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A Review of the Department of Defense's National Security Personnel System



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November 2008



Preface

The National Defense Authorization Act (NDAA) for Fiscal Year 2004 granted the Department of Defense (DoD) the authority to develop the National Security Personnel System (NSPS). The department had sought a new personnel system that, in its view, would provide greater flexibility and timeliness to better enable it to meet its national security mission. To that end, NSPS incorporates some changes in human resources management intended to speed up the hiring process and strengthen employees' performance, for example.

The Congressional Budget Office (CBO) prepared this report, which evaluates NSPS to date, at the request of the Chairman of the Subcommittee on Readiness of the House Committee on Armed Services. The main objective of the report is to examine the extent to which NSPS has achieved, or has the prospect of achieving, the most salient goals stated in the 2004 NDAA. In examining key changes in NSPS, this report drew on the experience of past personnel experiments within DoD and the rest of the federal government.

Adebayo Adedeji of CBO's National Security Division performed the analysis under the supervision of Matthew S. Goldberg and J. Michael Gilmore. David Brauer, Mark Hadley, Douglas Hamilton (formerly of CBO), Stephanie Ruiz, and Ralph Smith (formerly of CBO) provided helpful comments on a draft of the analysis. Susan Gates of the RAND Corporation reviewed the entire report. (The assistance of an external reviewer implies no responsibility for the final product, which rests solely with CBO). Victoria Liu (formerly of CBO) provided valuable research assistance, and Carol Frost helped with data processing.

Christine Bogusz edited the manuscript, and Sherry Snyder proofread it. Cindy Cleveland produced drafts of the manuscript and prepared the tables. Maureen Costantino prepared the report for publication and designed the cover. Lenny Skutnik printed the initial copies, Linda Schimmel handled the print distribution, and Simone Thomas prepared the electronic version for CBO's Web site (www.cbo.gov).

Robert A. Sunshine
Acting Director

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Summary and Introduction

In 2003, the Congress authorized the Secretary of Defense to establish a human resources management system, the National Security Personnel System (NSPS), within the Department of Defense (DoD).¹ That system was authorized at the request of DoD, which had complained of inflexibilities in the traditional federal personnel system.² The department claimed that with its constraining rules in hiring, assigning, compensating, and rewarding employees, the traditional system was cumbersome even during normal peacetime operations; during wartime, when the system faced additional stresses, it was more problematic. According to senior DoD officials, civilian employees—an integral resource in the global war on terrorism—would be more valuable if the human resources system were more “modern, flexible, and agile.”³

Officials at DoD often use the General Schedule (GS) system—which governs most white-collar federal employees and covers more nonpostal federal employees than other personnel systems, such as the Federal Wage System—to highlight what they perceive as shortcomings

of the federal personnel system.⁴ Some of DoD’s concerns with the GS system are also shared by other government officials and observers who perceive that system as defining jobs too narrowly and prescribing too many procedures for filling those jobs. They also assert that compensation levels under the GS system do not keep up with those in the private sector, limiting the ability of the federal government to compete for the best workers.⁵ Some observers have argued that pay levels and pay raises do not sufficiently distinguish the better government workers from their lower-performing counterparts, discouraging the former group and making them more difficult to retain. Finally, some view the government’s labor relations process as cumbersome and slow to resolve disputes.

The basic features of the current GS system were established by the Classification Act of 1949. The Civil Service Reform Act of 1978 granted the Office of Personnel Management (OPM) the authority to conduct personnel demonstration projects to test new personnel management and pay systems. Federal agencies could obtain per-

1. Sec. 1101 of the National Defense Authorization Act for Fiscal Year 2004 (2004 NDAA, Public Law 108-136; see 5 U.S.C. 9901 et seq., 117 Stat. 1621). That act also established a new compensation system for the Senior Executive Service (SES) throughout the federal government (section 1125 of Public Law 108-136). The legislation broadened the pay bands for SES employees and encouraged a management system that makes more meaningful distinctions among performance levels (see Appendix A).
2. Statement of David S. C. Chu, Under Secretary of Defense for Personnel and Readiness, before the Subcommittee on Oversight of Government Management, the Federal Workforce, and the District of Columbia of the Senate Committee on Governmental Affairs, *An Overlooked Asset: The Defense Civilian Workforce* (May 12, 2003).
3. Statement of David S. C. Chu, Under Secretary of Defense for Personnel and Readiness, before the Subcommittee on Personnel of the Senate Committee on Armed Services, *Active and Reserve Military and Civilian Personnel Programs* (April 5, 2005).

4. The Congressional Budget Office (CBO) focuses on the GS system when making comparisons between the traditional federal personnel system and NSPS partly for that reason (most of DoD’s employees that will be under NSPS would be converted from the GS system). Another reason CBO focuses on the GS system is that the Congress, in the National Defense Authorization Act for Fiscal Year 2008 (Public Law 110-181), directed that DoD exclude its “prevailing rate” or wage-grade employees from NSPS. DoD’s wage-grade employees are typically blue-collar workers in a recognized trade, craft, or manual labor occupation. They include blue-collar workers in DoD entities that do not receive direct appropriations (the so-called nonappropriated fund entities, such as DoD’s retail stores or “exchanges”).
5. In 2002, the Office of Personnel Management issued a white paper that criticized the GS system’s compensation policies as inadequate for the personnel management challenges the federal government faces. See Office of Personnel Management, *A Fresh Start for Federal Pay: The Case for Modernization* (April 2002).

mission from OPM to waive existing personnel laws (as codified in title 5 of the U.S. Code) and implement new rules on a test basis for a specified period. In 1980, for example, OPM gave DoD permission to implement a demonstration project at its laboratories in the Naval Air Warfare Centers in China Lake, California, and other locations (collectively referred to as the “China Lake” demonstration project).⁶ More demonstration projects and alternative personnel systems were implemented within DoD and other federal agencies in the ensuing years. Those personnel systems represent movement away from the GS system toward approaches that reduce the number of stages in the hiring process, use a smaller number of broader job definitions, and make all pay increases contingent on employees’ satisfactory performance. Today, DoD and the federal government as a whole have more than 25 years of experience with alternative personnel systems.⁷

The Department of Defense’s Objectives and the Design of the National Security Personnel System

Implementing NSPS will bring new personnel policies similar to those in demonstration projects and alternative personnel systems to the rest of DoD’s civilian employees. According to DoD officials and the legislation authorizing the creation of NSPS, the goals of the system are these:

- Increase management flexibility in hiring and compensating employees,
- Increase management flexibility with regard to adverse actions and labor relations issues, and
- Motivate effective work.⁸

6. In 1994, the Congress, via the National Defense Authorization Act for Fiscal Year 1995 (Public Law 103-337), indefinitely extended the China Lake demonstration project, effectively making it an alternative personnel system.

7. In addition to the 10,000 employees in the China Lake alternative personnel system, about 46,000 DoD employees (7 percent of total DoD civilian employees) are in demonstration projects that are either ongoing or have been made into a permanent alternative personnel system. Including those DoD demonstration projects, roughly 70,000 federal civilian employees (4 percent of total federal non-Postal Service employees) are in ongoing or permanent demonstration projects.

The Department of Defense used the authority it was granted in the National Defense Authorization Act for Fiscal Year 2004 (Public Law 108-136) to design the system. The major elements of that system are similar to those of the GS system:

- Classification (rules for defining and grouping jobs on the basis of factors like level of difficulty and responsibility);
- Staffing and workforce shaping (procedures for filling jobs and laying off workers, if necessary);
- Performance management (rules for evaluating and rewarding employees’ performance); and
- Adverse actions and labor relations (policies for addressing adverse actions—such as suspension, termination, and reduction in grade or pay—and collective bargaining, which is negotiation between an employer and a labor union, usually on wages, hours, and working conditions).

In specific attempts to achieve its three goals, DoD used the implementation of NSPS to launch certain changes to the personnel system (see Table 1-1).

To address DoD’s goal of increased flexibility in hiring and compensating employees, NSPS groups jobs into broader pay bands than does the GS system. One of the rationales of pay banding in NSPS is to allow DoD’s managers greater room to make initial salary offers and to move employees between jobs with varying levels of responsibilities. Furthermore, in an attempt to accelerate the hiring process, NSPS gives DoD the power to, in some instances, hire employees directly (not through OPM).

To increase management flexibility with regard to adverse actions and labor relations issues, NSPS, among other things, sought to expand “management rights” (actions that management can take without collective bargaining)

8. Those goals represent CBO’s synopsis of information from multiple DoD sources such as testimonies (for example, statement of David S. C. Chu, *An Overlooked Asset*) and policy documents (Department of Defense and Office of Personnel Management, Department of Defense Human Resources Management and Labor Relations Systems: Final Rule, 70 Fed. Reg. 66116 (2005)).

Table 1-1.

Selected Features of the National Security Personnel System and the Goals They Are Intended to Address

DoD's Goal	Personnel System Changes in NSPS
Increase Management Flexibility in Hiring and Compensating Employees	Place jobs in broader pay bands, which better accommodate higher starting salaries. Relax the rules for filling positions from outside the government—by allowing the targeting of a local commuting area, for example. Grant authority to hire for positions with severe shortages or critical skills within DoD (instead of OPM).
Increase Management Flexibility with Regard to Adverse Actions and Labor Relations Issues ^a	Shorten the notice period for adverse actions and strengthen the role of DoD in appeals of adverse actions. Add procedures in making work assignments and deployments to the list of management rights excluded from bargaining. Create the National Security Labor Relations Board to address labor relations issues DoD deems most important to carrying out its mission.
Motivate Effective Work	Link individual performance to organizational missions and objectives. Revise the performance management system so that employees with an “unacceptable” performance rating receive no increases in pay of any kind (neither performance-based nor cost-of-living increases). Create pay bands with broader salary ranges to provide greater room for compensating high-performing employees. Allow employees, within certain limits, to be assigned to a higher-paying job within a pay band without official promotion action. Emphasize performance rather than time in federal employment in making layoff decisions.

Source: Congressional Budget Office.

Note: DoD = Department of Defense; NSPS = National Security Personnel System; OPM = Office of Personnel Management.

- a. These elements of NSPS will not be implemented, as directed by the Congress in the National Defense Authorization Act for Fiscal Year 2008.

and shorten the amount of time employees have to appeal adverse personnel actions. According to DoD, the standard civil service processes take too long, encourage an adversarial relationship between employees and management, and do not adequately accommodate DoD's need to make decisions quickly (as required by its national security mission). The Congress, via the National Defense Authorization Act for Fiscal Year 2008 (Public Law 110-181), directed DoD to stop implementing the NSPS elements relating to adverse actions, appeals, labor relations, and workforce shaping and instead revert to the policies that already exist under traditional civil service law. DoD has revised the NSPS regulations to conform with that legislation.⁹ Although that action by the Congress effectively nullified the adverse actions, appeals, and labor relations elements of NSPS, this study nonetheless examines the changes DoD attempted to make, the rationale for them, and the issues involved in the ensuing debate. (For more details, see Chapter 4.)

To motivate effective work, NSPS includes a performance management system that ties all pay raises to appraisals of employees' work (unlike the GS system, in which a substantial portion of annual pay increases is provided to all employees regardless of performance). NSPS also requires managers to link individual performance standards to the missions or objectives of their organization. The pay bands in the system have a broad salary range so as to give managers greater room to compensate high-performing employees.

Implementation Plan for the National Security Personnel System

In 2006, DoD published details of its plan to implement NSPS. The new system would be implemented using a phased approach, converting employees into the system in "spirals." DoD had always intended to delay the con-

version of its roughly 145,000 blue-collar ("wage grade") employees until late in the process; ultimately, Public Law 110-181 excluded those employees from NSPS altogether.¹⁰ That legislation also exempted employees in certain demonstration projects at DoD laboratories from converting to NSPS until October 1, 2011. In addition, DoD has decided to exclude certain groups of white-collar employees from the new system.¹¹ According to DoD, those employees and employees in the exempted DoD laboratories total 64,000. Taking those exclusions into account and given that DoD employs a total of roughly 681,000 civilians, about 472,000 white-collar employees are eligible for conversion to NSPS.¹²

In April 2006, DoD converted the initial part of the first spiral, Spiral 1.1, consisting of about 11,100 nonunion white-collar employees. The next group, Spiral 1.2, covering 66,600 nonunion white-collar employees, was converted to NSPS between October 2006 and February 2007 (see Figure 1-1). In March 2007, DoD announced the conversion of the third group, Spiral 1.3, covering about 35,400 nonunion white-collar employees, which happened in March and April 2007.

In October 2007, DoD announced plans for the next round of conversions, Spiral 2, which would include an additional 75,000 nonunion white-collar employees.¹³ According to those plans, employees in Spiral 2 would be converted by December 2008. By that date, a total of about 188,000 nonunion white-collar employees would have been converted to the new system. (See Appendix B for a list of the DoD organizations in each of the conversion spirals; those organizations have headquarters in

9. The revised NSPS regulations were initially published in the *Federal Register* in May 2008 (see National Security Personnel System: Proposed Rule, 73 Fed. Reg. 29882 (2008), codified at 5 C.F.R. 9901). That publication also included adjustments and clarifications to existing NSPS regulations. DoD and OPM published revised final regulations in September 2008 (see National Security Personnel System: Final Rule, 73 Fed. Reg. 56344 (2008), codified at 5 C.F.R. 9901). Also, it was reported in November 2008 that DoD would not seek to transfer its union employees to NSPS. See Stephen Losey, "NSPS Won't Include Union Employees," *Federal Times* (November 2, 2008).

10. Public Law 110-181, sec. 1106. In addition, that legislation limited the total number of employees who could be converted to the new system in any single year to at most 100,000.

11. Those groups include employees in intelligence agencies, educators in overseas locations, faculty, employees in certain senior positions, and other experts and consultants.

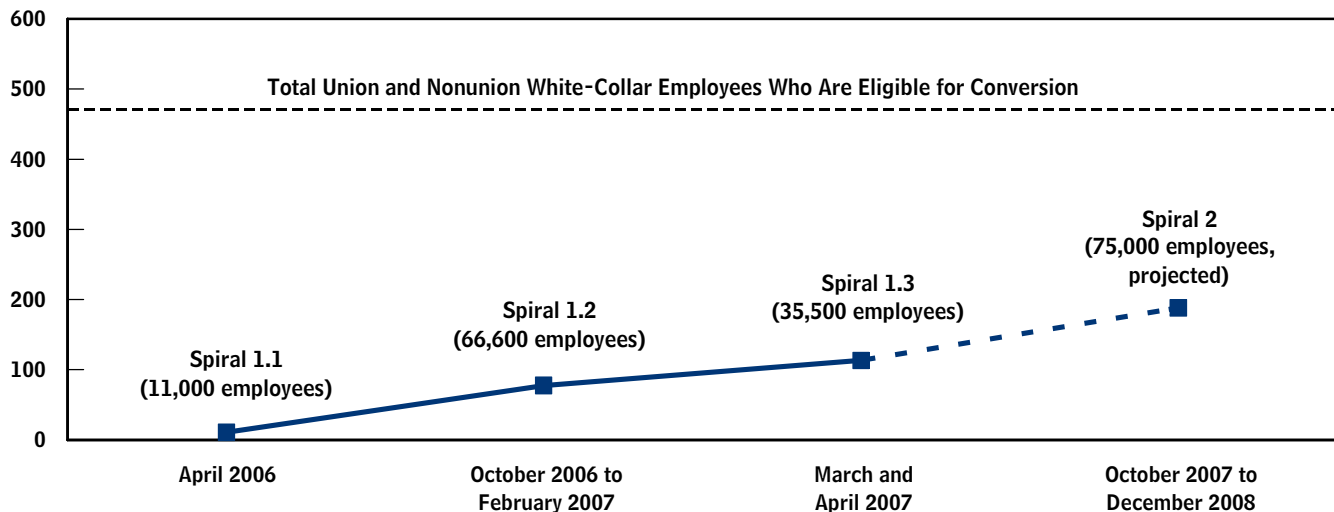
12. The total number of civilian employees (681,000) minus blue-collar workers (145,000) minus other exempted employees (64,000) equals the number of eligible employees (472,000).

13. The number of employees identified for conversion in each spiral may differ slightly from the number observed after the completion of each spiral because of changes in the status of some employees and positions. For instance, some NSPS employees may move to a non-NSPS position, while some previously filled NSPS positions may later be unfilled or eliminated.

Figure 1-1.

Timeline for Converting Nonunion, White-Collar Department of Defense Employees to the National Security Personnel System

(Number of employees, in thousands)



Source: Congressional Budget Office based on data from Department of Defense, National Security Personnel System (NSPS) Program Executive Office.

Note: The number of employees identified for conversion in each spiral may differ slightly from the number observed after the completion of each spiral because of changes in the status of some employees and positions that occur throughout the year. For instance, some NSPS employees may move to a non-NSPS position, while some previously filled NSPS positions may later be unfilled or eliminated.

various locations in the United States and overseas.) The Department of Defense has not yet released its conversion plan beyond Spiral 2. After those conversions have been completed, about 284,000 employees will await conversion. According to DoD, 252,000 of those remaining employees are union members, while 32,000 are not. Thus, most of DoD's eligible nonunion white-collar employees have been converted to the system.

Differences Between the National Security Personnel System and the General Schedule System

NSPS differs from the GS system in several ways. One major difference is that the classification structure in NSPS uses fewer categories than the GS system. The 23 occupational groups and 15 pay grades in the GS system are reduced to four "career groups" and up to four broader pay bands in NSPS. While not an end in itself, pay banding is intended to improve DoD's flexibility in compensating its employees.

Pay banding has some potential advantages. The salary ranges in the pay bands provide more latitude to accommodate a wider variation in individual pay related to differences in skill and performance. For instance, an employee with superior performance could be rewarded with higher pay without necessarily requiring a promotion or a change in jobs. In that way, talented professionals who do not wish to be managers can remain in their jobs and be compensated at the highest level in their pay band. Another possible advantage of pay banding is that the wider salary range provides greater latitude for a DoD organization to adjust to local job market conditions by offering new employees higher starting salaries without placing them in higher-graded jobs. If realized, those potential benefits should help DoD attract well-qualified job candidates and retain employees who perform well. As will be discussed later in this chapter and in Chapter 6, DoD could monitor hiring and retention trends to find out whether those outcomes are being realized.

Pay banding has some potential disadvantages, too, although they have not been directly observed in NSPS at this point. One possible disadvantage is that greater effort may be needed to monitor and control payroll costs, which could increase considerably over time if employees advance quickly through the larger salary range in a pay band.¹⁴ One federal agency—the Office of Federal Housing Enterprise Oversight—cited a rapid increase in payroll costs as a reason for moving away from pay banding.¹⁵

That so-called salary creep is not unavoidable, however. Previous research findings on payroll cost increases in personnel demonstration projects with pay banding are mixed—some agencies experienced faster payroll growth compared with a comparison group of GS employees, while others experienced slower growth.¹⁶ Rewarding performance through a mix of lump-sum bonus awards and salary increases, as DoD currently does, could help control payroll cost growth. Another practice that can constrain cost growth is to allocate a fixed percentage of the current payroll to the pool of money available to fund annual pay increases. DoD follows that practice as well, with funding for performance-based pay increases under NSPS tied to a portion of the annual governmentwide pay increase.¹⁷

14. Some observers would argue that even some underperforming employees could experience considerable salary growth over time. For instance, when an employee underperforms in one or two years and later performs well, supervisors might be inclined to increase that employee's salary to the level of his or her peers who have consistently performed well.

