, that serve as a useful guide to the Subcommittee in its oversight capacity.

Based on this research and mindful of the principles mentioned above, we recommend that the Subcommittee work with agencies pursuing alternative personnel systems to collect and analyze **metrics in seven areas**: *recruitment, retention, skills gaps, performance distinctions, performance culture*, *leadership* and *implementation*. The Subcommittee could gain additional insight from the data by looking at these metrics by specific demographic group – e.g., minority employees or a particular age group – as compared to the workforce as a whole.

Recruiting
To assess whether they are winning the war for talent, leading organizations are collecting information about **new hire rates** – e.g., the ratio of new employees hired to the number of planned hires for critical skills – and **new hire quality** – e.g., monitoring Federal Human Capital Survey results about the skills of new hires.

Retention
To measure whether DOD is retaining high-performing employees with critical skills, we recommend that the Subcommittee look at the **attrition rates of high performers** compared to overall attrition and the **attrition rates of critical skill employees** compared to overall attrition.

Skills Gaps
If NSPS is achieving its goals, DOD should be closing the gap between the **actual numbers of employees with a critical skill compared to the number needed**. Ideally, the Subcommittee will monitor the results over time to assess whether the gap is decreasing.

Performance & Rewards
A modern compensation system should make meaningful distinctions between employees based on their performance. Members can evaluate whether managers are effectively using the NSPS by monitoring **employee evaluations** – e.g., the numbers of employees reaching the various levels of performance – and **employee bonuses and rewards** – e.g., the number of employees receiving various levels of pay and bonuses.

Performance Culture
The Partnership advocated for, and the final NSPS legislation included, a provision requiring an annual survey of employees across the federal government. The survey should prove to be an invaluable window into employees' views of their agencies' management practices.

The survey questions specified in recent regulations issued by OPM include several questions about supervision and pay that constitute a **Performance Culture Index** with items such as:

- Promotions in my work unit are based on merit.
- In my work unit, steps are taken to deal with a poor performer who cannot or will not improve.
- In my work unit, differences in performance are recognized in a meaningful way.

The Subcommittee can compare the results of components participating alternative personnel systems with the results of components operating under the General Schedule system. The Subcommittee and the agencies involved will want to monitor the results over time to track whether the "performance culture" is increasing.

Leadership

In any organization, it is vital that supervisors and senior leaders treat employees fairly, resolve disputes in a reasonable manner, and have the respect of their employees. Members of the Subcommittee can evaluate leadership effectiveness by using another set of questions from the Federal Human Capital Survey. The Partnership has created an **Index for Effective Leadership**, which we use in our *Best Places to Work* rankings. This index includes items such as:

- I have a high level of respect for my organization's senior leaders.
- Complaints, disputes or grievances are resolved fairly in my work unit.
- In my organization, leaders generate high levels of motivation and commitment in the workforce.

The Subcommittee can compare an agency's scores on these questions to scores across government and the private sector.

Implementation – Pulse Surveys

Finally, it is important to examine real-time data on the success of alternative personnel systems and their implementation. **Pulse surveys** are short surveys going to a small, representative sample of employees used to provide leaders with real-time information on critical issues. Agencies could administer pulse surveys semi-annually to examine employee opinions on system training/briefings, understanding of the new system, satisfaction with the new system, et cetera. This data will allow agencies to improve the rollout of their systems based on employee feedback.

Conclusion

Mr. Chairman, Representative Marchant, Members of the Subcommittee, we thank you again for the opportunity to share our views on the new personnel systems in the federal government and our recommendations for the best way forward. We look forward to being of assistance to this Subcommittee and to the Congress as you consider the future of federal civil service policy.