The Great Government Pay Debate

Howard Risher, Editor

Introduction to the Debate

The three statements that follow were provided by individuals who have public positions that are likely to influence how government pay systems are planned and managed. Government pay and benefits have become political issues and the goal is to provide a forum prior to the election where three distinct positions can be stated, followed by comment and rebuttal.

The first statement, by the two independent members of the Federal Salary Council, Stephen Condrey and Rex Facer II, joined by a colleague Jared Llorens, argues for a variation on the existing program model. As background, the Council makes annual recommendations to the U.S. Office of Personnel Management (OPM) and the President’s Pay Agent on needed adjustments to the federal white-collar salary system.

The second was drafted by Andrew Biggs and Jason Richwine, prominent critics of government pay practices and occasional spokespersons on this subject for the American Enterprise Institute and the Heritage Foundation, respectively. Their comments are posted occasionally on the websites of their respective organizations.

The third statement was provided by Michael Filler, who serves as a presidentially appointed member of the National Council on Federal Labor–Management Relations and Director of the Public Services Division, International Brotherhood of Teamsters. The Teamsters has over 260,000 public and professional employees across North America.

Following each statement are comments by the two other “sides.”

This article is intended to highlight the issues that are contentious as well as those where there is agreement. A key point is the general agreement that government pay should be aligned with market levels although there are differences in exactly what that means.

The debaters:

Stephen Condrey and Rex Facer II, independent members of the Federal Salary Council, joined by a colleague Jared Llorens,

Andrew Biggs and Jason Richwine, occasional spokespersons on this subject for the American Enterprise Institute and the Heritage Foundation respectively

Michael Filler, presidentially-appointed member of the National Council on Federal Labor-Management Relations, and Director of the Public Services Division, International Brotherhood of Teamsters.
Reforming Federal Pay

Stephen Condrey, President of Condrey & Associates, President-Elect of the American Society for Public Administration, Chairman of the Federal Salary Council and Editor-in-Chief of the Review of Public Personnel Administration

Rex Facer II, Associate Professor of Public Finance and Management, Romney Institute of Public Management, Brigham Young University, and member of Federal Salary Council

Jared Llorens, Assistant Professor, Louisiana State University Public Administration Institute

The topic of federal pay systems and overall pay comparability appears to be developing into a potential presidential campaign issue. Despite recent criticisms of the effectiveness of the General Schedule (GS) pay system, we believe it has served the federal government’s workforce well for a number of years. However, the current GS system needs to be revitalized to ensure that it meets the strategic objectives of the federal government, is compatible with modern organizational structures and addresses the rapidly developing needs of contemporary human resource management systems.

Ultimately, the sheer size and scope of the federal GS system makes any effort at examination and reform a complex challenge. As such, we believe support from top leadership, committed to recognizing the contribution of federal employees, will be necessary to accomplish the reforms we propose. We suggest, in this brief essay, that the basic structure of the federal GS system provides an effective way to classify positions and compensate federal workers and, therefore, should serve as a foundation for a revitalized compensation strategy. However, as with any compensation system, it is time to reevaluate the federal system for both enhanced external and internal alignment.

External Compatibility: Strengthening Salary Survey Data

The OPM and the Federal Salary Council depend on the Department of Labor’s Bureau of Labor Statistics (BLS) to provide annual salary survey data to adjust pay rates within the GS system. Recently, the Department of Labor has chosen to discontinue funding for the Bureau’s National Compensation Survey (NCS) and adopt a salary survey approach based on the statistical modeling of salary comparability using data from the Occupational Employment Statistics survey. In effect, this new approach will rely on a more limited data sample to estimate pay comparability between the federal government and private sector.

Instead of discontinuing the NCS, we believe that the Department of Labor should expand and strengthen this important survey to provide more grounded assessments of federal pay comparability. Sound compensation decisions are based on transparent and robust data. An expanded NCS would strengthen overall confidence in how federal pay rates are determined, as well as provide for more reliable assessments of the competitiveness of federal pay.

Furthermore, salary administration should be based on a conscious philosophy outlining where an organization wants to set its pay rates in relationship to those rates provided in the relevant labor market. In our opinion, the NCS provides the necessary data to make these decisions while methodologies grounded in statistical modeling fall considerably short of meeting this goal.

Internal Alignment: Ensuring Equity

While much of the “debate” concerning federal pay has been focused on external market data, it is our contention that internal alignment issues are also of particular concern. Any effective compensation system balances the need for external market competitiveness with an equitable internal alignment of positions within an organization.