15. Karen Rutzick, "Agency Decides Pay Banding Is Not the Answer," *Government Executive* (September 30, 2005).

Founded in 1993, OFHEO is a small federal agency within the Department of Housing and Urban Development. It oversees the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac). OFHEO is now part of the Federal Housing Finance Agency, which was created on July 30, 2008, when President George W. Bush signed the Housing and Economic Recovery Act into law. The law created a single regulator to oversee Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. In addition, the law combined the staffs of OFHEO, the Federal Housing Finance Board, and the government-sponsored enterprise mission office at the Department of Housing and Urban Development.

16. General Accounting Office, *Human Capital: Implementing Pay for Performance at Selected Personnel Demonstration Projects*, GAO-04-83 (January 2004).

A further potential disadvantage of broad pay bands is that employees who have similar types of jobs and who perform at similar levels, but in different work units, might see their salaries diverge over time if their work units have different procedures or standards for determining pay raises. That potential outcome could lead to equal-pay-for-equal-work concerns in the workforce.

A second major way in which the NSPS and GS systems differ is in how they evaluate and reward performance. Under the GS system, there is less uniformity across agencies in their performance appraisals because the method for rating employees' performance can range from summary "pass/fail" to multiple-level rating scales. Furthermore, agencies are not required to link individual performance standards to their organizational missions or objectives. In contrast, NSPS imposes a standard five-level rating scale (unacceptable, 1; fair, 2; valued performer, 3; exceeds expectations, 4; and role model, 5), and an employee's rating on that scale must be linked to the agency's goals and objectives.

Furthermore, in the GS system, employees receive at least the annual cost-of-living adjustment that is awarded to practically all employees regardless of their performance. In NSPS, an employee who is rated as not performing up to minimum standards for his or her position (level 1) does not receive either a performance-based pay raise or the annual adjustment.

That greater emphasis on performance in NSPS increases the importance of the performance management process to the system's success. NSPS provides standardized benchmark "performance indicators" (detailed descriptions of tasks at various levels of performance) as well as lists of "contributing factors" (descriptions of behaviors, such as critical thinking, that are needed to accomplish tasks). Supervisors use those benchmarks to evaluate how well employees accomplish their work and to assign performance ratings. As part of that process, supervisors must make judgments on where employees stand relative to the benchmarks. Performance appraisal processes that

17. According to section 1106 of the National Defense Authorization Act for Fiscal Year 2008 and NSPS documents, 60 percent of the annual governmentwide pay increase is used to adjust salaries in pay bands for all employees with performance ratings of "fair" or better. The remaining 40 percent is used for performance-based increases to further differentiate gains in base pay for employees at different performance levels.

require supervisors to make similar judgments are common in the private sector. For such processes to be most effective, research indicates that openness, trust, and good communications skills on the part of both employees and supervisors are essential.

Has the National Security Personnel System Achieved Its Goals to Date?

At this preliminary stage, it is difficult to evaluate how well NSPS has met its goals. Implementation of the new system is not complete, and sufficient time has not yet elapsed since the first employees were converted to accumulate an adequate amount of useful data. As a result, the Congressional Budget Office limits its assessment to the particular NSPS goals for which some data are available and then provides examples of the type of information that DoD would need to collect to enable a more complete evaluation. CBO also discusses the overall cost of implementing NSPS. Even though a review of the experience of private-sector employers with personnel systems designed to address similar workforce challenges might provide useful insights for DoD, CBO did not perform such an analysis because the necessary data were unavailable.

Goal No. 1: Increase Management Flexibility in Hiring and Compensating Employees

The National Security Personnel System aims to give DoD greater flexibility in hiring and compensating its employees. For instance, unlike the previous system in which OPM oversaw the hiring process, NSPS has provided the Secretary of Defense with new hiring authorities in certain circumstances, such as when a severe shortage or critical need can be documented. In addition, NSPS adopts simplified rules for defining jobs and places those jobs in broader pay bands, which allow greater latitude in setting pay for individual employees on the basis of their particular qualifications and specific market conditions. Pay bands also enable DoD to assign employees to a wider range of job opportunities than was previously possible.

The new rules that are intended to streamline the employment process should reduce the time it takes to hire employees. Furthermore, the pay-setting advantages of pay bands should make it easier to retain workers, par-

ticularly the more highly qualified ones with strong employment prospects in the private sector. Because NSPS is newly implemented, there is little evidence that CBO could draw on to assess the achievement of those outcomes. In order to provide such an assessment, CBO would need data from DoD on timeliness of hiring, retention rates, and qualification levels. For example, to monitor the timeliness of the hiring process, DoD could collect information on the number of days that elapse from the time a human resources office is notified of a vacancy to the date an offer is made to a job candidate (the so-called time to hire). DoD could also monitor retention rates, which may improve if the pay banding flexibilities result in more competitive salaries.¹⁸ The ability to offer higher starting salaries should allow DoD to attract better-qualified applicants. Data on the qualification levels (education and experience) of new hires before and after the implementation of NSPS would help DoD evaluate that outcome.

Whether employees perceive NSPS as an improvement over the GS system could affect their support for the new system. To explore that issue, CBO obtained and analyzed data from surveys of DoD's civilian employees and supervisors on their attitudes toward NSPS. The results of CBO's analysis suggest that DoD's employees are not yet convinced that NSPS's desired effects on DoD's personnel processes have been or will be achieved. In the five surveys conducted between October 2004 and May 2007, about 30 percent of DoD employees who had not been converted to NSPS agreed or strongly agreed that NSPS *will* improve selected personnel processes, such as those for hiring new employees. In May 2007, 23 percent of employees converted to NSPS and their supervisors thought that NSPS *had* improved those personnel processes. As of the same date, about 15 percent of those employees and their supervisors thought that NSPS is,

18. Pay is not the sole factor that affects the retention of employees. According to a survey of U.S. workers by the Society for Human Resource Management, after pay, other job characteristics that employees most frequently cite as "very important" to job satisfaction are, in descending order, benefits, job security, flexibility to balance life and work issues, and communication between employees and senior management. See Society for Human Resource Management, *2007 Job Satisfaction Survey Report* (June 2007).

overall, better or much better than the previous personnel system.¹⁹

Because the employees converted to NSPS are not a random sample of all DoD employees, the survey findings for the sampled group may not extrapolate to the rest of the employees. However, those findings could portend unfavorable views about personnel processes under NSPS. It remains to be seen whether employees' opinions of NSPS will improve as more are converted and as the system matures.

Goal No. 2: Increase Management Flexibility with Regard to Adverse Actions and Labor Relations Issues

In making its case for a new personnel system, DoD stated that the ability to make decisions promptly was essential for it to carry out its national security mission. Also essential for DoD are the abilities to manage its workforce and assign them to duties it deems appropriate. Reflecting those concerns, NSPS regulations included rules intended to reduce the time it takes for DoD to carry out adverse actions and address any follow-on appeals. The regulations also broadened the scope of management rights beyond those established in prior legislation. As an example, procedures for making work assignments and determining deployments (such as sending civilian employees to a war zone) would be excluded from bargaining unless the Secretary of Defense chose to do so.

Because of the directive in Public Law 110-181, DoD has not, and will not, implement the adverse actions, appeals, and labor relations elements of NSPS. For that reason, CBO has not attempted to assess whether NSPS's initial goal of increased management flexibility has been met.

19. The results of focus group meetings with NSPS employees conducted by the Government Accountability Office between August 2007 and July 2008 supported those survey results. According to GAO, although some of DoD's employees and their supervisors under NSPS seemed optimistic about the intent of the system, most of the DoD employees and supervisors at the focus group meetings "expressed a consistent set of wide-ranging concerns." The concerns cited include a negative impact on employee motivation and morale and the rapid pace at which the system was implemented, which often resulted in employees feeling unprepared and unable to find answers to their questions. For more details, see Government Accountability Office, *Human Capital: DoD Needs to Improve Implementation of, and Address Employee Concerns About, Its National Security Personnel System*, GAO-08-773 (September 2008).

Goal No. 3: Motivate Effective Work

NSPS increases the importance of job performance in determining how employees are rewarded. The performance management changes in NSPS lay out specific procedures for appraising and rewarding performance. One fundamental departure from the previous system is that, under NSPS, underperforming employees can be denied all types of pay raises—including the heretofore widely awarded general salary increases. To see whether the new system is achieving its objective of motivating effective work, CBO examined some partial, indirect evidence on NSPS's performance management system.

CBO analyzed performance appraisal data for DoD employees converted to NSPS in the first three spirals and compared those results with the experience of other federal departments and agencies with pay-for-performance systems (namely, the personnel systems at China Lake, Naval Sea Systems Command, and the Department of Commerce).²⁰ The data for the other federal pay-for-performance systems are from 2002, the most recent year for which performance appraisal data for those agencies are available. CBO also examined survey data on employees' attitudes toward NSPS. The results of CBO's analysis may be summarized as follows:

- *Although fewer employees have received above-average ratings under NSPS, virtually no employees have received "unsatisfactory" performance ratings.* CBO's analysis of the performance appraisal data shows substantial variation in the extent to which the relevant federal departments and agencies differentiate performance. The percentage of employees receiving above-average ratings ranged from 33 percent in NSPS to 87 percent at the Department of Commerce's demonstration project. The data also show that virtually no employees in either NSPS or in the demonstration projects received an unsatisfactory performance rating. However, those findings cover only a portion of DoD's employees under NSPS for a relatively short time (since the implementation of the new system).²¹ To the extent that NSPS performance appraisals reveal chronically poor performers, DoD could keep track of their retention rates, which should decrease in the longer term if the performance management system meets its intended objectives.

20. The personnel systems at Naval Sea Systems Command and the Department of Commerce are ongoing demonstration projects.

21. The data cover roughly 102,000 employees. About 180,000 DoD employees have been converted to NSPS as of June 2008.

■ *DoD's employees under NSPS are most concerned about the performance appraisal process.* In surveys conducted between April 2005 and May 2007, a larger percentage of DoD's employees indicated that communicating performance expectations, making fair personnel decisions, and motivating employees to perform well are among the most important skills for supervisors under NSPS (compared with the percentage of employees who indicated the importance of other skills, such as career counseling). Similarly, the subject most often identified by DoD employees as the most important training area is the performance management system; subjects like labor relations and appeals processes were cited by fewer employees as the most important training areas. According to DoD, the measures it is putting in place to ensure that the performance management system functions properly include training supervisors to provide candid and constructive feedback to employees and emphasizing the need for continuous, meaningful dialogue between supervisors and employees.

However, the Government Accountability Office's (GAO's) recent focus group meetings with DoD's NSPS employees revealed concerns similar to those indicated by the surveys. The NSPS employees in the focus group meetings noted, in their view, the excessive amount of time and effort required to navigate the performance management process and the potential influence that employees' and supervisors' writing skills have on employee ratings.²² GAO also reported that DoD has not developed a specific action plan to address the issues identified by its employees' concerns, citing the Program Executive Office's (PEO's) preference to wait until employees have more experience under the system before making changes.

It remains to be seen how well the NSPS requirement to link individual employees' performance to organizational goals has been achieved. In general, organizational goals are derived from successively higher-level objectives such as military service-specific missions and DoD-wide objectives. As such, they are usually stated in terms that are probably too broad to allow for a straightforward link to the duties and responsibilities of individual jobs. According to DoD, the Program Executive Office for NSPS and

officials at the components provided instructions to employees and supervisors on linking individual performance objectives to organizational goals. The basic approach is to begin with higher-level objectives and cascade down to lower-level ones, ultimately reaching individual job objectives. Employees identified for conversion to NSPS and their supervisors received training on how to accomplish that task and carried out a trial run or mock performance evaluation process.

Even the employees who were converted first to NSPS (those in Spiral 1.1) have undergone only two performance appraisal cycles since then. That experience is not sufficient for CBO to determine how effectively the task of linking individual performance to DoD's overall goals was accomplished. (Direct information on employees' performance appraisals and the linkage to organizational goals was not available to CBO.)

The Costs of Implementing NSPS

The costs of implementing NSPS are twofold. First, there are monetary costs such as those incurred in setting up and operating the Program Executive Office and developing training materials. The major organizational levels at which NSPS implementation costs are incurred include the various offices in DoD components where employees are actually converted to NSPS as well as the Program Executive Office, which coordinated the design and implementation of the new system. Officials at the DoD components informed CBO that they did not receive any special funding for their activities on the design of NSPS and conversion of employees. Instead, those activities were funded from existing resources.

Second, there are opportunity costs when employees are diverted from their normal duties and tasked to work on NSPS-related activities. For instance, the DoD components assigned staff to the NSPS Program Executive Office to help design the new system. Also, employees at the DoD components attended various informational training sessions on NSPS and received more in-depth training on topics such as linking individual performance to organizational goals. In addition, the first group of employees converted to the system carried out a mock performance evaluation process before their real appraisal. All of those NSPS-related activities involved opportunity costs in the sense that the time spent was no longer available for employees' normal duties. According to officials at the DoD components and the PEO, the

22. See Government Accountability Office, *Human Capital: DoD Needs to Improve Implementation of, and Address Employee Concerns About, Its National Security Personnel System*.

direct costs of providing training to employees are documented and tracked. However, CBO was unable to verify the accuracy of those records and independently estimate the salary costs of DoD employees who supported the design and ongoing implementation of NSPS.

In 2007, DoD estimated that it would cost about \$166 million through 2008 to implement NSPS. That estimate reflected the direct cost of designing and implementing the system, including the cost of setting up and operating the NSPS Program Executive Office and the National Security Labor Relations Board, a new departmental entity that would adjudicate selected labor disputes. A report by GAO concluded that DoD's figure probably understates the costs the department will incur in implementing NSPS. That is because DoD did not include other direct costs, such as the full salary costs of military and civilian personnel who directly supported NSPS departmentwide, or any indirect costs, such as operation and maintenance costs for buildings and general administrative services.²³ Moreover, GAO could not determine the total amount of funds DoD had expended or obligated on NSPS in 2005 and 2006, citing deficiencies in DoD's cost-reporting system and inadequate pro-

gram oversight. In May 2008, DoD provided another estimate of \$143 million for the continuing costs of implementing NSPS from 2009 through 2011.²⁴ Information that would allow a determination of whether that latest estimate addressed the problems with previous ones was not available to CBO.

In a more recent report, GAO states that, according to the NSPS Program Executive Office, each DoD component took actions to address concerns about oversight of the process for reporting costs. For example, the Army established new account processing codes that comply with NSPS reporting categories and provided for an independent review to determine whether the Army's Major Commands are meeting established internal procedures for tracking, capturing, and reporting NSPS implementation costs in specific categories. In addition, the other components (the Navy, the Office of the Secretary of Defense, and other DoD agencies) have taken steps to improve the accuracy of the NSPS implementation costs they report.²⁵

23. See Government Accountability Office, *DoD Needs Better Internal Controls and Visibility over Costs for Implementing Its National Security Personnel System*, GAO-07-851 (July 2007).

24. See National Security Personnel System: Proposed Rule, 73 Fed. Reg. 29282 (May 22, 2008), codified at 5 C.F.R. 9901.

25. For more details, see Government Accountability Office, *Human Capital: DoD Needs to Improve Implementation of, and Address Employee Concerns About, Its National Security Personnel System*.

Human Resources Management Under the General Schedule System

The main elements of all the personnel systems for white-collar employees in the federal government comprise rules for classifying jobs and setting pay levels. Most white-collar federal employees are covered by the classification and compensation structure known as the General Schedule system. That system is supported by other personnel policies for staffing (hiring), adverse actions (such as firing) and appeals, and labor relations. The basic features of the GS system date back to the late 1940s when it was established by the Classification Act of 1949, which merged several separate “schedules” of pay rates into one “General Schedule.”¹ The system, as it exists today, is described in chapters 51 and 53 in title 5 of the U.S. Code.

One of the hallmarks of the GS system is that its pay structure applies to all occupations. The system has governmentwide rules and procedures for setting pay for newly hired employees, increasing an individual employee’s pay, and adjusting the overall pay structure on the basis of comparisons with pay levels in the private sector. This chapter briefly discusses the main features of the GS system, focusing on those that are most relevant to the key objectives of the Department of Defense’s National Security Personnel System.

Job Classification and Compensation Structure

The basis of the GS pay structure is its job classification system, which sorts jobs in hundreds of occupations into 15 grade levels on the basis of the difficulty of the work performed, educational requirements, and level of responsibility. Movement from one grade to another, for

an incumbent employee, is typically accomplished through a change in jobs resulting from a promotion. Each grade has a specified pay range; higher numeric grade levels receive greater pay. Each grade’s pay range, which is about 30 percent, is further divided into 10 fixed rates of pay, or “steps”; each step represents a 3 percent increase, on average. (Table 2-1 presents the GS pay structure as of January 2008.)

An employee’s pay is typically set at one of the steps, and entry-level pay is normally at the first step. Supplements are added to the basic pay ranges to reflect local job market conditions and changes in the cost of living, so the actual amounts in each grade’s pay range vary from one locality to another. (Table 2-1 shows the minimum amounts, excluding the locality supplements.) The pay for a given grade in a certain locality is the same for nearly all occupations. However, the Office of Personnel Management can establish special salary rates to increase the pay for occupations in grade levels for which there are significant difficulties in hiring or retaining personnel at the standard pay rates.

In addition to its use in setting pay rates, that job classification system is a factor in other elements of human resources management. For example, grade level is used to determine qualifications standards for new hires and also serves as part of the framework for determining how employees are affected during layoffs.

Pay Progression

Federal employees progress through the steps within a pay grade after serving for one, two, or three years at their current level. The advancement depends on their position in the grade: For employees currently in steps 1 through 3, the waiting period is one year; the period is two years for employees in steps 4 through 6 and three years for

1. See Office of Personnel Management, *A Fresh Start for Federal Pay: The Case for Modernization* (April 2002).

Table 2-1.**Annual Pay Rates, by Grade and Step, in the General Schedule System, January 2008**

(2008 dollars)

Grade	Step 1	Step 2	Step 3	Step 4	Step 5	Step 6	Step 7	Step 8	Step 9	Step 10
1	17,046	17,615	18,182	18,746	19,313	19,646	20,206	20,771	20,793	21,324
2	19,165	19,621	20,255	20,793	21,025	21,643	22,261	22,879	23,497	24,115
3	20,911	21,608	22,305	23,002	23,699	24,396	25,093	25,790	26,487	27,184
4	23,475	24,258	25,041	25,824	26,607	27,390	28,173	28,956	29,739	30,522
5	26,264	27,139	28,014	28,889	29,764	30,639	31,514	32,389	33,264	34,139
6	29,276	30,252	31,228	32,204	33,180	34,156	35,132	36,108	37,084	38,060
7	32,534	33,618	34,702	35,786	36,870	37,954	39,038	40,122	41,206	42,290
8	36,030	37,231	38,432	39,633	40,834	42,035	43,236	44,437	45,638	46,839
9	39,795	41,122	42,449	43,776	45,103	46,430	47,757	49,084	50,411	51,738
10	43,824	45,285	46,746	48,207	49,668	51,129	52,590	54,051	55,512	56,973
11	48,148	49,753	51,358	52,963	54,568	56,173	57,778	59,383	60,988	62,593
12	57,709	59,633	61,557	63,481	65,405	67,329	69,253	71,177	73,101	75,025
13	68,625	70,913	73,201	75,489	77,777	80,065	82,353	84,641	86,929	89,217
14	81,093	83,796	86,499	89,202	91,905	94,608	97,311	100,014	102,717	105,420
15	95,390	98,570	101,750	104,930	108,110	111,290	114,470	117,650	120,830	124,010

Source: Office of Personnel Management.

Note: Pay rates reflect the minimum amount and exclude the locality supplements.

employees in steps 7 through 9.² Those periodic increases are awarded as long as an employee's performance is at an "acceptable level of competence."³ According to governmentwide regulations, an acceptable level corresponds to a performance appraisal rating of 3 ("fully successful") or higher in five-level appraisal programs or a rating of "pass" in appraisal programs that use only two summary levels (pass/fail).⁴ An employee's progress through the steps can be accelerated through the award of an addi-

tional step increase in recognition of high-quality performance beyond the level ordinarily found in that position.

Federal employees also receive an annual adjustment or structural increase applied to the entire GS pay table. Based on the U.S. Bureau of Labor Statistics' measure of the cost of labor (the employment cost index), that adjustment reflects the policy that federal pay rates should be comparable with nonfederal pay for similar types of work.⁵ The adjustment is paid to all employees as a general pay increase and not differentiated on the basis of performance.

2. Some researchers have associated periodic step increases at fixed intervals that lengthen over time with a "learning curve" theory. Initial annual pay increases reward gains in knowledge, skills, and performance that are presumed to occur in the first few years in a grade. Pay raises decelerate to a biennial pace when an employee achieves mastery of the job. Finally, skill acquisition within a grade is presumed to taper off in later years, when the final step increases are granted at three-year intervals to reward continued mastery of the job and loyalty. See Office of Personnel Management, *Alternative Pay Progression Strategies: Broadbanding Applications*, PMD-05 (April 1996).

3. 5 U.S.C. § 5335.

4. Typically, the rating levels in five-level appraisal programs in the federal government are: (1) unacceptable; (2) minimally successful; (3) fully successful; (4) exceeds fully successful; and (5) outstanding.

5. Usually set by the Congress, the adjustment rate is not always equal to the rate of increase in the employment cost index. Between 2001 and 2006 (the dates for which comparable data are available), the rate of the annual structural increase in base pay combined with the increase in the locality supplements was higher than the rate of increase in the employment cost index: GS salaries including locality pay increased by an average of 3.9 percent during that period, compared with a 3.1 percent average increase in the employment cost index for private-sector white-collar workers. The Congress usually sets the same basic annual increase for military and civilian personnel: Federal civilian employees received the same percentage pay raises as military personnel in 27 of the past 33 years (1975 to 2008).

Staffing and Workforce Shaping

The traditional process for hiring federal employees is described in chapters 31 through 37 of title 5 of the U.S. Code. That legislation prescribes governmentwide procedures for admitting individuals into the civil service, including rules for advertising positions, examining and selecting candidates, and assigning personnel. In general, the rules call for an open competition for all civil service positions, with some exceptions. For example, direct appointments may be made when OPM has determined that there is a severe shortage of candidates for specific jobs or a critical need for specific skills. Exceptions may also be made to obtain the services of specially qualified professional personnel for carrying out research and development functions.⁶

In addition, the law established procedures for ranking job applicants for selection or retention. For instance, in selecting employees for federal employment, preference must be given to individuals with prior military service. Likewise, in the event of a reduction in force (or layoff), the rules for releasing competing employees rank employees on the basis of certain qualifications (known as retention factors). In decreasing order of importance, those factors are tenure (career, term-limited, or temporary employment statuses), veteran status, time in federal employment, and performance rating. Normally, OPM has the authority to administer those staffing procedures (as well as procedures dealing with other parts of the personnel system) unless it chooses to delegate that authority to agencies.

Adverse Actions and Appeals and Labor Relations

Regulations for adverse actions and appeals set out the rules for taking disciplinary action against employees for

causes based on performance or conduct. Such disciplinary action could include suspension, termination, and reduction in grade or pay. The rules provide for notice of proposed adverse actions, the right to reply, and the right to appeal to the Merit Systems Protection Board. Affected employees are entitled to written notice of at least 30 days, and they must receive at least 7 days to respond. The board, on reviewing a case, can sustain an agency's decision only if that decision is "supported by substantial evidence" in the case of an action based on an employee's performance, or "supported by a preponderance of the evidence" in the case of an action based on any other cause, such as conduct.⁷ If employees are not satisfied with the decision of the board, they can further appeal to the U.S. Court of Appeals for the Federal Circuit, the next step in the process.

The regulations in existing law that cover labor relations set forth the rights and duties, respectively, of employees and agencies to engage in collective bargaining, as well as the procedures for doing so.⁸ The regulations also stipulate actions by management that are excluded from bargaining. Those "management rights" include setting the mission of organizations, determining the number of employees, and deciding to hire, assign, retain, separate, and discipline employees.⁹ Management could also take actions that "may be necessary to carry out the agency mission during emergencies," in accordance with applicable laws.¹⁰ The Federal Labor Relations Authority adjudicates labor relations disputes.

7. Those legal standards are in 5 U.S.C. § 7701(c)(1).

8. 5 U.S.C., ch. 71.

9. However, an agency may elect to bargain on those issues.

10. 5 U.S.C. § 7106(a)(2)(D).

6. 5 U.S.C. § 3104, 3304.

The Department of Defense's Objectives for the National Security Personnel System

According to the Department of Defense, the traditional General Schedule system is a rigid “one size fits all” approach to defining work, hiring and managing personnel, and rewarding performance.¹ DoD views that system as cumbersome and inflexible—it constrains the department from tailoring hiring and compensation policies to meet specific needs, for example. In designing its new National Security Personnel System, DoD’s goals were the following:

- Increase management flexibility in hiring and compensating employees,
- Increase management flexibility with regard to adverse actions and labor relations issues, and
- Motivate effective work.²

DoD sought to achieve those objectives by taking an approach that differed in many respects from that used by the traditional federal personnel system. (Table 3-1 summarizes and compares selected elements of the GS system and NSPS.) In this chapter, the Congressional Budget Office examines each of DoD’s objectives for NSPS and the elements of that new system that are meant to achieve those objectives.

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1. See Department of Defense and Office of Personnel Management, Department of Defense Human Resources Management and Labor Relations Systems: Final Rule, 70 Fed. Reg. (2005).
 2. Those goals, as stated, are the Congressional Budget Office’s interpretations of the rationale for NSPS from DoD sources such as testimonies (statement of David S. C. Chu, Under Secretary of Defense for Personnel and Readiness, before the Subcommittee on Oversight of Government Management, the Federal Workforce, and the District of Columbia of the Senate Committee on Governmental Affairs, *An Overlooked Asset: The Defense Civilian Workforce*, May 12, 2003) and policy documents (ibid.).

Increase Management Flexibility in Hiring and Compensating Employees

According to DoD, the previous personnel system’s procedures for defining jobs and hiring employees are burdensome and overly time consuming. As a case in point, DoD officials indicate that the GS system’s rules for “grading” jobs do not provide sufficient latitude for managers to select starting grade and salary for new employees. That constraint impedes DoD’s ability to hire talented people. In attempting to address those concerns, DoD, in designing NSPS, made changes to its staffing process, provided new hiring authorities under its control (instead of the control of the Office of Personnel Management), and established new methods (notably pay banding) for the way in which jobs are classified and graded. NSPS also provides additional ways for employees to move internally to other jobs.

Staffing

DoD states that its NSPS regulations provide for a streamlined process of placing individuals into jobs. Applicants qualify for positions under NSPS in the same way as under the General Schedule system: They must demonstrate the knowledge, skills, abilities, and competencies needed to be successful in the position. NSPS also uses the employment authorities under current law.³ However, although vacancies must still be announced in order to hire workers from outside the government, NSPS provides new flexibility in its rules and procedures. For example, in announcing vacancies, managers now have the option to target applicants from a local recruiting area or other targeted recruitment sources. Also, no minimum open period is required for announced job openings; the open period is based on the type of position

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3. Legislation governing employment or appointing authorities is in 5 U.S.C., chs. 31, 33.

Table 3-1.

Comparison of Elements in the General Schedule System and the National Security Personnel System

Element	Structure in GS System	Structure in NSPS
Classification and Compensation	Jobs sorted into 15 grade levels, each with 10 subdivisions or “steps.” Over 300 classification standards (rules for defining positions in terms of duties, responsibilities, and qualification requirements, establishing titles for those positions, and assigning them into grades). Movement to higher grades by promotion requiring official personnel action. Entry pay normally at first step of grade level.	Jobs placed in broader pay bands with 3 or 4 levels (no grades or steps). 15 classification standards. Assignment to higher-paying job within a pay band possible without official promotion action. Entry pay varies within a pay band to reflect occupation-specific market conditions.
Performance Management and Pay Progression	Use of tailored performance standards that vary from position to position. Performance appraisal systems may have as few as two summary rating levels (for instance, “pass/fail”). No requirement to link individual performance standards to agency/organizational mission and objectives. Annual general pay increase awarded to virtually all employees. Periodic step increase conditional on an “acceptable” level of performance; an additional step increase (a quality step increase) is given for exceptional performance.	A common set of performance indicators applies to all positions under the same category of work (for example, supervisory, analytical, professional, or technical). Five-level performance rating system applies to all employees. Individual performance standards linked to agency/organizational mission and objectives. Employees with “unacceptable” performance ratings receive no increases in pay of any kind. Part of a general increase is set aside for performance-based payouts. Only employees with performance ratings that meet or exceed performance standards receive an increase in base pay and annual general and locality adjustments.

Continued

being filled and the availability of qualified candidates in the labor market.

In addition, NSPS legislation provides DoD with new appointment authority to hire personnel without prior approval from the Office of Personnel Management under specified circumstances, such as the following:

- A severe shortage of candidates for particular occupations,

- A critical need for certain occupations, and
 - A need for time-limited appointments so as to be able to hire individuals to meet legitimate nonpermanent staffing needs.
- DoD must notify OPM when it exercises that authority. CBO’s discussions with DoD officials indicate that DoD has yet to exercise that authority for its NSPS employees. For all other hiring authorities, DoD must coordinate

Table 3-1. **Continued**
Comparison of Elements in the General Schedule System and the National Security Personnel System

Element	Structure in GS System	Structure in NSPS
Staffing (Hiring)	Job announcements open to all U.S. citizens. Hiring authorities for positions with severe shortages or critical needs require the Office of Personnel Management's approval.	Relaxed rules for filling positions from outside the government (for example, the ability to target a local commuting area). Hiring authorities for positions with severe shortages or critical needs may be approved within the Department of Defense.
Adverse Actions	30-day notice is given to affected employees. Affected employees may appeal to the Merit Systems Protection Board (MSPB). Existing law specifies legal standards MSPB would use in reversing DoD's adverse action decision. MSPB decisions subject to judicial review in Appeals Court.	15-day notice is given to affected employees.^a Affected employees may appeal to the MSPB, but NSPS regulations require that the board use administrative judges for initial review. DoD would review and could modify the judges' initial decision. NSPS regulations use more stringent legal standards that limit the ability of judges to modify DoD-imposed penalties. NSPS allows employees to appeal to the full MSPB but specifies the legal standards listed in the NSPS legislation that the board would use to overturn its initial decision.^a
Labor Relations	Management rights such as determining organizational mission, setting the number of employees, and making decisions to hire, assign, retain, separate, and discipline employees are excluded from bargaining. Subject to applicable laws, management is not restricted in taking actions necessary to carry out DoD's mission during emergencies. The Federal Labor Relations Authority (FLRA) oversees labor relations issues.	Expands management rights by adding procedures in making work assignments and deployments to the list of those rights that are excluded from bargaining unless the Secretary of Defense, at his or her unreviewable discretion, elects to bargain.^a The National Security Labor Relations Board (created by DoD) would address labor relations issues DoD deems most important to carrying out its mission. Other issues are overseen by FLRA.^a

Source: Congressional Budget Office based on title 5 of the U.S. Code and data from Department of Defense, National Security Personnel System Program Executive Office.

Note: DoD = Department of Defense.

a. These elements of NSPS will not be implemented as directed by the Congress in the National Defense Authorization Act for Fiscal Year 2008.

with OPM before establishing those authorities or jointly publish a notice in the *Federal Register*.

Under NSPS, current employees can move to other positions in the same pay band or in a different pay band. If the position is in the same pay band, then competitive procedures may not apply. If it is in a higher pay band, then competitive procedures apply.

Transfer Without Competition. Because pay schedules and pay bands encompass many levels of work and occupations, employees under NSPS can move from one position to another without competition. For example, an employee can be reassigned to a different position or set of duties within a pay band or to a position in a comparable pay band temporarily or permanently. In some instances, employees can even move to a higher level of

work without competitive procedures. For example, an employee's position can be reclassified into a higher pay band because of additional duties and responsibilities, or an employee can be promoted to a position in a higher pay band for 180 days or less.⁴

Transfer With Competition. Competitive procedures apply when an employee is being selected or applying for a position in a higher pay band than his or her current position. Under those conditions, NSPS regulations allow for alternative forms of competition, which do not require vacancy announcements but instead consider performance. Examples of alternative forms of competition include exceptional performance promotion, alternate certification, and assessment boards. Under exceptional performance promotion, an employee with the highest performance rating (level 5, or "role model") could be selected for promotion to a job in the same occupation without completing an application, after the selecting official considers other employees with the same level of performance. Under alternate certification rules, a manager could name an employee to fill a vacant position if the manager and the human resources office determine he or she is among the best-qualified employees being considered for the position. DoD's components (the services and agencies) may establish assessment boards that convene regularly to evaluate and recommend employees for vacant positions.

Classification and Compensation

Like the GS system, NSPS recognizes relationships between occupations that involve similar work by grouping those occupations into career groups. The GS system has 23 occupational groups, each consisting of dozens of individual occupations.⁵ NSPS regroups occupations into four career groups: three specialized ones (scientific and

engineering, medical, and investigative and protective services) and a standard one that includes all occupations not covered by a specialized career group. When NSPS is fully implemented, about 73 percent of covered employees will fall into the standard career group, DoD projects, and 19 percent will fall into the scientific and engineering career group. The other two career groups will each account for 4 percent of employees in the new system (see Figure 3-1). Each NSPS career group has up to four pay schedules based on, among other things, job competencies and career patterns.⁶

Unlike the GS system (with its 15 grade levels), NSPS sorts jobs into three or four pay bands representing a range of basic pay.⁷ In the GS system, a specific position—with its certain duties and responsibilities—is associated with an occupation and grade level. Supervisors typically cannot assign tasks with greater or lesser difficulty to an incumbent employee without reclassifying the position. In NSPS, the broader groupings of jobs allow greater latitude for job assignments, a flexibility that DoD's managers have frequently used since the system was implemented. In general, employees can be assigned to new better-paying jobs in a given pay band (involving a pay increase of up to 5 percent) without competition. Also, the wider range of pay in each band makes it easier to accommodate higher starting salaries for new hires if the market demands it.

In addition to pay bands, NSPS implements several pay policies intended to respond to local market conditions. First, it bases adjustments to the minimum and maximum pay in each band—"rate range adjustments"—in part on labor market conditions for each career group. Second, NSPS provides for local market supplements, which are additional payments to employees in specified

4. That policy also exists in the GS system.

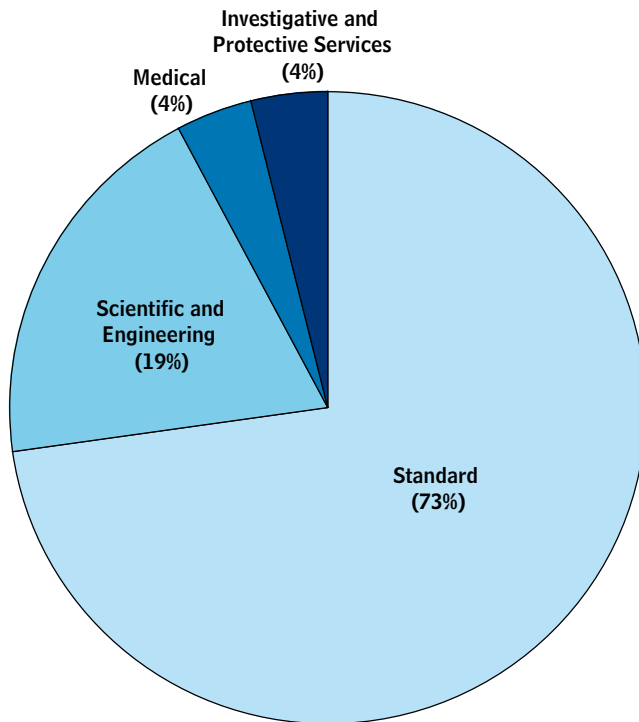
5. The GS occupational groups are social science, psychology, and welfare; human resources management; general administrative, clerical, and office services; biological sciences; accounting and budget; medical, hospital, dental, and public health; veterinary medical science; engineering and architecture; legal kindred services; information and arts; business and industry; copyright, patent, and trademark; physical sciences; library and archives; mathematics and statistics; equipment, facilities, and services; education; investigation; quality assurance, inspection, and grading; supply; transportation; information technology; and a miscellaneous group for occupations not classified elsewhere.

6. There are 15 pay schedules in total. For the standard career group, they are "professional/analytical," "technician/support," "supervisor/manager," and "student"; for the scientific and engineering career group, they are "professional," "technician/support," and "supervisor/manager"; for the investigative and protective services career group, they are "investigative," "fire protection," "police/security guard," and "supervisor/manager"; and for the medical career group, they are "physician/dentist," "professional," "technician/support," and "supervisor/manager."

7. In essence, each pay band represents a collection of GS grades with minimum and maximum rates of pay.

Figure 3-1.
Career Groups in the National Security Personnel System

(Percentage of employees in each group)



Source: Congressional Budget Office based on data from Department of Defense, National Security Personnel System Program Executive Office.

local market areas, occupations, specializations, or pay bands. Calculated as a percentage of base salary, those supplements replace the locality pay and special salary rates of the GS system. However, unlike the GS system, in which all occupations in the same local area receive the same locality supplements, in NSPS, supplements may vary by occupational specialty, occupation, or career group within the same local area. Similarly, different pay bands in the same career group may receive different amounts. According to NSPS policy, employees with an “unacceptable” performance rating are not eligible for either the rate range adjustments or the local market supplement increases.

Increase Management Flexibility with Regard to Adverse Actions and Labor Relations Issues

NSPS's initial set of regulations included provisions intended to reduce the time it takes for the Department of Defense to carry out adverse actions and address any follow-on appeals. The regulations also broadened the scope of management rights—actions that management can take without collective bargaining—beyond those in prior legislation. In addition, the regulations curbed bargaining over the procedures DoD must follow when exercising management rights and the appropriate actions that DoD must take for employees affected by the exercise of those management rights.⁸ (Box 3-1 provides a summary of NSPS provisions on adverse actions and appeals and the labor relations process.) According to NSPS documents, those changes were needed to provide DoD with more flexibility in managing its workforce—a necessity for the department to carry out its national security mission.

After the initial regulations were issued, several unions representing more than 350,000 DoD civilian employees filed suit against the Secretary of Defense and the Director of OPM, arguing that, among other things, the regulations exceeded DoD's statutory authority.⁹ A lower court agreed with the unions, and the case advanced to the federal appeals court, which decided in favor of DoD. Meanwhile, DoD began implementing other parts of the system for its nonunion employees. Public Law 110-181 directed DoD to restore the adverse actions, appeals, and labor relations policies that existed under regular civil service law.¹⁰ Thus, the NSPS provisions described in Box 3-1 were never implemented and DoD reverted instead to the policies under preexisting law.

8. Department of Defense Human Resources Management and Labor Relations Systems, paras. 9901.901, 9901.910(c).

9. See *American Federation of Government Employees v. Donald H. Rumsfeld*, Civ. No. 05-2183 (EGS).

10. See Public Law 110-181, sec. 1106. That legislation also required DoD to follow governmentwide rules for reductions in force or layoffs. According to those rules, employees are placed on a retention list on the basis of their ranking for certain factors. The retention factors, which reflect the ability of employees to displace one another, are, in descending order of importance, tenure (career, term-limited, or temporary employment statuses), veteran status, time in federal employment, and performance rating. NSPS had revised the order of the retention factors by placing performance rating before time in federal employment.