It is our opinion that the OPM should be given authority to make strategic, internal adjustments to the federal GS system to remedy existing inequities. These adjustments include the following action items:

- Allow for grade-level pay rate adjustments to better reflect the relevant labor market. Targeted adjustments of this type would better capture the upper end of the labor market.
- Strengthen OPM’s ability to audit agency classification decisions to better assure equal pay for equal work across federal agencies.
- Expand pay ranges within GS grades from the current 30% to 40% or 50% from minimum to maximum compensation. Expanding the within-grade pay ranges would ease the pressure on reclassification actions, more closely reflecting the pay ranges of large organizations and alternatively lessening the “pay gap” present in the federal GS.
- Consolidate disparate federal pay systems where possible. It is impossible to manage an overall pay philosophy or vision with the dozens of special pay authorities that exist today. Where feasible, it is our recommendation that these systems be brought back under a revitalized GS system.
• Strengthen career ladders and lattices to more closely link career progression and individual employee movement through the salary schedule. Strengthening career ladders for federal workers provides greater employee control over career progression and is more compatible with modern organizational theory and philosophy.
• More closely link pay and performance. While we believe that pay and performance should be more closely linked, a full-scale pay-for-performance system with open ranges and wide variations in possible pay outcomes will not work in the federal government setting. What we recommend is a reduction in step values coupled with expanded pay ranges to allow an increased use of quality steps and a renewed emphasis on recognizing outstanding performance.

Federal Pay Issues in Summary
As is clear from this essay, we approach federal pay from a technical/organizational perspective rather than a partisan or political one. We realize that issues surrounding federal pay take place in a political environment. However, the political discourse and rhetoric surrounding the compensation of federal workers have certainly increased and become decidedly more partisan over the past several years. It is our hope that a more data-driven approach to healing what ails the federal pay system will win out over partisan debate. The federal GS has provided a sound basis and framework for setting federal pay for decades—it is time to modernize it, not demonize and abolish it.

Comments by Biggs and Richwine
We strongly agree with the authors that continued funding of the BLS NCS is in the public interest. We would expand the NCS to cover federal employment to provide a cleaner apples-to-apples comparison between federal, state/local and private sector pay and benefits.

We disagree, however, with the authors’ contention that “the NCS provides the necessary data to make these decisions while methodologies grounded in statistical modeling fall considerably short of meeting this goal,” a statement for which they provide no explanation or evidence. As we note in our statement, NCS employer survey data align well with household survey data such as from the Current Population Survey when it comes to comparing state and local government pay to that of the private sector. It is only in comparing federal pay to private sector salaries that significant differences arise. We explain how those differences might come about and what they imply for federal pay levels.

Comments by Filler
I believe Condrey, Facer and Llorens are correct in suggesting that aspects of the existing federal pay system provide a good foundation for a modernized compensation model. Moreover, I agree that market survey data should be a factor in determining how pay might be set, but the internal alignment piece with meaningful stakeholder input through employee representatives is critical. One need only review the history of the National Security Personnel System within the Department of Defense (DoD) to appreciate the shortcomings of an overly legislated approach. With the National Security Personnel System, valuable recommendations of the workforce were ignored, when DoD implemented significant changes to its compensation system, that have since been scuttled after wasting millions of taxpayer dollars.

Is a single federal pay system the answer? I am not convinced that a goal of pay reform should be one size fits all. Several other agencies have for many years operated under pay demonstration projects with varying degrees of success. And, a number of the federal financial regulatory agencies, which have traditionally set pay at levels higher than the GS, may be adversely affected with a single government-wide approach.

In conclusion, the process for modernizing the pay system is important to achieving a meaningful end product, and how it can be used to drive individual and organizational performance.
The Challenge of Determining Fair Pay for Government Employees

Andrew G. Biggs, Resident Scholar, American Enterprise Institute

Jason Richwine, Senior Policy Analyst, Heritage Foundation

The public sector pay controversy has touched every level of government over the past few years, playing out in political campaigns, newspaper headlines and Internet blogs. But even as the political debate over reform continues, we believe that the purely empirical issue regarding the relative generosity of public sector compensation has been settled: On average, public employees receive higher combined wages and benefits than they would receive in the private sector.

The average, of course, does not apply to all workers or to all jobs. Wages and benefits differ at the federal, state and local levels, between different cities and states and between different types of jobs and employees. The challenge for policy makers is not to simply reduce total public sector compensation but to cut back in ways that ensure fair market compensation for all public employees rather than just for the average employee.