Motivate Effective Work

The Department of Defense seeks to foster a high-performance culture. Viewing the GS system as one in which high performers and low performers are paid alike, DoD is attempting to revamp its performance management process to better tie pay increases to employees' performance. The concept of pay for performance was one of the major issues the Congress discussed while it was considering NSPS legislation. That legislation expressly required DoD to develop an evaluation system to better link individual pay to performance.

Advocates for the GS system point out that the rules of pay progression are well understood and accepted, allow for predictable compensation costs, and are devoid of the potential turmoil that could result from systems based on subjective performance criteria. Advocates for reform generally express dissatisfaction that, notwithstanding rules and regulations, the GS system places relatively little value on performance and a significant value on time served.¹¹ They note that even though pay increases within a pay grade are conditional on an "acceptable" level of performance, those increases are virtually automatic as most employees receive favorable ratings.¹² According to that view, the GS system promotes mediocre performance and hinders the retention of top performers in the federal government. Advocates for reform also point out that most private employers do not grant general increases for their white-collar employees because they consider performance to be a fundamental value that should drive their compensation system. Pay for performance is not new in government institutions; the federal government and some local governments have already converted to it or experimented with it.¹³

In response to the Congress's direction, the design of NSPS explicitly incorporates a pay-for-performance system. The principles of the new performance management system include the following:

- Only employees who meet or exceed performance standards receive an increase in base pay or rate range adjustments and supplements (such as the local market supplements).¹⁴
- Higher levels of performance are rewarded with larger increases in pay. Superior performers advance faster through a pay range.

As is the case with many federal agencies in the GS system, employees' performance in NSPS is rated on a 5-point scale (though the language used to describe the rating levels differs). NSPS's 5-point scale has scores ranging from 1 for "unacceptable" performance to 5 for "role model" (see Table 3-2).¹⁵ Employees rated at level 3 or higher are eligible for performance-based pay increases, rate range adjustments, and local market supplement increases. Employees with a rating of 2 (fair) receive rate range adjustments and increases in the local market supplement but no performance-based pay increase. Employees with a rating of 1 receive no increases of any kind. A supervisor's assessment of an employee's performance is subject to review by a panel of senior management officials whose responsibility is to seek equity and consistency in performance ratings in a pay pool.¹⁶ A pay pool manager approves the final rating.

The actual pay raise granted to an employee depends on the number and value of the "shares" he or she receives.

11. According to OPM, more than 75 percent of federal pay increases bear no relationship to individual performance. See Office of Personnel Management, *A Fresh Start for Federal Pay: The Case for Modernization* (April 2002).

12. For example, some researchers have noted that 98 percent to 99 percent of federal employees receive a rating of "satisfactory" or better. See Brigitte W. Schay, "Broadbanding in the Federal Government: A 16-Year Experiment," *American Compensation Association Journal* (Autumn 1996).

13. Today, pay for performance is a component of alternative personnel systems for many federal agencies. A summary of human resources practices at those agencies is available at www.opm.gov. The trend in pay for performance for teachers is examined in *Reforming Teacher Pay: The Search for a Workable Goal-Driven Compensation System* (San Francisco, Calif.: WestEd, 2005), www.wested.org/cs/we/view/rs/797.

14. Rate range increases are adjustments applied to the minimum and maximum amounts in a pay band. They are usually intended to make pay levels in a pay band comparable with rates in the private sector.

15. DoD prefers that multilevel rating method because it allows raters to make meaningful distinctions in performance. The research literature reviewed by CBO suggests that the reliability of ratings decreases when there are fewer than 3 categories or more than 9 and that 3 to 5 categories seems to work best. See National Research Council, *Pay for Performance: Evaluating Performance Appraisal and Merit Pay* (Washington, D.C.: National Academy Press, 1991).

16. A pay pool is a group of employees who work in an organization or work unit and share funding for performance payouts.

Box 3-1.**Selected Provisions on Adverse Actions, Appeals, and the Labor Relations Process Under the National Security Personnel System**

The National Security Personnel System's (NSPS's) provisions on adverse actions, appeals, and the labor relations process will not be implemented. Instead, the Department of Defense (DoD) will revert to the policies under preexisting law, as directed by the National Defense Authorization Act for Fiscal Year 2008 (Public Law 110-181). This analysis examines what those provisions would have entailed if they had been implemented.

Before an employee can be removed or otherwise penalized because of his or her conduct or performance, typical due process rights as determined by legal custom provide that the employee is given notice, an opportunity to reply, a decision, and a postdecision review. Under NSPS, affected employees would have received a 15-day notice period for adverse actions (compared with 30 days under existing legislation) and a modified process for appealing an adverse action.

NSPS legislation would have given DoD the authority to establish the procedures employees could use when appealing adverse actions, including the legal standards third parties might use to determine whether to modify (or mitigate) DoD-imposed penalties (see 5 U.S.C. § 9902 (h)(2)). The NSPS regulations would have allowed Merit Systems Protection Board (MSPB) administrative judges or private arbitrators to review employees' initial appeal of DoD adverse actions. However, although those judges and arbitrators could have reviewed and adjudicated a case, they could not have modified DoD-imposed penalties unless such penalties were "totally unwarranted in light of the pertinent circumstances."

NSPS regulations also would have required that the decisions of judges or private arbitrators on cases appealed to them be reviewed by DoD before they became final. If employees were still not satisfied, they could have appealed their cases to the full MSPB and, further, to the Court of Appeals for the Federal Circuit. The full MSPB could have ordered that DoD change its decision on the basis of criteria listed in NSPS legislation (see 5 U.S.C. § 9902 (h)(5)).

In addition, NSPS regulations would have provided the Secretary of Defense with the authority to establish

offenses that, because they had a direct and substantial impact on national security, warranted a mandatory penalty of removal from the civil service. Employees charged with those offenses would still have had their due process rights, however.

Before NSPS, existing law governing labor-management relations allowed management and labor to negotiate some aspects of work. Management rights excluded from bargaining include determining the mission, budget, and number of employees in the department as well as deciding to hire, assign, direct, retain, remove, and discipline employees (see 5 U.S.C. § 7106). NSPS regulations would have expanded the list of management rights that were excluded from bargaining to include the "procedures observed in making work assignments and deployments unless the Secretary, in his or her sole, exclusive, and unreviewable discretion, elects to bargain."¹ The procedures that DoD would have followed in exercising its expanded management rights would have been subject to bargaining only at the discretion of the Secretary of Defense.² Moreover, the Secretary, at his or her discretion, could have withdrawn from negotiations before an agreement had been reached. Those management rights exist under current law, but only in emergencies.

Finally, the NSPS regulations would have created the National Security Labor Relations Board (NSLRB), whose members would have been appointed and removed by the Secretary of Defense. The NSLRB would have adjudicated certain labor disputes DoD deemed most important to accomplishing its mission; other matters would have been retained by the Federal Labor Relations Authority (FLRA). The decisions of the NSLRB would have been subject to review by the FLRA and further judicial review. Thus, the NSLRB would have represented another layer in the labor relations process.

1. See Department of Defense and Office of Personnel Management, Department of Defense Human Resources Management and Labor Relations Systems: Final Rule, 70 Fed. Reg. (2005), codified at 5 C.F.R. § 9901.
2. The proposed NSPS regulations initially excluded those procedures from bargaining.

Table 3-2.

Performance Rating Scale and Associated Rewards in the National Security Personnel System

Performance Rating		"Shares" Received	Standard Salary Adjustments Received
5	Role Model	5 to 6	{ Performance-based pay increase Rate range adjustments Local market supplement increases
4	Exceeds Expectations	3 to 4	
3	Valued Performer	1 to 2	
2	Fair	0	{ Rate range adjustments Local market supplement increases
1	Unacceptable	0	No increases

Source: Congressional Budget Office based on data from Department of Defense, National Security Personnel System Program Executive Office.

Notes: The actual pay raise granted to employees depends on the value of the shares. That value is obtained by dividing the amount of funds available for pay raises in a pay pool—a group of employees who work in an organization or work unit and share funding for performance-based payouts—by the total number of shares awarded in the performance evaluation cycle, weighted by each employee’s base salary.

Rate range increases are adjustments applied to the minimum and maximum amounts in a pay band and are usually intended to make the pay band comparable with market rates.

Those shares are distributed on the basis of each employee’s performance rating. Higher ratings receive more shares: A rating of 5 gets five to six shares; a rating of 4 gets three to four shares; a rating of 3 gets one to two shares; and ratings of 2 and 1 get zero shares. The value of a share is obtained by dividing the amount of funds available for pay raises in a pay pool by the total number of shares awarded in the performance evaluation cycle, weighted by each employee’s base salary.¹⁷ Thus, the percentage pay raise that an employee receives is the product of the number of shares and the value of each share. In that way, pay raises are not predetermined but instead depend on the results of the performance evaluation.¹⁸

That system can result in discrepancies in pay raises across pay pools, however. Because the value of a share

decreases with the number of shares awarded, outperforming employees in a pay pool or team with a large number of mediocre workers could receive larger pay raises than similarly outstanding performers who are part of a strong team, all else being equal. That outcome is possible because funds for pay pools are fixed—a policy that helps limit the potential for overall growth in DoD’s payroll costs. If the overall percentage pay increase was not set uniformly across pay pools, differences in team performance could be addressed by focusing on the performance of the entire team and providing larger funds to the pay pools of better-performing teams. However, that approach might not always be feasible in the public sector because measuring output in that sector is difficult. Measuring output in the private sector, in contrast, is easier, because team performance could be gauged by focusing on financial outcomes, such as net revenues or sales.

17. For example, consider a pay pool consisting of two employees, A and B, with annual base pay of \$50,000 and \$40,000, respectively. Employee A receives four shares in a performance evaluation cycle, and employee B receives three shares. If \$5,000 is available for pay raises in that pay pool, the share value is calculated as follows: $\$5,000 \div [(\$50,000 \times 4) + (\$40,000 \times 3)] = 0.0156$. Employee A’s payout would be 6.3 percent (4×0.0156) of his or her base pay, or \$3,125. Similarly, employee B’s payout would be 4.7 percent (3×0.0156) of his or her base pay, or \$1,875.

18. That approach contrasts with that of some other organizations in the federal government that use alternative personnel systems. The pay-for-performance system at DoD’s China Lake, for instance, has predetermined pay increases for each rating level. For further details, see General Accounting Office, *Human Capital: Implementing Pay for Performance at Selected Personnel Demonstration Programs*, GAO-04-83 (January 2004).

Nevertheless, in discussions with CBO, department officials pointed out that NSPS provides ways to recognize team or unit performance. First, pay pools may establish rules for deciding on higher or lower awards of shares that consider organizational success among the criteria for individual performance evaluations. Indeed, cooperation and teamwork are among the contributing factors used to

evaluate employees in the NSPS performance management system. Second, a discretionary Organizational or Team Achievement Recognition payout, which provides an increase in base pay or a bonus (or both) apart from those earned individually in a pay pool, is available to recognize team performance.

Issues and Concerns Raised During the Public Review and Comment Period

The legislation in Public Law 108-136 established procedures for the Department of Defense to collaborate with employees and their representatives in developing the National Security Personnel System.¹ The procedures include a 30-day period for employees, their representatives, and the public to review and submit formal comments or recommendations on the proposed system. That period is followed by a “meet and confer” period of at least 30 days during which DoD would meet with employee representatives and attempt to resolve any issues on which there was disagreement. The legislation further requires DoD to notify the Congress of any decision to implement those parts of the proposed system on which disagreement with employee unions remains. DoD may implement those parts of the system, but not until 30 days after notifying the Congress.²

According to DoD, it received more than 58,000 comments during the 30-day public comment period, mostly in the form of letters sent via electronic and regular mail. The Department of Defense provided a summary of the comments to the Congressional Budget Office for this analysis (the comments themselves were not made available to CBO).

According to the information provided by DoD, the comments generally covered the spectrum from approval to rejection of the proposed system. The main features of NSPS shift some responsibility for the overall personnel system away from traditional human resources specialists to department managers.³ Many commenters focused on the need for fairness in the system, citing too much

power being given to managers without corresponding accountability. Echoing the arguments made in the legal challenge by employee unions, commenters also expressed concern about maintaining due process rights and the scope of bargaining.

Commenters recommended changes to specific parts of the proposed regulations. Representatives from the Department of Defense and the Office of Personnel Management reviewed those suggestions and made any changes to the proposed regulations that they considered appropriate.⁴ According to DoD, differences with commenters remain over several issues, such as the scope of bargaining, the specificity of some parts of the NSPS regulations, and the use of work behavior (such as staying up to date in an employee’s occupational specialty) as part of performance evaluations.

Performance Management

Most commenters opposed a pay-for-performance system and urged DoD to retain the existing General Schedule system. Commenters were concerned that a pay-for-performance system would lower morale, undermine teamwork, and promote unhealthy competition among workers and that DoD’s managers would not be able to apply performance standards fairly and consistently to pay decisions. Despite those concerns, DoD retained pay

1. See 5 U.S.C. § 9902(f). Those procedures were included in section 1101(a) of Public Law 108-136 but were later eliminated by Public Law 110-181.

2. Ibid.

3. For instance, DoD officials have direct hiring authority, which streamlines the hiring process. Also, employees may progress through a pay band without an official promotion.

4. For more details on the major changes made to proposed NSPS regulations as a result of comments received during the meet-and-confer process, see Department of Defense and Office of Personnel Management, Department of Defense Human Resources Management and Labor Relations Systems: Final Rule, 70 Fed. Reg. (2005).

for performance, stating that the concept of higher rewards for better performers is valued in American society and crucial for DoD to carry out its mission. According to many observers, the GS system poorly addresses that principle. Because 99 percent of all GS employees meet minimal performance requirements, pay increases over time are determined primarily by time in grade.

Many commenters also expressed concern that funding of pay pools for pay raises would be insufficient and that such funding would probably be reallocated during budget execution for other uses, such as military operations, that might be deemed more pressing. According to NSPS documents, one of the required features of NSPS's design is that, on the whole, increases in civilian payroll costs will conform to guidance issued by the Office of Management and Budget (OMB)—that is, funds appropriated for civilian pay increases will be the same in both the GS system and NSPS. Also, the NSPS legislation (in Public Law 108-136, as amended by Public Law 110-181) stipulated certain pay limitations requiring that, for fiscal years 2004 through 2012, overall pay increases for employees under NSPS be the same as they would have been if those employees had not been converted to the new system.⁵ For fiscal years after 2012, the legislation also required DoD to develop a formula that ensures, to the maximum extent practicable, that employees are not disadvantaged in the overall amount of pay available as a result of conversion to NSPS.⁶ According to DoD officials, the department has implemented financial policies that protect pay pool funding. For example, appropriate senior-level officials are required to certify that funds allocated to performance-based pay have been used only for that purpose.⁷ In addition, any exception to the minimum funding of pay pools will be based on stringent criteria and must have higher-level approval.

5. 5 U.S.C. § 9902(e)(4).

6. 5 U.S.C. § 9902(e)(5). That constraint accommodates changes that may affect pay amounts, such as changes in the function of each organization or changes in the mix of employees performing those functions.

7. A senior official in each component certifies that the amount paid out for compensation in that component is not less than the amount that would have been paid out to employees had those employees not been converted to NSPS.

Adverse Actions and Appeals and Labor Relations

Before issuing the final NSPS regulations, DoD had proposed regulations that provided for shorter notice for adverse actions and an accelerated adjudication process for those cases that employees appeal.⁸ In the proposed regulations, DoD would have Merit Systems Protection Board administrative judges initially review adverse actions cases appealed by employees and decide whether to modify DoD-imposed penalties. Decisions by the administrative judges would then be reviewed—and possibly modified further—by DoD before becoming final. If necessary, employees could subsequently appeal cases to the full board and, ultimately, the Federal Circuit Court of Appeals.

Exercising the authority provided to it by NSPS legislation, DoD established the legal standard that administrative judges would use to modify DoD-imposed penalties during the initial appeal of cases.⁹ The proposed NSPS regulations provided that the judges would not modify DoD-imposed penalties unless those penalties were “wholly without justification.”¹⁰ The proposed NSPS regulations also specified that criterion for the review of cases by the full Merit Systems Protection Board, although the NSPS legislation had established a different set of criteria for that level in the appeals process.¹¹

DoD received comments from employees and labor unions expressing concern that, on the whole, the proposed regulations would limit due process rights of DoD's employees and diminish the authority of third parties (such as the board and arbitrators) to fully and fairly adjudicate adverse actions cases.

8. Specifically, the proposed regulations allowed employees a 15-day minimum advance notice of a proposed adverse action and a 10-day reply period to respond to charges specified in the notice. Under existing law, the advance notice is 30 days and the reply period is 7 days.

9. See 5 U.S.C. § 9902(h)(2) as added by Public Law 108-136 prior to amendment by Public Law 110-181.

10. National Security Personnel System, 70 Fed. Reg. 7552, 7568 (2005).

11. According to the NSPS legislation, the full MSPB could modify a DoD-imposed penalty if the board found the initial decision to be “arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with the law.” See 70 Fed. Reg. 7552 and 5 U.S.C. § 9902(h)(5) as added by Public Law 108-136 prior to amendment by Public Law 110-181.

Although employees and labor unions suggested that the notice period for adverse actions be extended, DoD decided to retain the 15-day period in its final NSPS regulations, noting that the regulations protect due process rights while still providing for a streamlined process. DoD also reiterated that the notice periods are minimum times and that local management may allow extensions on a case-by-case basis.

After employees and unions expressed concern that the “wholly without justification” standard for mitigating DoD-imposed penalties was too stringent, the final NSPS regulations adopted another standard (“totally unwarranted in light of the pertinent circumstances”), which DoD considered to be less strict.¹²

Commenters were also opposed to DoD’s review of administrative judges’ decisions and expressed concern that the appeals process would not be truly independent. Nevertheless, the final NSPS regulations retained those provisions. DoD noted that NSPS legislation allowed the department to establish an internal appeals process using adjudicators other than judges, but DoD chose to retain the judges in the interest of using existing and widely recognized institutions.¹³ According to DoD, because it bears full accountability for national security, it is best able to determine penalties for employees’ misconduct or poor performance. Nevertheless, DoD attempted to address the concerns about the process by agreeing that the review of judges’ decisions would take place in the Office of the Secretary of Defense rather than at the local level where the case originated.¹⁴

Because NSPS legislation established the standards for a full MSPB review of adverse actions cases, employees and unions argued that DoD did not have the authority to set its own more stringent standards. DoD agreed and made changes in the final NSPS regulations to reflect the standards for full MSPB review as provided in the NSPS legislation.¹⁵

Those procedures for adverse actions also apply to mandatory removal offenses (MROs)—offenses that the Secretary of Defense deems warrant a mandatory penalty of removal from federal service because they have a “direct and substantial adverse impact on the Department’s national security mission.”¹⁶ Although the proposed NSPS regulations did not include a list of MROs, they stipulated that future documents implementing the details of the system (the so-called implementing issuances) would identify such offenses in advance to all employees.¹⁷ Nonetheless, employees, unions, and other commenters objected. They expressed fears that removal could be too harsh a penalty for offenses that were not yet specified and that employees would not be given adequate notice of disciplinary action. DoD agreed, in principle, with the spirit of those concerns and shared a list of potential mandatory removal offenses with labor unions that participated in the meet-and-confer process.¹⁸ DoD retained the adverse actions procedures for MROs in the final NSPS regulations but included a requirement that a list of MROs be publicized via notice in the *Federal Register*.¹⁹

NSPS regulations on labor relations reduced the scope of collective bargaining over employment policies in relation to the extent of bargaining rights under existing law.²⁰ For instance, NSPS regulations broadened management rights by expanding the list of actions that management can take without collective bargaining. The regulations also reduced bargaining over the procedures DoD must follow when exercising its management rights and the “appropriate arrangements” that DoD must make for affected employees. According to DoD, it developed those regulations under the authority provided by the Congress in the NSPS legislation “to address the unique role that the Department’s civilian workforce plays in

12. Department of Defense and Office of Personnel Management, Department of Defense Human Resources Management and Labor Relations Systems (codified at 5 C.F.R. § 9901).

13. *Ibid.*

14. *Ibid.*

15. *Ibid.*

16. Although employees charged with such offenses are entitled to appeal the decision to the MSPB’s administrative judges, NSPS regulations preclude the judges from mitigating the removal penalty.

17. National Security Personnel System, 70 Fed. Reg. 7552 (2005).

18. Department of Defense and Office of Personnel Management, Department of Defense Human Resources Management and Labor Relations Systems.

19. *Ibid.*

20. The Civil Service Reform Act of 1978 establishes the collective bargaining rights of federal civilian employees, including those at the Department of Defense (see 5 U.S.C., ch. 71).

supporting the Department's national security mission."²¹ Employee unions opposed those regulations, arguing that DoD exceeded its statutory authority and that existing law already provided DoD with sufficient flexibility to handle emergencies.²²

On other specific matters, commenters (including unions) objected to the creation of the National Security Labor Relations Board. They claimed that an internal DoD review board would be influenced by management, unlike the independent Federal Labor Relations Author-

ity. According to their view, the impartiality of the board would be at risk because board members would be appointed by (and could be removed by) the Secretary of Defense. In the final NSPS regulations, DoD retained the NSLRB but agreed to give labor unions an opportunity to participate in the process for nominating board members. In addition, the Secretary of Defense will consider individuals nominated by unions for two nonchair positions on the board.²³ (The secretary's authority to remove board members is limited to standard causes like inefficiency, neglect of duty, and malfeasance in office.²⁴) DoD noted that using the NSLRB to adjudicate labor disputes instead of the FLRA helps ensure timely and efficient case management, as is required by the unique nature of the department's mission. DoD further noted that NSLRB decisions could still be appealed to the FLRA and the courts.

According to Public Law 110-181, none of the NSPS policies regarding adverse actions and labor relations procedures (including MROs) will be implemented, however. The legislation mandated that DoD revert to the relevant policies in preexisting law.

21. See 5 U.S.C. § 9902(m)(1) as added by Public Law 108-136 prior to amendment by Public Law 110-181.

22. On those grounds, unions filed suit against the Secretary of Defense and the Director of the Office of Personnel Management after DoD published the final NSPS regulations (see Department of Defense and Office of Personnel Management, Department of Defense Human Resources Management and Labor Relations Systems). In February 2006, the U.S. District Court accepted the unions' argument, in part, and directed DoD to stop implementing the parts of NSPS involving adverse actions, appeals, and labor relations (*American Federation of Government Employees v. Rumsfeld*, 422 F. Supp. 2d 16 (D.D.C. 2006)). In May 2007, the Appeals Court reversed the judgment of the District Court and upheld the NSPS regulations at issue (see *American Federation of Government Employees v. Gates*, 486 F. 3d 1316 (D.C. Cir. 2007)). After the Appeals Court's reversal, the unions requested a review of the reversal decision by the full Circuit Court of Appeals. That request was denied in September 2007 (*American Federation of Government Employees v. Gates*, 2007, U.S. App. LEXIS 21553 (D.C. Cir. Sept. 5, 2007) (per curiam)).

23. Department of Defense and Office of Personnel Management, Department of Defense Human Resources Management and Labor Relations Systems.

24. Those standards are similar to the FLRA's standards for removing members.

The Role of the Department of Defense's Components in Designing and Implementing the System

In 2004, the Secretary of Defense established a Program Executive Office to oversee the design and implementation of the National Security Personnel System and appointed the Deputy Secretary of Defense, Gordon R. England, as senior executive to provide overall direction.¹ But it is the Department of Defense's military departments and other organizations—as the direct employer of the affected workers—that are essential to the ultimate success of the system. The Congressional Budget Office examined the role those “components” played in designing NSPS and some of the issues they face in implementing it.²

Role in Designing the National Security Personnel System

In 2004, the PEO sponsored town hall meetings and focus group sessions for employees and supervisors (including military supervisors) at various sites in all of DoD's components to solicit their input on ways to modify the existing personnel system. The PEO also established working groups consisting of employees from the military departments, other DoD components, and the Office of Personnel Management. The working groups considered input from the meetings and focus groups in developing options for the new system.

1. A team of senior officials from the Department of Defense and the Office of Personnel Management advised both the senior executive and the PEO.
2. The components are the Department of the Army, Department of the Navy (which includes the Marine Corps), Department of the Air Force, Office of the Secretary of Defense, and other DoD agencies.

CBO's discussions with officials in DoD's components and its examination of documents provided by the PEO indicate that the various groups' deliberations benefited from the experience of demonstration projects and alternative personnel systems within DoD and the rest of the federal government. Those officials in DoD's components stated that they solicited ideas from employees at many levels and locations. In general, they characterize their role in designing NSPS as collaborative.

Conversion of Employees

As discussed in Chapter 1, about 472,000 union and nonunion white-collar employees are eligible for conversion to NSPS. The Department of Defense converted about 113,000 nonunion employees to NSPS in Spiral 1. The department expects to complete conversions under Spiral 2, consisting of an additional 75,000 nonunion white-collar employees, by December 2008. A vast majority of the remaining white-collar employees eligible for conversion at that time belong to unions.³ DoD's components had leeway to determine the rate at which to convert employees on the basis of their capabilities and needs. One factor that determined the speed of conversion was the capacity to provide training on NSPS topics (such as writing individual performance objectives) to employees and supervisors identified for conversion. That training capacity was, in turn, largely determined by the availability of funding. Because officials at DoD's components did not specifically request or budget for dedicated

3. It was reported in November 2008 that DoD would not seek to transfer its union employees to NSPS. See Stephen Losey, “NSPS Won't Include Union Employees,” *Federal Times* (November 2, 2008).

Box 5-1.**The Costs of Implementing the National Security Personnel System**

Implementation costs for the National Security Personnel System are incurred at two major levels: the various offices in the Department of Defense's components (where employees are actually converted to NSPS) and the NSPS Program Executive Office (which coordinated the design and implementation of the new system). The Congressional Budget Office (CBO) held discussions with officials at the DoD components to estimate NSPS implementation costs at that level. The results of the discussions indicated that those costs would be difficult to estimate because the activities on the design of NSPS and the conversion of employees were funded from existing resources. Had the DoD components instead received separate funding for those activities, the costs would have been easier to track and verify.

A significant portion of the components' direct costs of implementing NSPS was probably the time spent by employees who were diverted from their normal duties to instead work on NSPS-related activities. For instance, the DoD components assigned staff to the NSPS Program Executive Office to help design the new system. Also, employees at the DoD components attended various informational training sessions on NSPS and received more in-depth training on topics such as linking individual performance to organizational goals. In addition, the first group of employees converted to the system conducted a mock performance evaluation before their formal annual

appraisal. All those NSPS-related activities involved opportunity costs—the time that employees spent was no longer available for their normal duties. The DoD components and the NSPS Program Executive Office attempted to track the direct costs, such as those incurred in developing and disseminating training materials, but not the opportunity costs. The Congressional Budget Office was unable to independently verify the accuracy of DoD's records and estimate the salary costs of DoD employees who supported the design and ongoing implementation of NSPS.

As of November 2005, DoD projected the costs of implementing NSPS at about \$158 million from fiscal years 2005 through 2008.¹ That estimate included the following elements:

- Program implementation costs for all parts of the new human resources system—the costs associated with designing and implementing the system and the costs of setting up and operating the

1. That estimate does not include the initial payroll costs related to the conversion of employees to the new system, such as one-time pay adjustments upon conversion for the within-grade increase that employees would have earned to date (the so-called WGI buyout). See Department of Defense and Office of Personnel Management, Department of Defense Human Resources Management and Labor Relations Systems: Final Rule, 70 Fed. Reg. (2005).

Continued

funding for NSPS conversion, the funds for the training were provided from their existing resources. That treatment has made it difficult to track the costs of implementing NSPS, and the accuracy of DoD's reported costs remains doubtful.⁴ CBO was not able to independently verify the costs. (For more information on the costs of implementing NSPS, see Box 5-1.)

4. DoD requires its components to report their expenditures on NSPS to the PEO. Cost categories include design and implementation, training, automated systems, program office operations, and program evaluation.

DoD's components adopted different approaches concerning which employees were converted first. For example, the Department of the Air Force converted whole organizations or military bases first, whereas the Department of the Navy converted its human resources specialists and headquarters-type organizations first. Therefore, the employees the components have converted or identified for conversion so far are not a random or representative sample of total employees within each component. Of the 113,000 employees converted to NSPS in the first three spirals, 43,000, 20,000, and 41,000, respectively, are employees of the Department of the Army, Depart-

Box 5-1.**Continued****The Costs of Implementing the National Security Personnel System**

Program Executive Office.² Also included in this category are the costs of developing and delivering training to employees, conducting outreach to employees and others, collaborating with employee representatives, conducting evaluations of NSPS, and developing information technology modifications to personnel and payroll systems.

- The costs to establish the National Security Labor Relations Board. Those costs include the salaries of members and professional staff, as well as other costs associated with setting up a new organization. DoD intends to rely on existing infrastructure as much as possible to minimize the costs.

In March 2007, the NSPS Program Executive Office provided CBO with an updated cost estimate of \$165.8 million through fiscal year 2008.

The elements in DoD's estimate represent costs directly connected with implementing the new system. According to a report from the Government Accountability Office, however, DoD's estimate does not include the full costs that the agency is likely to incur in implementing NSPS. GAO concluded that although DoD's estimate includes some direct costs (such as the start-up and operations of the PEO as well as the development and delivery of NSPS training courses), other direct costs (such as the full salaries of military and civilian personnel who directly supported NSPS departmentwide) were not well-documented or included.³ GAO also found that the cost estimate does not account for any indirect

costs—such as operating and maintenance costs for buildings and general administrative services—associated with the development and implementation of NSPS. Moreover, GAO could not determine the total amount of funds DoD had expended or obligated on NSPS in 2005 and 2006, citing deficiencies in DoD's cost-reporting system and inadequate oversight.

In its revised NSPS regulations published in the *Federal Register* in May 2008, DoD estimated that the overall costs associated with continuing to implement the system will be \$143 million from 2009 through 2011.⁴ Information that would allow a determination of whether that latest estimate addressed the problems with previous ones was not available to CBO.

In a more recent report, GAO states that, according to the NSPS Program Executive Office, each DoD component took actions to address concerns about oversight of the process for reporting costs. For example, the Army established new account processing codes that comply with NSPS reporting categories and provided for an independent review to determine whether the Army's Major Commands are meeting established internal procedures for tracking, capturing, and reporting NSPS implementation costs in specific categories. In addition, the other components (the Navy, the Office of the Secretary of Defense, and other DoD agencies) have taken steps to improve the accuracy of the NSPS implementation costs they report.⁵

2. The Program Executive Office consisted of 12 people as of November 2005.
3. For more information, see Government Accountability Office, *DoD Needs Better Internal Controls and Visibility over Costs for Implementing Its National Security Personnel System*, GAO-07-851 (July 2007).

4. See National Security Personnel System: Proposed Rule, 73 Fed. Reg. 29882 (May 22, 2008), codified at 5 C.F.R. 9901.
5. For more details, see Government Accountability Office, *Human Capital: DoD Needs to Improve Implementation of, and Address Employee Concerns About, Its National Security Personnel System*, GAO-08-773 (September 2008).

ment of the Navy, and Department of the Air Force. Another 8,600 employees work in the Office of the Secretary of Defense or for other DoD agencies.

Linking Individual Employees' Performance Objectives to Organizational Missions

The NSPS performance management process explicitly incorporates the legal requirement that it be linked to "the agency's strategic plan."⁵ As such, that process directed that individual performance expectations be aligned with the Department of Defense's mission, strategic goals, and organizational objectives.⁶

The PEO and DoD's components communicated that requirement to employees and supervisors and provided instructions on how it might be accomplished. The basic approach is to begin with higher-level objectives and cascade down to lower-level ones—and, ultimately, to individual job objectives for each position. According to DoD officials, employees identified for conversion to NSPS and their supervisors received training on how to accomplish that task and carried out a trial-run performance evaluation process. During discussions with CBO, DoD officials indicated that engaging employees in that exercise produced a side benefit: Employees gained a better understanding of their duties and the role they play in the organization.

5. 5 U.S.C. § 9902(b)(7).

6. Department of Defense, *Civilian Personnel Manual*, DoD 1400.25-M, subchapter 1940.

So far, employees converted under Spiral 1.1 have undergone two performance appraisal cycles (for 2006 and 2007); those converted under Spirals 1.2 and 1.3 have undergone one performance appraisal cycle. On the basis of that limited information, CBO is unable to determine how effectively individual performance objectives were linked to organizational objectives. However, a review of the documentary resources DoD's components provided to supervisors and employees suggests that the linking might be difficult to achieve. The reference documents reviewed include the President's Management Agenda, the Quadrennial Defense Review, and the National Defense Strategy.⁷ Service-specific and lower-level organizational missions and objectives are derived from the departmentwide goals stated in those documents.

Typically, those departmentwide and organizational objectives are stated in terms that are probably too broad to allow for a straightforward connection to the duties and responsibilities of individual jobs. In discussions with CBO, officials in DoD's components indicated that, other than using common instructions and documentary references, the effort to link individual job objectives to organizational goals was decentralized within each component.

7. The President's Management Agenda is intended to improve the effectiveness and efficiency of the U.S. government. Announced by President George W. Bush in 2001, the PMA evaluates and scores the operations of federal agencies in five areas, such as financial accountability and budget-performance integration. The Quadrennial Defense Review analyzes U.S. strategic objectives, potential military threats, defense strategy, and military force structure.

Has the National Security Personnel System Achieved Its Goals to Date?

In large part, the Department of Defense designed the National Security Personnel System to avoid the perceived disadvantages of the traditional General Schedule system. The changes in NSPS were designed to increase management flexibility in hiring and compensating employees, increase management flexibility with adverse actions and labor relations issues, and motivate effective work.

Because of the legal dispute between DoD and employee unions concerning the labor relations and adverse actions elements of NSPS, DoD began implementing only the job classification, performance management, and staffing elements of the system for its nonunion employees. Eventually, Public Law 110-181 reinstated adverse actions, appeals, and labor relations policies under existing civil service law. That decision did not substantially affect the other elements of NSPS, which DoD continues to implement.

Given that NSPS implementation is ongoing, sufficient data do not yet exist to enable the Congressional Budget Office to determine precisely what success NSPS has had to date in achieving its intended objectives.¹ Nonetheless, CBO used available data to identify evidence linking key changes in the system to the achievement of DoD's

underlying goals. The findings presented in this chapter are preliminary. For CBO to more completely evaluate the system, DoD would need to collect additional information.

Increased Management Flexibility in Hiring and Compensating Employees

Compared with the GS system, NSPS makes changes in the hiring process and the way in which jobs are classified and compensated.

Hiring

NSPS aims to improve flexibility in hiring employees by giving DoD direct control over new hiring authorities and by simplifying the rules for defining jobs and hiring new workers. Those changes should reduce the time it takes to hire new employees. The new hiring authorities should enable DoD to more rapidly fill job vacancies, including those for hard-to-fill jobs that require exceptional educational or similar qualifications. As a result, vacancy rates should decrease over time. If DoD wanted to monitor the timeliness of its employment process, it could collect data on the number of days that elapse from the time a human resources office is notified of a vacancy to the date an offer is made to a job candidate.

Compensation

One of the key changes in NSPS is pay banding. While not an end in itself, pay banding aims to improve DoD's flexibility in compensating its employees and to motivate effective work.

Federal agencies have been experimenting with pay banding and new performance management approaches since the 1980s. At that time, the Department of Defense set up demonstration projects (approved by the Office of

1. In its consideration of unions' challenges to specific parts of the NSPS appeals process, the Circuit Court of Appeals for the District of Columbia essentially reached the same conclusion when it decided that those challenges are not yet ready for judicial review. The unions' lawsuit specifically challenged that the appeals process standard that precluded administrative judges under the Merit Systems Protection Board from mitigating a DoD-imposed penalty does not meet legal standards for "fair treatment." In its decision, the Appeals Court stated that because it does not yet know how the Secretary of Defense would choose to apply those particular regulations in specific cases, it has no concrete factual context in which to consider the challenges.

Personnel Management) at two naval research and development laboratories, in China Lake and San Diego, California.² Over the years, OPM approved a total of 17 demonstration projects, many of which implemented pay bands and pay-for-performance systems.³

Pay banding began to take hold in the private sector during the early 1990s.⁴ Many of the companies that first implemented pay banding did so to create greater organizational flexibility and to support a new and flatter organizational structure.⁵ Pay banding further evolved in the private sector into “career banding.” That system emphasizes skill development and career development by rewarding employees for acquiring specific skills and competencies.

In NSPS, DoD created three to four pay bands within four pay schedules for four career groups. (See Figure 6-1 for a depiction of the pay bands and associated minimum and maximum salaries for the standard career group—the largest career group in terms of the number of employees covered when NSPS is fully implemented. Appendix C presents the pay banding structure for all four career groups.)⁶ The pay ranges in many pay bands are identical across career groups and, for the most part, correspond directly to a range of GS grades.⁷ The ranges of pay in the bands involve maximum rates that are up to 168 percent higher than the minimum rates (see Table C-1 in Appendix C).⁸

The wider pay ranges in the bands contrast with the narrower ranges in the GS grades. Salaries in each GS grade have a range of 30 percent; grades are divided into 10 steps, each of which represents a 3 percent increase in salary. Advancement through the grades in the traditional

GS system is automatic and depends mostly on tenure. That approach suited proponents of that system, who were concerned that the process for determining pay advancement be clear, understandable, and free from bias. Opponents of that system have sought ways to link pay to performance and reward employees with superior performance by advancing them through the system more quickly. Pay banding is viewed as an opportunity to introduce such a system. Because of its greater range between minimum and maximum pay rates, pay banding could achieve wider variation in pay than the traditional system.

Some Advantages of Pay Banding. Pay banding could help improve the way DoD pays its employees and manages their careers. Potential advantages of pay banding include the following:

- Pay banding could provide DoD with greater flexibility to make pay decisions on the basis of local job market conditions. For instance, if market conditions warrant, new hires could be paid higher starting salaries without necessarily placing them in a higher job classification. In addition, DoD could more easily target general increases in pay (the minimum and maximum salaries in a pay band as well as local market supplements) to specific occupations, unlike the GS system in which adjustments to pay rates apply to all occupations.
- If properly designed, pay banding could provide a way to recognize dual career tracks and enhance job mobility. In the NSPS pay banding structure, each career group has pay bands for professional-type jobs and roughly parallel pay bands for management jobs (see Figure 6-1 and Table C-1). The three pay bands for professional/analytical jobs in NSPS’s standard career

2. Title VI of the Civil Service Reform Act of 1978 allows federal agencies to experiment with alternative personnel systems under waivers granted by the Office of Personnel Management.

3. Those include demonstration projects in DoD (China Lake and Acquisition Workforce) and in other federal agencies, such as the Department of Commerce.

4. Kenan S. Abosch and Janice S. Hand, *Broadbanding Design, Approaches, and Practices* (report prepared by Hewitt Associates for the American Compensation Association, 1994), p. 4.

5. *Ibid.*, p. 13.

6. In addition to the pay amounts listed in Figure 6-1 and Table C-1, employees receive adjustments, applied as percentages of base pay, to reflect market conditions in specific locations (so-called “local market supplements”) and for certain occupations.