Careful reform will not be easy—and developing the perfect system is not realistic—but even minor steps toward a more rational compensation system can help balance government budgets.

When comparing wages among different types of workers—for example, testing for discrimination based on race or gender, or looking for a pay premium for union members—most labor economists rely on what is called the “human capital model.” This approach is based on evidence that the main drivers of pay differences among workers are differences in their human capital—that is, their education, work experience and other traits related to productivity. Specific work tasks, unless associated with different levels of employee skill, are less important drivers of pay.

Using regression analysis, economists can analyze the effect on wages of being employed by the government while controlling for human capital differences between the public and private sector workforces. These analyses generally show that state and local government workers receive wages slightly below those of similar private sector workers, while federal employees receive slightly higher wages.

Other economists have approached the problem by analyzing how wages differ between public and private jobs that require the same levels of skill. In a recent academic study, two BLS economists compared salaries in state and local government to private sector positions demanding the same job skills. State government employees receive salaries 2.3% below those for similar private sector jobs, while local government employees were paid 9.2% more than private jobs demanding similar skills. The study did not attempt to analyze federal employee wages, as the BLS data set does not grade the skill requirements of federal jobs.

Whether the relevant comparison is worker-to-worker or job-to-job, the suggestion that public sector workers receive vastly lower salaries than they would receive in the private sector is not supported by the most rigorous research.

The clear difference maker in public–private comparisons is fringe benefits, particularly retirement packages. Most government employees continue to participate in traditional “defined benefit” pensions, which can be several times more generous than the defined contribution 401(k) plans common in the private sector. For example, an Illinois school teacher who retired in 2010 after 30 to 34 years of service would collect a pension of $60,756 a year, a benefit that is guaranteed against market risk and also exceeds the income of 95% of retirees in Illinois. To match that, a private sector employee with the same salary would need to contribute roughly 45% of his or her earnings to his or her 401(k).

On top of pensions, most federal, state and local employees continue to be eligible for retiree health coverage, which can be worth thousands of dollars per year. In California, for instance, the cost of accruing retiree health benefits is equivalent to over 10% of wages. Public employees have protested recent reductions in the generosity of retiree health care, but most private sector workers receive no coverage at all.

Generous fringe benefits can push public sector compensation well ahead of private sector pay.

A common rejoinder to this empirical argument is that instead of reducing benefits for government workers, benefits in the private sector should be increased. Unfortunately, this is not a viable option for private sector employers.

In a competitive labor market, employers cannot pay workers significantly more than they produce without risking bankruptcy. Employers also cannot pay workers significantly less than they produce without losing employees to rival firms. Without changes in worker productivity, total employee compensation—meaning salaries, benefits, taxes paid on workers’ behalf and so forth—is not very flexible.

While legislation could raise private sector benefits by fiat—for example, by mandating health or pension coverage—private employers would need to offset the added cost by lowering salaries, leaving the public sector compensation advantage unchanged. Mandating higher private sector benefits is no solution to public–private pay disparities.

In contrast to the private sector, governments are not limited to paying their workers according to their
productivity. The public sector is restricted not by profit and loss but only by voter-imposed constraints on taxing and borrowing. Given the ability of the public sector workforce to influence policy—directly through collective bargaining and indirectly through political organizing—it should not be surprising when government workers receive a compensation premium.

Restricting collective bargaining and union influence will help change the political dynamics that lead to excessive average compensation and rigid salary structures. Union membership and dues should be made optional, not required. Direct reforms to benefits, such as raising retirement ages to match private sector norms and shifting public employees to 401(k)-style plans also would help restore pay parity.

Comment by Filler

For many years, collective bargaining had a positive impact on wages and benefits in the public and private sectors, until ongoing depressed economic conditions resulted in changes to pay, pension and health care. Even compensation increases of the federal government, as set through laws passed by Congress and signed by the President, have been frozen. And one should not overlook the fact that many state or local public employers across the United States retain the ultimate authority to resolve public sector bargaining impasses and make necessary adjustments to the terms and conditions of employment.

More recently, an ever-increasing amount of scrutiny has focused on the retirement incomes of public employees. The trend to convert those covered by defined benefits retirement plans into 401(k) arrangements—prone to a helter-skelter investment strategy and the shifting winds of Wall Street—will result in more workers not having adequate financial resources during their postemployment period. Unlike the lavish golden parachutes given to many private executives, the vast majority of public employees (like their private sector counterparts) will need to supplement their monthly retirement checks. Regrettably, government critics would like to see more public employees placed into the Titanic’s lifeboats with stagnant wages and underperforming pensions.