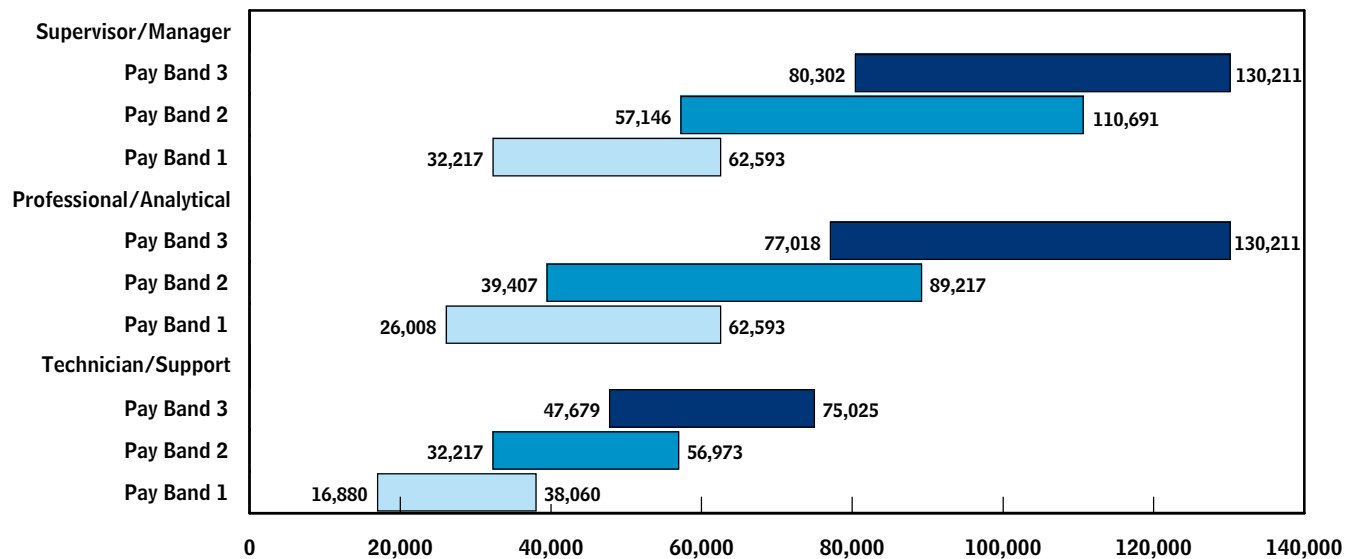
7. For example, the minimum and maximum rates of pay in Pay Band 1 in the professional/analytical pay schedule of the standard career group roughly correspond to GS Grade 5/Step 1 and Grade 11/Step 10, respectively. That approach implicitly accepts the validity of the GS grades as a basis of compensating the many occupations that map into the same GS grade but may have different pay rates in the private sector. For instance, an economist and an engineer might be in the same GS grade in the federal government, yet those occupations may command private-sector salaries that are very different from each other and from the government pay level.

8. That range excludes pay bands for developmental positions (the “student” pay schedule).

Figure 6-1.

Annual Base Salary Ranges for Pay Bands in the Standard Career Group, January 2008

(2008 dollars)



Source: Congressional Budget Office based on data from Department of Defense, National Security Personnel System Program Executive Office.

Note: The student category is excluded.

group, for instance, have salaries with a combined range of \$26,008 per year to \$130,211 per year. Similarly, pay bands for supervisor/manager jobs in the same career group have salaries with a combined range of \$32,217 per year to \$130,211. That arrangement allows high-performing employees in professional jobs who wish to remain in such jobs to do so and be rewarded with higher salaries without moving to managerial positions. Employees would serve in jobs for which they are comparably better suited, thus enhancing the productivity of the workforce. In a more general sense, pay banding could also allow freer movement across a range of job opportunities because employees would not be bound by narrowly described work definitions.

- Pay banding could allow for pay progression to be linked to organizational goals and missions when movement through the bands is tied to performance.
- Pay banding could simplify salary administration. The wider pay range provides greater flexibility to reward a particular outstanding employee without compelling that employee to compete for a position at a higher grade.

Some Disadvantages of Pay Banding. The potential disadvantages of pay banding include the following:

- Payroll costs could increase considerably because the spread between the minimum and maximum salaries is larger in pay banding than in a narrower grade structure, such as the GS system. Employees could quickly advance within the pay bands to salary levels higher than their market value. That situation could be exacerbated by a relatively lenient performance evaluation process, leading to “band drift.”⁹ Additional resources or tools would be needed to monitor the pay structure to control costs.
- Pay banding could raise questions about fairness and increase the burden of oversight. Differences in the rigor of performance appraisals across work units could lead to employees’ moving through a pay band at different rates. That situation could ultimately

9. Even some underperforming employees could experience considerable salary growth over time. If an employee underperforms in one or two years and later performs well, for example, supervisors may be inclined to increase that employee’s salary to the level of his or her peers who have consistently performed well.

increase the chance of a wide divergence in salaries among apparently similar individual employees or categories of employees and might lead to allegations of pay discrimination or charges of violation of the principle of equal pay for equal work. Reducing the chances of allegations like those requires that the pay system be designed and executed in a transparent and credible manner and that pay progression in the workforce be monitored continually.

- Pay banding could reduce the ability to use the compensation system as a tool for determining relationships between jobs. Because jobs are lumped together and pay levels in a band are tied to the individual and not the job per se, the distinguishing characteristics of jobs could disappear.

One federal agency that switched its compensation system from broader pay bands back to a structure with more steps is the Office of Federal Housing Enterprise Oversight (OFHEO). After nine years of experimentation with seven broad pay bands, the agency switched to a structure with 18 pay grades in 2002 to provide employees with more opportunities for promotion and to control costs.¹⁰ According to the agency's officials, employees moved quickly through the pay bands, reaching pay levels beyond their market value when compared with employees in similar financial institutions. OFHEO's officials viewed employees in that situation as overcompensated. The officials also stated that even though the pay bands offered greater opportunities for pay raises within the same job classification, the structure did not provide a sufficient career ladder. Employees wanted more vertical promotion.¹¹

Such band drift is not unavoidable, however. Previous research indicates that evidence of salary cost growth in personnel demonstration projects or alternative personnel systems with pay banding is mixed—some agencies experienced higher salary cost growth compared with a comparison group of traditional GS employees, whereas others experienced slower cost growth. For example, the

General Accounting Office reported that average salaries in DoD's China Lake alternative personnel system increased about 4 percentage points (cumulatively) more than the increase in a comparison group during the first five years of that system.¹² Average salaries at the National Institute of Standards and Technology were about 9 percentage points higher than comparable GS salaries in the first five years of that agency's alternative personnel system. But other organizations, such as DoD's Naval Research Laboratory, Naval Sea Systems Command Warfare Centers (Dahlgren, Virginia), and Naval Sea Systems Command (Newport, Virginia), experienced about 3 percent slower rates of salary increase relative to a comparison group over the first three years of their demonstration projects.

To control salary cost growth, some of those personnel systems directly manage employees' movement through a pay band, thereby preventing salary migration to the top end. For example, some systems award larger pay increases in the lower end of a pay band and smaller pay raises at the higher end; others require increasingly higher minimum performance ratings at greater pay band levels before awarding pay raises.¹³ Another way to control salary cost growth is to reward performance through a mix of lump-sum bonuses and salary increases, as DoD currently does. Unlike salary increases, bonuses are awarded one year at a time, do not compound over time, and do not count toward an employee's life insurance or retirement benefits. Discussions with DoD officials indicated that the agency's components have some leeway in granting performance awards. For example, some components set "control points" within a pay band, delineating salary levels beyond which employees are more likely to receive one-time awards than equivalent permanent pay increases. NSPS's approach of allocating a fixed amount to pay pools and distributing the funds to employees on the basis of the shares they receive in their performance appraisal is another way to control salary cost growth.

Motivating Effective Work

The performance management system in NSPS is intended to "promote a performance culture in which the

10. See Karen Rutzick, "Agency Decides Pay Banding Is Not the Answer," *Government Executive* (September 30, 2005), www.govexec.com/dailyfed/0905/093005r1.htm.

11. In contrast, employees in DoD's science and technology laboratory demonstration project, which converted to pay banding and pay for performance between 1997 and 2001, reported satisfaction with advancement within pay bands.

12. See General Accounting Office, *Human Capital: Implementing Pay for Performance at Selected Personnel Demonstration Programs*, GAO-04-83 (January 2004).

13. Ibid.

performance and contributions of DoD's civilian workforce are more fully recognized and rewarded.”¹⁴ To that end, the system requires that individual performance measures be linked to organizational objectives. Because elements of the system are relatively new to many DoD organizations, they may not yet have in place effective processes for measuring and evaluating employees' performance in that way. In this section of its analysis, CBO examines some conditions that affect the likelihood that the performance management system in NSPS will meet its intended objectives.

Measuring and Appraising Performance

The performance of employees under the General Schedule system is evaluated against standards that describe the main responsibilities of each job.¹⁵ Performance evaluations in NSPS essentially take the same approach. In both systems, employees and their supervisors develop the job or performance objectives for their position. However, NSPS provides new standardized descriptions of “performance indicators” and “contributing factors” used in performance appraisals. Performance indicators provide general descriptions of work at various levels of performance.¹⁶ Contributing factors emphasize behaviors that are essential to accomplishing job objectives, and those factors are used to evaluate how employees accomplish their work.¹⁷ For each contributing factor, benchmark descriptors define both the “expected” and “enhanced” performance levels for each pay schedule and pay band.¹⁸ Supervisors assess employees' performance against the standards described in the benchmark descriptors.

Before converting employees to the new system, DoD provided training on NSPS's performance management system, covering topics such as writing effective job objectives and aligning them with higher-level organizational objectives. In addition, the first wave of employees converted to the new system (Spiral 1.1) carried out a mock performance evaluation process in preparation for the actual performance evaluation. That process indicated to DoD that it needed to bolster employees' and supervisors' skill in writing job objectives and accomplishments. Consequently, DoD developed a one-hour course and a self-paced Web-based tool (called iSuccess) to assist employees in writing effective job objectives and self-assessments.¹⁹

Information on specific performance plans (including job objectives and contributing factors) for DoD's employees converted to NSPS was not available to CBO. There are, however, some general guidelines for developing performance objectives, which CBO examines next.

Guidelines for Developing Performance Objectives

Developing individual performance objectives depends on the existence of good measures. That task is probably more difficult for complex jobs than for less complex ones. To channel work effort in the right direction, all activities that are important for effective job performance should be included in the list of performance objectives used to evaluate employees. Researchers have pointed out that employees tend to devote disproportionate effort to job activities included in their performance evaluations, negatively affecting overall job performance when relevant job aspects are excluded.²⁰ For some positions, though, determining objective, quantitative measures of performance is difficult. The guidelines DoD provided to

14. See Department of Defense and Office of Personnel Management, Department of Defense Human Resources Management and Labor Relations Systems: Final Rule, 70 Fed. Reg. (2005).

15. The Position Description document describes each job's main tasks.

16. For example, in Pay Band 1 of the professional/analytical pay schedule, a performance indicator at level 3 (valued performer) is stated as “with guidance, organized and prioritized own tasks to deliver the objective, adjusting work plans and overcoming obstacles as necessary.” A corresponding performance indicator at level 5 (role model) is stated as “contributed results beyond what was expected; results were far superior in quality, quantity, timeliness and/or impact to the stated objective.”

17. Communication, technical proficiency, and cooperation and teamwork are among the seven contributing factors evaluated in NSPS.

18. Under the “technical proficiency” contributing factor for Pay Band 2 of the professional/analytical pay schedule, for example, employees are expected to apply “substantive knowledge and skills ... to independently perform a full range of assignments” Transitioning from the “expected” to the “enhanced” level for the same pay band and pay schedule requires that employees apply “depth and breadth of knowledge to independently perform well on the most complex or varied assignments at this level.”

19. More details on iSuccess are available at www.cpms.osd.mil/nsps/isuccess.html.

20. For example, see Edward E. Lawler III, *Pay and Organization Development* (Reading, Mass.: Addison-Wesley, 1981). Examples include salespeople who emphasized sales at the expense of long-term customer relations.

employees encourage them to use quantitative measures. To the extent that this is not done or is not possible, however, employees and supervisors must use subjective measures. While using subjective measures is not necessarily undesirable, a certain level of trust between employees and supervisors should be present for employees to believe that pay is fairly based on performance under those circumstances.

The five-point rating system in NSPS requires supervisors to make some judgments when evaluating employees. In deciding which rating an employee has earned—unacceptable, fair, valued performer, exceeds expectations, or role model—supervisors must use contributing factors to assess how an employee has accomplished his or her work. For contributing factors like “critical thinking,” supervisors must determine whether the employee’s work behaviors were at the “expected” or “enhanced” level relative to established benchmarks. Such appraisal processes that require supervisors to make judgments are common in the private sector. According to research results, supervisor-subordinate relationships have worsened because of an appraisal in fewer than 10 percent of the cases.²¹ Nevertheless, openness, trust, and good communication on the part of both employees and supervisors are essential for the effectiveness of such processes.

Performance objectives can be set at the individual or group level. Jobs for which tasks are independent of other jobs might be well suited to individual-level performance objectives, as stipulated under NSPS. Individual-level appraisals in appropriate situations have the advantage of clearly linking individual performance and rewards. Group-level performance measures might be more appropriate in cases in which jobs are interdependent or jointly produce output. In those situations, cooperation and teamwork essential to overall performance might be undermined by individual-level performance measures.²² That consideration applies to performance appraisals in the traditional GS system as well.

Performance Distinctions and Pay Raises

For pay-for-performance systems to be effective, performance appraisals must make meaningful distinctions in employees’ performance and tie greater rewards to higher levels of performance.²³ Employees’ motivation to perform is increased when they know that their hard work will be recognized and rewarded relative to those who do not perform well.

To examine how effectively NSPS’s pay-for-performance process has met those criteria, CBO obtained and analyzed data from the performance ratings and associated compensation for employees converted to the system in the first three spirals. The Department of Defense evaluated the performance of those employees at the end of 2007 and paid out performance-based pay raises and bonuses in January 2008.²⁴ The data covered about 102,000 employees.

Those NSPS data were compared with 2002 data from personnel systems at China Lake, Naval Sea Systems Command (NAVSEA), and the Department of Commerce (see Figure 6-2).²⁵ The data show a significant

23. See Lawler, *Pay and Organization Development*; Beth J. Asch, *Designing Military Pay: Contributions and Implications of the Economics Literature*, MR-161-FMP (Santa Monica, Calif.: RAND Corporation, 1993); and Paul F. Hogan and others, *Conceptual Framework for Analyzing and Developing a Compensation System* (report prepared by Lewin-VHI, Inc., for the 8th Quadrennial Review of Military Compensation, February 1995).

24. Those performance-based pay raises and bonuses are separate from the general adjustments to pay bands and increases in local market supplements. As discussed in Chapter 3, only employees with a rating of 3 (valued performer) or higher receive performance-based increases in base pay and bonuses.

25. The performance evaluation data for China Lake, NAVSEA, and the Department of Commerce come from General Accounting Office, *Human Capital: Implementing Pay for Performance at Selected Personnel Demonstration Programs*. At the time of GAO’s analysis, 2002 was the most recent year for which performance evaluation data for those organizations were available. NAVSEA, a DoD organization, is part of the Defense Laboratories Demonstration Project that began in the late 1990s. Although the NSPS legislation originally excluded employees at certain DoD laboratories from NSPS until after October 1, 2008 (an exclusion that was extended under Public Law 110-181 to October 1, 2011), the legislation leaves the conversion of employees in the DoD laboratories after the exclusion period ends to the discretion of the Secretary of Defense so long as the flexibilities provided by NSPS are greater than the flexibilities provided under the existing demonstration project.

21. Ibid.

22. The fact that the NSPS performance management system dictates that supervisors consider cooperation and teamwork as contributing factors when evaluating individual performance might help address that concern.

variation in the extent to which those organizations differentiate employees' performance. For instance, at least 40 percent of employees in NAVSEA and the Department of Commerce received the highest performance rating, while 5.1 percent of NSPS employees and 11 percent of employees in China Lake received a similar rating. The percentage of employees receiving above-average ratings (the first two categories) ranges from 42 percent in NSPS to 87 percent in the Department of Commerce. A greater proportion of NSPS employees (56 percent) were rated "average" or "acceptable" than were employees at the other organizations (13 percent to 44 percent).

Virtually no employees at any of the organizations received an unsatisfactory performance rating. The fact that a majority (or, in some cases, a vast majority) of employees are rated acceptable or better and practically no employees are rated unacceptable in those non-GS personnel systems may be an accurate reflection of the employees' performance. Or there could be some other explanation. One of the main criticisms of the GS system is that it does not sufficiently identify poor performers. It is noteworthy that the distribution of ratings in the non-GS personnel systems likewise does not reveal a significant number of poor performers.

The rewards attached to the ratings represent another dimension of performance distinctions with important effects on employees' motivation. In general, employees' motivation to perform is enhanced when higher ratings garner larger pay raises. CBO analyzed pay raise data associated with the same performance rating categories discussed above.²⁶ The data show that employees with higher ratings received larger percentage increases in base pay, on average, than employees with lower ratings. For example, NSPS employees with the highest rating received a 6.6 percent increase in base pay, compared with 4.5 percent for employees with the next highest rating (see Figure 6-2). The same pattern of pay raises occurred for employees at China Lake, NAVSEA, and the Department of Commerce. The difference in the average pay raise awarded to employees receiving one rating instead of the next lower rating is about 2 percentage points for NSPS employees. For employees at China

Lake, NAVSEA, and the Department of Commerce, the difference is 1 to 2 percentage points.

Employees' Attitudes Toward NSPS

Organizations typically seek employees' support when making significant changes that affect work life, such as implementing a new personnel system. Employees' support affects both the smoothness of the transition to, and the ultimate success of, a new system. According to DoD, many NSPS regulations are intended to simplify human resources processes and improve opportunities for job assignments and career growth.

To gain an insight into employees' support for NSPS, CBO obtained and analyzed data from surveys of DoD's civilian employees and supervisors on their attitudes toward the system.²⁷ Those surveys included questions about DoD's civilian employees' awareness of, views on, and potential concerns about key elements of NSPS. Because NSPS is still being implemented, the available data provide preliminary indications of employees' attitudes toward the system.

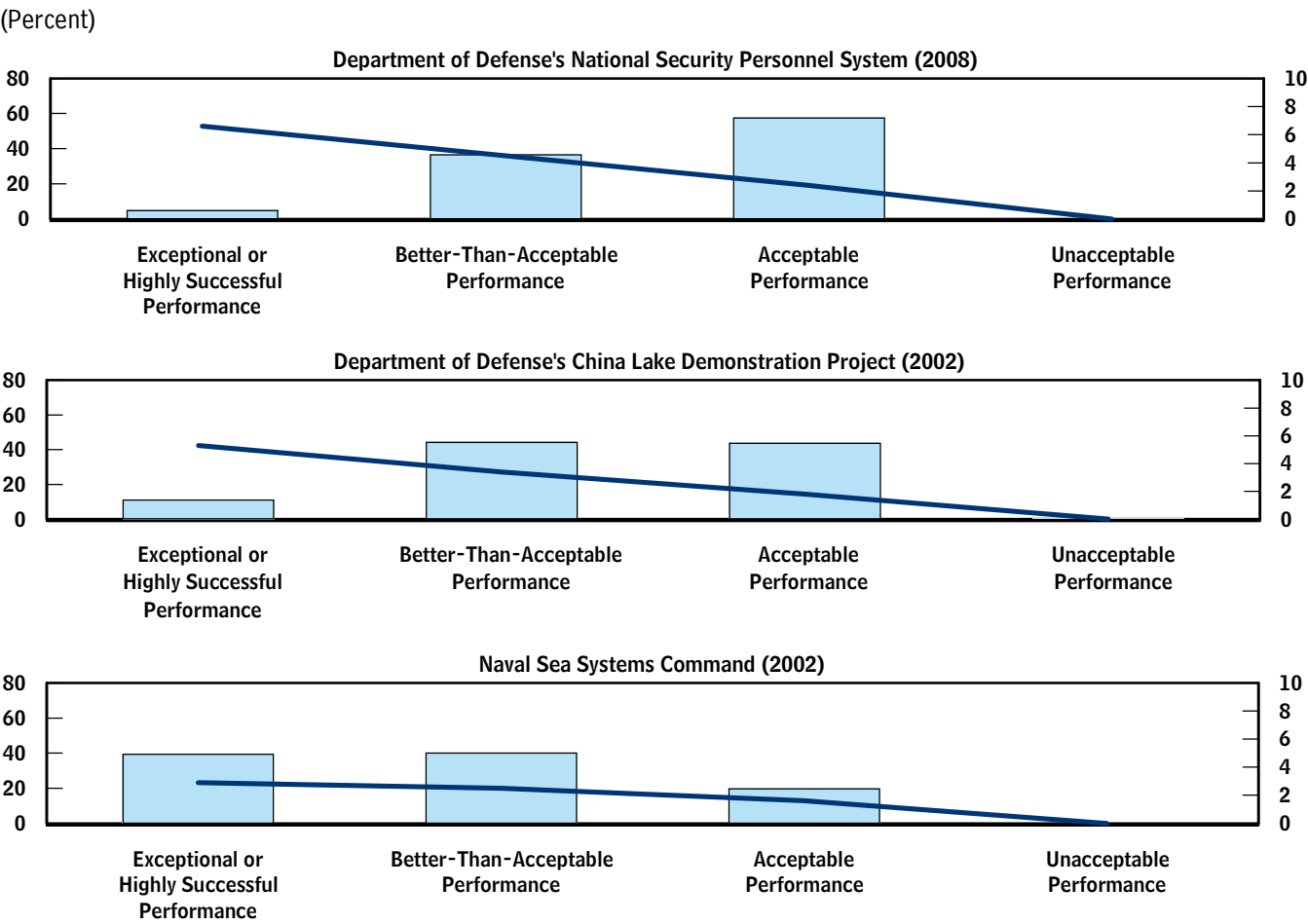
The results of CBO's analysis suggest that approximately half of DoD's employees were neutral about NSPS, and the remaining employees were about equally split between favorable and unfavorable opinions of the new personnel system.²⁸ The results also show that performance management issues could be a source of concern.

27. The data are from the Status of Forces Surveys (SOFS), a component of DoD's Human Resource Strategic Assessment Program (HRSAP) administered by the Defense Manpower Data Center. HRSAP is designed to measure the attitudes and opinions of the DoD community (active-duty and reserve service members, their families, and DoD's civilian employees) on a wide range of personnel issues. Survey questions about NSPS for DoD's civilian employees first appeared in the SOFS in October 2004. CBO obtained the survey data from that date through the most recent survey in May 2007; the latter data included responses from DoD's civilian employees as a whole and for a subset consisting of those employees converted to NSPS in Spirals 1.1, 1.2, and 1.3.

28. Employees' views could improve over time. For example, an average of 51 percent of employees in the Navy's China Lake demonstration project favored their new personnel system in the first five years of the system (between 1979 and 1983). By 1998, that percentage had increased to 71. Similarly, the percentage of employees favoring a group of demonstration projects at DoD laboratories patterned after the China Lake project increased from 34 percent in 1996 to 55 percent in 2001. For more details, see Office of Personnel Management, *Summative Evaluation 2002: DoD S&T Reinvention Laboratory Demonstration Program* (2002).

26. Pay raise data are a subset of data on performance ratings because some employees did not receive salary increases. For example, employees with "unacceptable" performance ratings did not receive pay increases, nor did other eligible employees who separated from DoD before the payout date of January 7, 2007.

Figure 6-2.
Performance Ratings and Associated Pay Raises for Employees in the National Security Personnel System and in Selected Pay-for-Performance Systems in the Federal Government



Continued

In the five surveys that DoD administered between October 2004 and May 2007, about 31 percent of the employees who had not been converted to NSPS, on average, agreed or strongly agreed that NSPS *will* improve personnel processes. Those specific processes are hiring new employees, disciplining or correcting poor work performance, linking pay to performance, rewarding good work performance, classifying jobs, improving communication between employees and supervisors, and ensuring that individual performance supports organizational missions (see Figure 6-3).²⁹ When asked in May 2007 whether they thought NSPS *had* improved those personnel processes, 23 percent of employees converted

to NSPS under Spirals 1.1 to 1.3 agreed or strongly agreed.³⁰

Among employees who had been converted to NSPS by May 2007 and their supervisors, 15 percent thought that NSPS, overall, is better or much better than the

29. Another 26 percent of employees disagreed or strongly disagreed that NSPS will improve those personnel processes; the remaining 43 percent of employees neither agreed nor disagreed.

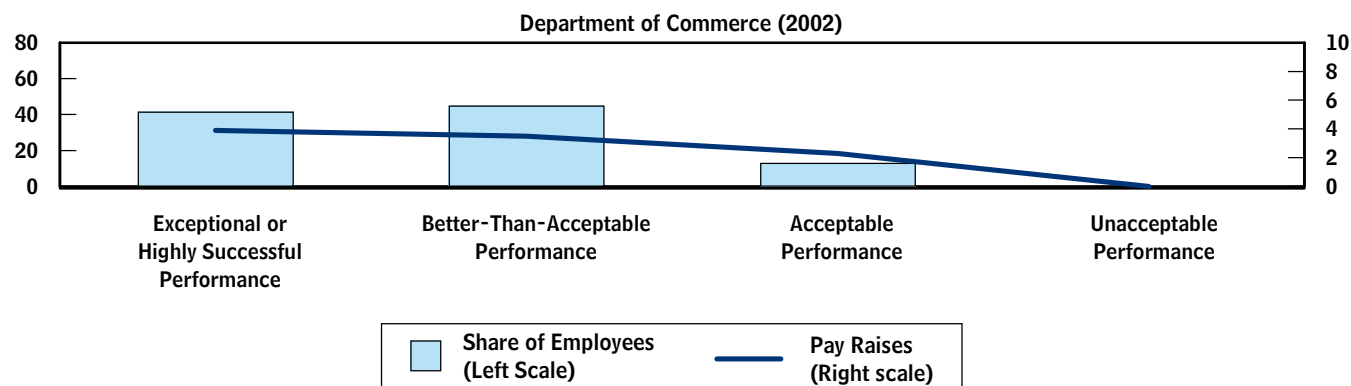
30. Thirty percent of employees disagreed or strongly disagreed that NSPS had improved those personnel processes. About 47 percent had neutral views.

Figure 6-2.

Continued

Performance Ratings and Associated Pay Raises for Employees in the National Security Personnel System and in Selected Pay-for-Performance Systems in the Federal Government

(Percent)



Source: Congressional Budget Office based on data from Department of Defense, National Security Personnel System Program Executive Office; and General Accounting Office, *Human Capital: Implementing Pay for Performance at Selected Personnel Demonstration Projects*, GAO-04-83 (January 2004).

Notes: NSPS = National Security Personnel System; NAVSEA = Naval Sea Systems Command; DOC = Department of Commerce.

The top rating for each organization is as follows: NSPS, "role model" (numerical rating of 5); China Lake, "highly successful" (numerical rating of 1); NAVSEA, exceptional contributor; DOC, scores between 90 and the maximum of 100.

The second-highest rating for each organization is as follows: NSPS, "exceeds expectations" (numerical rating of 4); China Lake, "highly successful" (numerical rating of 2); NAVSEA, major contributor; DOC, scores between 80 and 89.

Ratings for an acceptable level of performance are as follows: NSPS, "valued performer" (numerical rating of 3) and "fair" (numerical rating of 2); China Lake, "fully successful" (numerical rating of 3); NAVSEA, contributor; DOC, scores between 40 and 79.

Bottom ratings are as follows: NSPS, "unacceptable" (numerical rating of 1); China Lake, "less than fully successful" (numerical ratings of 4 and 5); NAVSEA, unacceptable; DOC, scores of less than 40.

previous personnel system (see Figure 6-4).³¹ For selected personnel processes—such as hiring employees, setting pay levels, and disciplining employees—the share of NSPS employees and their supervisors who thought that NSPS is better or much better than the previous personnel system was 14 percent, on average.³²

The employees converted to NSPS are not a random sample of all of DoD's employees—for instance, they were selected on the basis of occupation and location.

Therefore, the survey findings for that group may not apply to the rest of DoD's employees. However, the findings could portend unfavorable views about personnel processes under NSPS.

Also according to the survey results, employees are more concerned about issues related to the performance management system in NSPS than the other elements of the system. They most frequently indicated that communicating performance expectations, making fair personnel decisions, and motivating employees to perform well are among the most important skills for supervisors under NSPS; fewer indicated skills such as communicating effectively with people of diverse backgrounds or counseling employees on their career (see Figure 6-5). The proportion of employees who thought that communicating performance expectations is the single most important skill for supervisors under NSPS increased sharply among employees converted to NSPS under Spirals 1.1 to 1.3

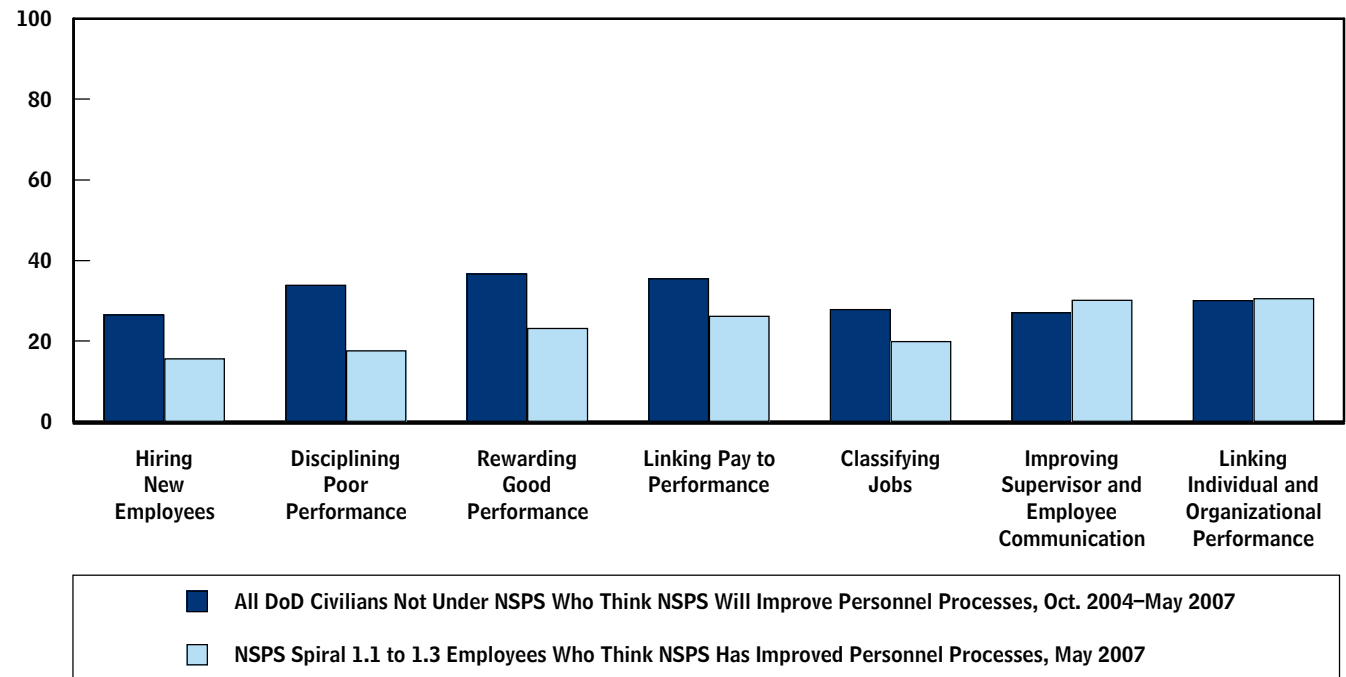
31. About 38 percent of employees thought NSPS is worse or much worse than the previous personnel system. About 46 percent of the employees thought NSPS, overall, is neither better nor worse.

32. For those selected personnel processes, about 22 percent of employees thought that NSPS is worse or much worse than the previous personnel system. Sixty-three percent had neutral views about NSPS compared with the previous personnel system.

Figure 6-3.

Share of Civilian Employees in the Department of Defense Who See Actual or Potential Improvement from the National Security Personnel System

(Percent)



Source: Congressional Budget Office based on data from Defense Manpower Data Center, *Status of Forces Survey of DoD Civilians*, selected quarters from October 2004 through May 2007.

Notes: This figure shows the percentage of civilian employees in the Department of Defense (DoD) not yet converted to the National Security Personnel System (NSPS) who agree or strongly agree that NSPS will improve selected personnel processes and the percentage of converted DoD civilians who agree or strongly agree that NSPS has so far improved those personnel processes.

Labels for survey response categories are paraphrased from actual survey response text.

compared with the rest of DoD's employees. Correspondingly, more employees stated that the most important training they would like to receive would be on the performance management system rather than other subjects, such as labor relations and adverse actions and appeals (see Figure 6-6).

During the public comment period on the proposed NSPS regulations, some employees expressed opinions that NSPS's performance management process could lower morale and that supervisors might not be able to apply performance standards fairly. According to DoD documents, the department is putting measures in place to ensure that the performance management system functions properly. Those measures include training supervisors to provide candid and constructive feedback

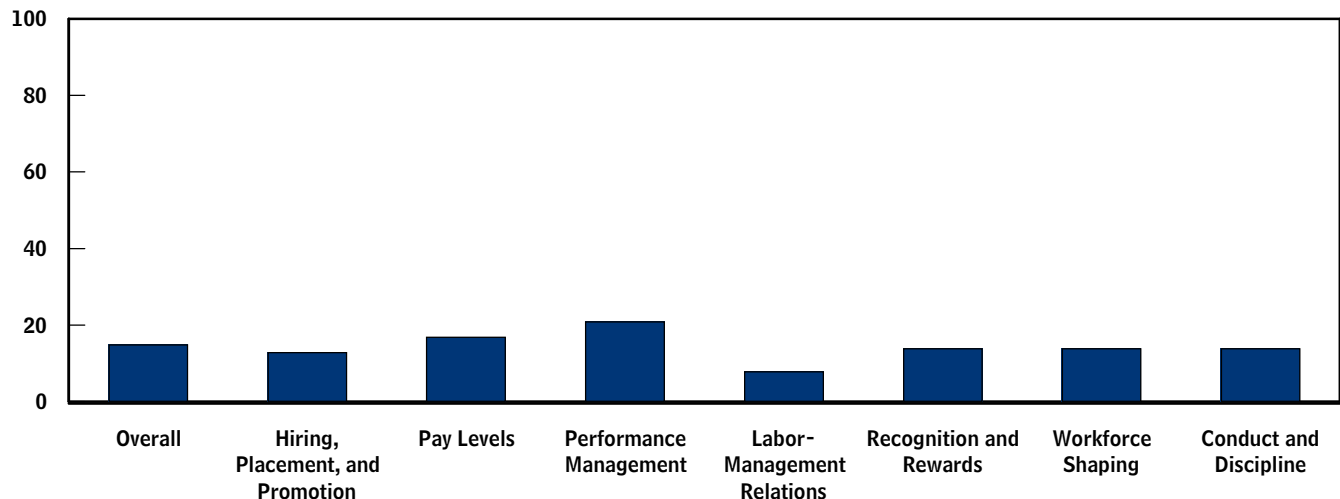
to employees and emphasizing the need for continuous, meaningful dialogue between supervisors and employees.

A more recent report based on focus group meetings with NSPS employees conducted by the Government Accountability Office between August 2007 and July 2008 presented conclusions that support the survey results. According to GAO, most of the DoD employees and their supervisors in the meetings noted the following concerns: (1) NSPS's negative impact on employee motivation and morale; (2) the excessive amount of time and effort required to navigate the performance management process; (3) the potential influence that employees' and supervisors' writing skills have on panels' assessments of employee ratings; (4) the lack of transparency and understanding of the pay pool process; and (5) the rapid pace at which the system was implemented, which often resulted

Figure 6-4.

Share of Civilian Employees in the Department of Defense Who Prefer the National Security Personnel System to the Previous Personnel System

(Percent)



Source: Congressional Budget Office based on data from Defense Manpower Data Center, *Status of Forces Survey of DoD Civilians*, May 2007.

Note: This figure displays the percentage of Department of Defense (DoD) civilian employees who were converted to the National Security Personnel System (NSPS) under Spirals 1.1, 1.2, or 1.3 or who supervise such employees and who think that NSPS is better or much better than the previous personnel system.

in employees feeling unprepared and unable to find answers to their questions.³³

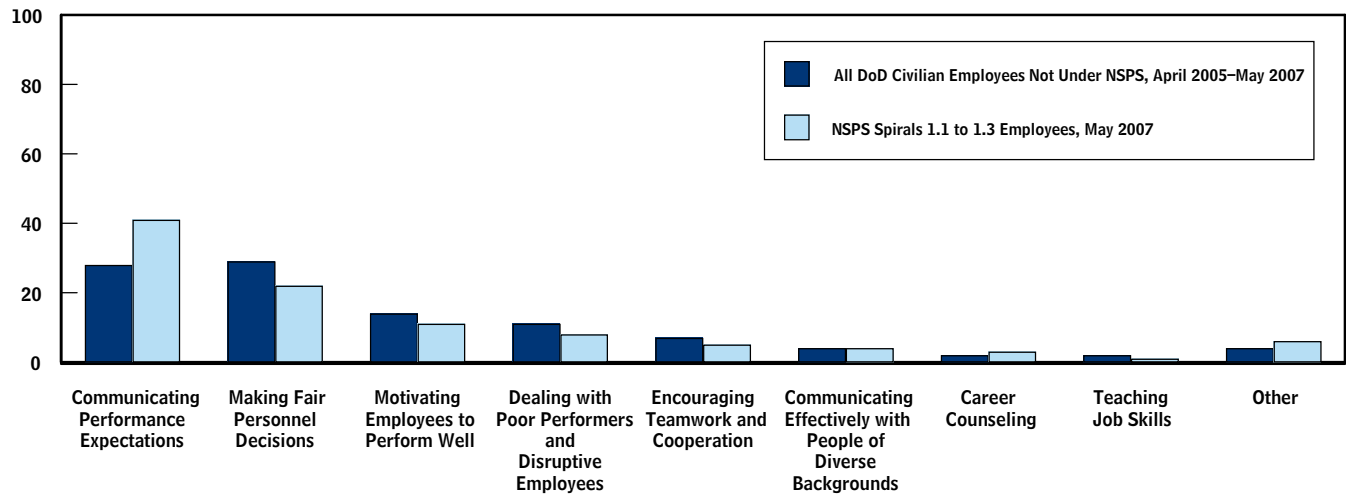
33. See Government Accountability Office, *Human Capital: DoD Needs to Improve Implementation of, and Address Employee Concerns About, Its National Security Personnel System*, GAO-08-773 (September 2008).

The Government Accountability Office also reported that DoD has not developed a specific action plan to address the issues identified by its employees, citing the NSPS Program Executive Office's preference to wait until employees have more experience under the system before making changes.

Figure 6-5.