As this debate continues, one should not confuse parity with poverty. Effective labor organizations, like public sector management associations, have an obligation to advocate for those they represent while taking into account the public interest. Unions can and will take necessary strategic steps to adapt to the new realities of constrained public budgets, as they prepare to address the critical issues of pay and benefits.

Comment by Condrey, Facer and Llorens

In contrast to Filler’s article, Biggs and Richwine address the larger issue of public sector pay comparability and their contribution is premised on the belief that existing public compensation systems should be more closely aligned with private sector norms. The authors touch on one of the long-standing controversies in estimating public–private pay comparability—whether to compare the wages of individuals (i.e., the human capital approach) or occupations between the two sectors—and point out that estimates based on the human capital approach have consistently shown evidence of wage premiums for federal employees. Although suitable for aggregate assessments of wage rates, the human capital approach is generally not considered an effective method of determining appropriate wage rates for disaggregated occupational levels. In practice, salary surveys in the public and private sector are most commonly based on occupational comparisons by level of work, and this is the method currently utilized by BLS economists in estimating federal pay comparability. Contrary to conclusions drawn from aggregated, human capital–based assessments, occupation-based wage comparisons have shown that federal employees tend to be underpaid at higher grade levels and overpaid at lower, more nonprofessional grade levels. While we do not fully agree the authors that private sector compensation practices should be adopted wholesale throughout the public sector, we do agree with their assertion that policy makers should focus their efforts on reforms “that ensure fair market compensation for all public employees rather than just the average.” As presently structured, the federal GS compensation system maintains a narrow focus on the “average” federal employee by mandating an across-the-board approach to federal GS pay adjustments. In reality, federal pay comparability differs substantially by grade level, and it is for this reason that one of our primary suggestions is to reform the existing compensation policy to allow for pay adjustments by grade level. This flexibility would provide immediate benefits by limiting pay increases for employees with existing pay premiums and bringing the pay for higher graded employees more in line with the private sector.

Reform in the Right Way: Compensation in the Public Sector

Michael Filler, Director of the Public Services Division, International Brotherhood of Teamsters

The ongoing economic challenges the United States has faced and the mounting political campaigns associated with the fall 2012 elections create another
opportunity to critique the government and those who carry out many critical functions on behalf of the public. This has led to a renewed focus on the salary and benefits received by government workers, as well as debates about taxes, budgets and deficits.

From a policy perspective, the discussion should seek to identify the right public compensation system, not one that merely attempts to compare public and private sector jobs as the model for determining the proper pay levels. A comparative compensation approach pits one group against another and results in envy, suspicion and distrust. It divides communities, states and regions within the country and undermines the concept of public service.

Some pay reform proponents have called for doing away with the federal government’s general pay schedule as a system that is tantamount to an entitlement. What is often overlooked in those debates is that a compensation model with specified progression increases is a way of rewarding employees who perform well, and it provides a level of monetary predictability for those who qualify. Such a pay arrangement is also an important component that reinforces the economic strength of communities, where employment stability and remuneration are maintained. One need only recall the period following World War II, when the standard of living was raised and the middle class was created.

Are pay flexibilities the answer? At the federal government level, “excepted service” systems have to do with hiring flexibilities and related exemptions from certain civil service rules, not ones that govern general pay and benefits. Typically, a law must be passed enabling an agency, department or bureau to have the authority to establish an alternative pay arrangement. Through demonstration projects enacted into law over many years, the federal government has experimented in different ways to compensate employees.

Certain elected officials and pundits seek to place the blame for the “public sector pay problem” on labor unions. Yet, when laws are enacted that set pay levels or convey retirement benefits, democratically elected bargaining representatives must establish meaningful political and legislative programs to effectively advocate for their members.

How much of the so-called “public sector pay problem” is real, and how much is manufactured to energize a particular candidate’s or political party’s base?

Do governmental agencies and departments need to hire “reward strategists” or be focused on selecting and promoting good managers who can properly evaluate and reward high performance?

Is changing the pay system necessary because of increased costs, or is it viewed as a way to improve the government’s overall performance? In other words, is it management, budget or both?

A basic foundation for change must be a credible performance management system; without one, the goal of a modernized compensation system cannot be realized. In the public sector, as with nonprofit entities, mission takes precedence over financial rewards that drive the private sector. Employees in the public sector tend to be motivated by addressing the public’s needs rather than pursuing personal monetary gain. In government, mission attainment is sometimes difficult to quantify and/or it may take many years to realize a particular outcome, whereas, in the private sector, growth in revenues or earnings is much more apparent.

Unlike the private sector, which is, in large part, subject to market and consumer demands, the public sector’s dynamic environment is affected by laws, legislators, administrators, government executives and the public. And, if a governmental department or agency performs well, its funding level is not increased in the following fiscal year to pay people more money for a job well done.

So the private sector performance pay model does not easily translate into a workable public sector system given the aforementioned distinctions. And even the private sector model is not without fault.

A July 2012 report issued by WorldatWork and Mercer (2012 Metrics & Analytics: Patterns of Use and Value) concludes that pay decisions of many organizations are too focused on external comparisons and not enough is being done to measure and assess the workforce and organizational reward practices. Based on a survey of compensation professionals, benchmarking and reporting take up an inordinate amount of time, while projections, simulations and predictive modeling are used less frequently. The report advances the proposition that data and analytics can play an important role in pay decisions and result in better, more fact-based decisions rather than relying on labor market analyses.

The other takeaway from the WorldatWork/Mercer report is that in a true total rewards environment, variables such as education levels, competencies and training/development investments should be taken into consideration. By only focusing on the “motivational” aspect of rewards and ignoring the “broader effect” rewards have on securing the right workforce, one misses ways to drive talent development and organizational performance.

More sophisticated analytics can provide organizations with greater insights into the effectiveness of their rewards strategy. To implement such a system, as the WorldatWork/Mercer report suggests, requires a total rewards philosophy that is predicated on a culture of measurement.

What do employees value and how do those factors play into career choices and organizational performance? An effective total rewards model looks at more than
merely market competitiveness and pay-for-performance sensitivity.

Rather than directing a legislative solution for a specific type of pay system, it would be best to achieve public sector compensation reform with very general statutory authority. The framework, however, should mandate the participation of labor as an equal partner, using a collaborative, consensus-based decision-making model, to ensure appropriate employee input.

The current Administration has created an environment where productive outcomes can be realized. The progress advanced under “New Beginnings” at the DoD demonstrates that DoD Unions and their management counterparts can work closely together to redesign a large and cumbersome department-wide personnel and pay system. And the comprehensive performance management initiative called GEAR (Goals, Engagement, Accountability and Results), which was the result of the combined efforts of the National Council on Federal Labor–Management Relations and the Chief Human Capital Officers Council, is evidence that effective reform can be achieved without the need for overreaching legislation.

Compensation reform can be the next logical step, once pilot GEAR projects being conducted at multiple federal agencies are assessed. Incorporating modernized pay systems within functioning performance cultures will allow for making the right decisions on pay that motivate individuals and drive organizational success.

Comment by Condrey, Facer and Llorens

To begin, Filler’s article is premised on the belief that public private pay comparisons should not be the critical focus of federal pay reform efforts. Instead, he holds that “a basic foundation for change must be a credible performance management system” and that future efforts should seek to build a more modern compensation system through reformed performance management systems developed with labor/management cooperation. While we agree with Filler that an effective performance management system is a key component of a fully functioning, modern compensation system, we do not believe that the federal government’s existing performance management structure is substantially lacking or that it is one of the most pressing concerns for reform. While there will always be a need to adapt performance management systems to the changing duties of federal occupations, a more pressing management challenge for the federal government is the development of a compensation system that rewards performance and allows the federal managers to compete in the market for talented candidates. Furthermore, while there may be a substantial percentage of federal employees not primarily motivated by monetary gain, as Filler points out, conventional wisdom and practical experience suggest that most employees do, in fact, want to be fairly and equitably compensated for their contributions. As such, we believe that the most pressing concern for federal employers should relate to ensuring that the federal compensation system corrects existing inequities in the GS salary system.

Comment by Biggs and Richwine

Filler writes that policy should “identify the right public compensation system, not one that attempts to compare public and private sector jobs as the model for determining the proper pay levels.” What is less clear is why? Common sense and economic theory indicate that equal total compensation between public and private sector workers of similar skills is both fair and cost-efficient. To the degree there are exceptions to this rule—for instance, compensating wage differentials based on differences in job security, work conditions or flexibility of work hours—they would tend to recommend lower pay for government employees, as public sector jobs tend to have superior nonpecuniary benefits. Filler argues that “a comparative compensation approach pits one group against another and results in envy, suspicion and distrust.” Only if one group believes it is being treated unfairly relative to others. If we abandon the goal of pay comparability, we also abandon any need to explain to the public why, for instance, public employees at the federal, state and local level should have retirement packages that are several multiples more generous than those received by the taxpayers who support them.