Most Important Skills or Abilities for Supervisors Under the National Security Personnel System, According to the Department of Defense's Civilian Employees

(Percent)

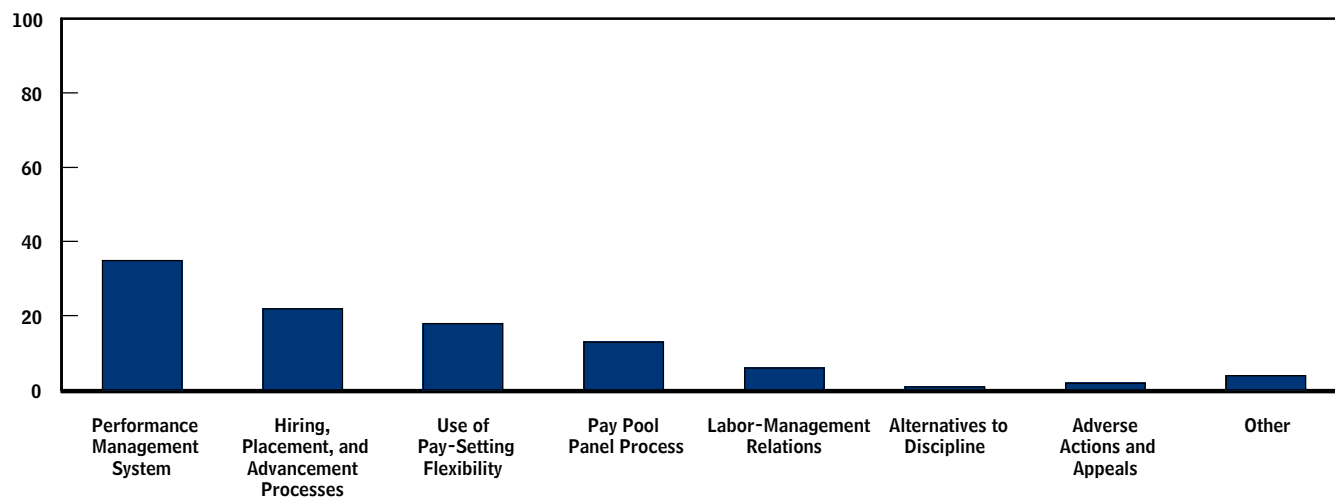


Source: Congressional Budget Office based on data from Defense Manpower Data Center, *Status of Forces Survey of DoD Civilians*, November 2005, May 2006, and May 2007.

Note: Labels for survey response categories are paraphrased from actual survey response text.

Figure 6-6.**Most Important Training Areas Needed Under the National Security Personnel System, According to the Department of Defense's Civilian Employees**

(Percent)



Source: Congressional Budget Office based on data from Defense Manpower Data Center, *Status of Forces Survey of DoD Civilians*, November 2005 and May 2007.

Notes: The percentages represent the average responses (measured in November 2005 and May 2007) of civilian employees in the Department of Defense who had not been converted to the National Security Personnel System.

Labels for survey response categories are paraphrased from actual survey response text.

The Pay-for-Performance System for the Senior Executive Service

The National Defense Authorization Act for Fiscal Year 2004 (Public Law 108-136) established a new pay system for members of the Senior Executive Service (SES). That law directed that executive pay be based on “individual performance, contribution to the agency’s performance, or both, as determined under a rigorous performance management system.”¹ The new SES pay system went into effect on January 11, 2004.

The SES was established by the Civil Service Reform Act of 1978. It covers positions above Level 15 of the General Schedule (GS) that are not filled by Presidential appointment with Senate confirmation and that have managerial, supervisory, and policymaking responsibilities.² Roughly 90 percent of the approximately 7,000 SES employees governmentwide today are career appointees who fulfilled competitive selection requirements and serve without a time limit.³ The remainder consists of noncompetitively selected, noncareer appointees and others serving for a limited time or to meet a specific emergency need.

Until 2003, the SES had six rates of basic pay—ES-1 (lowest) through ES-6 (highest). The minimum SES basic pay was set at “not less than 120 percent of the minimum rate of basic pay payable for GS-15 of the General Schedule.”⁴ That language, which still stands today,

requires that minimum SES basic pay be increased every year in conjunction with the yearly adjustments to GS pay rates. The maximum SES basic pay could not exceed Level IV of the Executive Schedule (\$134,000 in 2003).⁵ Therefore, as of 2003, the six rates of annual basic pay for SES employees were ES-1, \$116,500; ES-2, \$122,000; ES-3, \$127,500; ES-4, \$133,800; ES-5, \$134,000; and ES-6, \$134,000. In addition to basic pay, Senior Executive Service employees received the same locality adjustment as GS employees.

The combination of the legally mandated (and annually growing) minimum pay and the ceiling at Level IV of the Executive Schedule led to compression in the SES pay schedule (evident in the negligible differences in basic pay between ES-4 and ES-6). The new SES pay system was developed partly to address that pay compression.

Another impetus for changing the SES pay system was the Presidential Management Agenda (PMA) introduced by the Bush Administration in 2001.⁶ The PMA unveiled strategic management of human capital as one of five governmentwide initiatives to improve the management and performance of the federal government.⁷

1. 5 U.S.C. § 5382(a).

2. Some agencies (such as the intelligence agencies) and positions (such as administrative law judges and positions in the Foreign Service) are excluded from the Senior Executive Service. The Office of Personnel Management oversees the overall SES program. For more information, see Office of Personnel Management, *The Senior Executive Service* (February 2004), www.opm.gov/ses/sesguide.asp.

3. The selection requirements include executive core qualifications, which describe leadership skills. More details are available at www.opm.gov/ses/recruitment/qualify.asp.

4. 5 U.S.C. § 5376(b)(1)(A).

5. The Executive Schedule contains the pay rates for executive positions (typically Presidential appointees) classified above the SES. Pay rates in the Executive Schedule have a significant effect on rates in the GS, SES, and other federal civilian systems because legislation governing those pay systems normally ties the maximum amounts payable to various levels of the Executive Schedule.

6. See Office of Management and Budget, *The President's Management Agenda, Fiscal Year 2002* (2002).

7. The other four initiatives are competitive sourcing, improved financial performance, expanded electronic government, and budget and performance integration.

The PMA criticized federal personnel policies for inadequately rewarding performance and called for a civil service that would, among other things, use appropriate incentives to improve the performance of individual employees and teams and foster leadership.

The new SES pay system:

- Eliminates locality pay.
- Replaces the six pay rates with one broad pay range.
- Increases the cap on annual SES base pay from Level IV of the Executive Schedule to Level III (from \$149,000 to \$158,500 in 2008).
- Adds a second, higher cap on SES base pay (Executive Schedule Level II, \$172,200 in 2008) for agencies that are certified as “having a performance appraisal system, which as designed and applied, makes meaningful distinctions based on relative performance.”⁸

Other restrictions on SES pay under existing law limit total cash compensation (including basic pay, bonuses, awards, and other cash payments) in any single calendar year to Level I of the Executive Schedule (\$191,300 in 2008).⁹ For agencies that have certified performance appraisal systems, however, section 1322 of the Home-

land Security Act of 2002 increased the cap on total cash compensation from Level I of the Executive Schedule to the equivalent of the Vice President’s annual salary (\$221,100 in 2008). (The cap on total cash compensation for agencies without a certified performance appraisal system remains at Level I of the Executive Schedule.) Table A-1 shows pay levels under the new SES system.¹⁰

The higher cap gives agencies with certified performance appraisal systems more flexibility to compensate their employees. But even though the minimum SES basic pay meets the statutory requirement, it is about 8 percent lower than the top of the GS-15 basic pay scale, the Congressional Budget Office notes.¹¹ The federal government’s ability to attract well-qualified candidates to the Senior Executive Service could be negatively affected if new members of that service were routinely offered the minimum pay on the SES pay scale.

As required in legislation, the Office of Personnel Management (OPM), with the concurrence of the Office of Management and Budget (OMB), developed guidelines for the certification process, which it updates each year.¹² The criteria that agencies’ performance appraisal systems must fulfill include linking individual performance expectations to organizational missions and objectives; involving employees in developing those performance objectives; focusing on measurable, observable outputs (including customer/stakeholder satisfaction and leadership competencies); evaluating agencies’ performance in relation to their goals under the Government Performance Results Act; and implementing meaningful distinctions in performance that are linked to pay adjustments and awards.

8. See 5 U.S.C. § 5382(b). The Office of Personnel Management (OPM) and the Office of Management and Budget oversee the certification process. The caps on total cash compensation in relation to the certification status of performance appraisal systems also apply to Senior Level (SL) and Scientific/Technical (ST) positions—nonexecutive senior positions classified above GS-15 for which technical expertise, not leadership, is the main qualification. According to OPM’s guidelines, the ST system covers positions that involve performance of high-level research and development in the physical, biological, medical, or engineering sciences or a closely related field. The SL system is for positions that do not have the fundamental research and development responsibilities that are characteristic of the ST system. For more details on SL and ST positions, see Office of Personnel Management, *The Senior Executive Service*. The certification status of SL and ST appraisal systems does not apply to the cap on basic pay for those employees. Also, Public Law 108-136 did not eliminate the locality adjustment for SL and ST employees.

9. See 5 U.S.C. § 5307. The cap on total cash compensation is not tantamount to a loss in pay. If a senior executive’s salary exceeds the cap, the excess amount is deferred and paid in the next calendar year.

10. A Congressional Research Service report provides more details and discusses some policy issues on the new SES pay system. See Congressional Research Service, *Senior Executive Service (SES) Pay for Performance System*, RL33128 (February 2007).

11. As required by law, the minimum SES basic salary of \$114,468 in 2008 equals 120 percent of the basic pay for a GS-15 Step 1 (\$95,390). However, that minimum SES salary falls short of the \$124,010 paid to a GS-15 Step 10 at the top of the GS pay scale.

12. Updated certification guidelines for 2007, data instructions, and examples of agencies’ performance plans are available at www.opm.gov/ses/performance/certification.asp.

Table A-1.

Pay Levels for the Senior Executive Service, January 2008

(2008 dollars)

	Agencies Without a Certified Performance Appraisal System	Agencies With a Certified Performance Appraisal System
Minimum Basic Pay	114,468	114,468
Maximum Basic Pay	158,500	172,200
Maximum Total Cash Compensation	191,300	221,100

Source: Congressional Budget Office based on data from the Office of Personnel Management.

Upon reviewing each agency’s performance appraisal system, OPM, again with OMB’s concurrence, may grant full or provisional certification. Full certification is granted for two calendar years but could be terminated if an agency fails to continue to fulfill the necessary requirements. An agency may be granted provisional certification for one year if its performance appraisal system meets design requirements but sufficient data do not yet

exist after implementation to determine whether its system meets the certification requirements.¹³

13. OPM may extend provisional certification into the following calendar year if warranted. For a list of agencies that have received certification for 2008, which includes the Department of Defense, see www.opm.gov/ses/performance/certification.asp.

APPENDIX

B

The Department of Defense's Plan for Converting Its Employees to the National Security Personnel System

The Department of Defense (DoD) is converting its civilian employees to the National Security Personnel System (NSPS) in phases, or "spirals." About 113,000 non-union white-collar employees in all military departments and the Office of the Secretary of Defense were converted

under Spirals 1.1, 1.2, and 1.3 between April 2006 and April 2007. Another 75,000 employees are expected to be converted under Spiral 2 by December 2008 (see Table B-1). The organizations and number of employees in Spiral 2 are subject to change as DoD refines the plan.

Table B-1.

Components and Number of Employees in the Department of Defense Identified for Conversion to the National Security Personnel System in Spirals 1 and 2

Component	Number of Employees
Spiral 1.1	
Department of the Army	2,348
Civilian Human Resources Activity	37
Civilian Personnel Operations Centers	1,466
Civilian Personnel Advisory Centers	845
Department of the Navy	4,354
Naval Sea Systems Command, Headquarters and Program Executive Offices	2,181
Naval Ordnance Safety and Security Activity	87
Office of Civilian Human Resources and Human Resources Service Centers	1,079
Joint Warfare Analysis Center	461
Strategic Systems Program Office	242
Human Performance Center	134
Commander, U.S. Pacific Fleet	170
Department of the Air Force	3,142
Secretary of the Air Force, Manpower/Reserve Affairs	37
Elements of Tinker Air Force Base	2,460
Air Force Audit Agency	645
Office of the Secretary of Defense, Defense Agencies/Activities and Other Offices ("4th Estate")	1,280
Defense Threat Reduction Agency	990
TRICARE Management Activity	290
Subtotal, Spiral 1.1	11,124
Spiral 1.2	
Department of the Army	14,373
U.S. Army Military District of Washington	67
U.S. Army Medical Command	539
Office of the Assistant Secretary of the Army	6,604
U.S. Army Surface Deployment and Distribution Command	204
U.S. Army Forces Command	492
U.S. Army Materiel Command	1,720
U.S. Army South	164
U.S. Army Corps of Engineers	4,497
U.S. Army Training and Doctrine Command	86
Department of the Navy	8,495
Chief of Naval Operations	1,231
Assistant for Administration, Office of the Under Secretary of the Navy	1,182
Bureau of Personnel	99
Naval Facilities Engineering Command	271
Naval Sea Systems Command	85
Marine Corps	1,828
Strategic Systems Programs	128
Fleet Forces Command	1,848
Commander, Pacific Fleet	431

Continued

Table B-1.**Continued**

Components and Number of Employees in the Department of Defense Identified for Conversion to the National Security Personnel System in Spirals 1 and 2

Component	Number of Employees
Spiral 1.2 (Continued)	
Department of the Navy (Continued)	
Naval Reserve Forces Command	225
Naval Special Warfare Command	545
Commander, Naval Installations	622
Department of the Air Force	36,706
Air Combat Command	4,521
Air Education and Training Command	5,156
Air Force District of Washington	1,527
Air Force Materiel Command	11,990
Air Force Reserve Command	1,417
Air Force Space Command	3,497
Air Force Special Operations Command	187
Air Mobility Command	3,781
Centrally Funded Training Program	1,058
National Guard Bureau	201
Pacific Air Force	2,139
U.S. Air Force Academy	280
U.S. Air Forces in Europe	952
Office of the Secretary of Defense, Defense Agencies/Activities and Other Offices ("4th Estate")	6,984
Washington Headquarters Services	819
TRICARE Management Agency (remaining)	114
Defense Security Cooperation Agency	300
Defense Business Transformation Agency	61
Office of Inspector General	1,360
Defense Finance and Accounting Service	692
Defense Acquisition University	170
OSD and WHS-Serviced Components (Joint Staff/Defense Advanced Research Projects Agency/ Office of Economic Adjustment/Defense Legal Services Agency/Defense Technology Security Administration/Defense Prisoner of War and Missing Personnel Office/Defense Test Resource Management Center/American Forces Information Service/Pentagon Force Protection Agency)	2,367
Missile Defense Agency	678
Civilian Personnel Management Service	423
Subtotal, Spiral 1.2	66,558
Spiral 1.3	
Department of the Army	26,241
Office of the Secretary of the Army	14,178
U.S. Army Acquisition Support Center	10
U.S. Army Corps of Engineers	2,000
U.S. Army Medical Command	3,544
U.S. Army, Pacific	556
U.S. Army Space and Strategic Defense Command	345
U.S. Army Training and Doctrine Command	2,198

Continued

Table B-1.**Continued**

Components and Number of Employees in the Department of Defense Identified for Conversion to the National Security Personnel System in Spirals 1 and 2

Component	Number of Employees
Spiral 1.3 (Continued)	
Department of the Army (Continued)	
U.S. Forces Command	891
U.S. Special Operations Command (Army)	113
Army Materiel Command	2,070
Army National Guard	330
U.S. Army Field Band	6
Department of the Navy	7,571
Chief of Naval Operations	195
Assistant for Administration, Office of the Under Secretary of the Navy	32
Commander, U.S. Pacific Fleet	5
Fleet Forces Command	205
Naval Education and Training Command	230
Naval Reserve Force	7
Naval Sea Systems Command	29
Space and Naval Warfare Systems Command	6,867
Naval Special Warfare Command	1
Department of the Air Force	1,232
Air National Guard	211
U.S. Air Forces Europe and Headquarters	1,020
U.S. Transportation Command	1
Office of the Secretary of Defense, Defense Agencies/Activities and Other Offices ("4th Estate")	318
Defense Finance and Accounting Service	274
Defense Threat Reduction Agency	44
Subtotal, Spiral 1.3	35,362
Total, Spirals 1.1, 1.2, and 1.3	113,044
Spiral 2 (Projected)	
Department of the Army	27,306
Department of Army, Headquarters	7,324
Eighth U.S. Army	168
Army National Guard	25
U.S. Army Central	106
U.S. Army Corps of Engineers	7,581
U.S. Army Europe	1,823
U.S. Forces Command	504
U.S. Army Materiel Command	2,459
U.S. Army Medical Command	4,380
U.S. Army Military District of Washington	34
U.S. Army Pacific	41
U.S. Army Training and Doctrine Command	2,457
U.S. Special Operations Command (Army)	404

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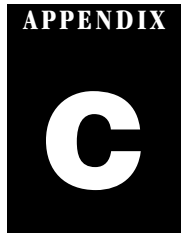
Table B-1.**Continued**

Components and Number of Employees in the Department of Defense Identified for Conversion to the National Security Personnel System in Spirals 1 and 2

Component	Number of Employees
Spiral 2 (Projected, Continued)	
Department of the Navy	31,871
Assistant for Administration, Office of the Under Secretary of the Navy	1,955
Bureau of Naval Personnel	846
Bureau of Medicine and Surgery	3,702
Chief of Naval Operations	886
Commander, Naval Installations Command	5,473
Commander, U.S. Pacific Fleet	1,719
Headquarters, U.S. Marine Corps	5,138
Military Sealift Command	391
Naval Education and Training Command	2,560
Naval Facilities Engineering Command	4,211
Navy Reserve Force Command	50
Naval Sea Systems Command	521
Naval Supply Systems Command	1,652
Strategic Systems Programs	235
U.S. Fleet Forces Command	2,532
Department of the Air Force, Air National Guard Units	173
Office of the Secretary of Defense, Defense Agencies/Activities and Other Offices ("4th Estate")	15,776
Defense Commissary Agency	2,164
Defense Contract Audit Agency	1,355
Defense Contract Management Agency	1,667
Defense Education Activity	2,547
Defense Finance and Accounting Service	1,326
Defense Human Resources Agency	445
Defense Information Systems Agency	715
Defense Logistics Agency	4,759
Defense Technical Information Center	74
National Defense University	289
Uniformed Services University of the Health Sciences	385
White House Support	28
WHS-Raven Rock Mountain Complex	22
Subtotal, Spiral 2	75,126
Total, Spirals 1 and 2	188,170

Source: Congressional Budget Office based on data from Department of Defense, National Security Personnel System Program Executive Office.

Notes: NSPS = National Security Personnel System; OSD = Office of the Secretary of Defense; WHS = Washington Headquarters Services. The number of employees identified for conversion in each organization may differ slightly from the number observed after the completion of each spiral because of changes in the status of some employees and positions throughout the year. For instance, some NSPS employees may move to a non-NSPS position, and some previously filled NSPS positions may later be unfilled or eliminated.



The Pay Banding Structure for the Four Career Groups in the National Security Personnel System

The National Security Personnel System (NSPS) groups all Department of Defense jobs into four career groups on the basis of the similarity of work performed. The jobs in each career group (standard, scientific and engineering, investigative and protective services, and medical) are further categorized into pay schedules on the basis of such factors as the level of responsibility, job competencies, and educational requirements. Then, each job is assigned into one of three (or, in some cases, four) pay bands.

The pay banding system differs from the 15 grade levels used in the traditional General Schedule (GS) system for white-collar employees in the federal government. The range of pay in each band is greater than the pay range in each GS grade and largely corresponds to a collection of GS grades. Table C-1 lists the minimum and maximum pay in each pay band for the four NSPS career groups. The table also lists the GS grades that correspond to each pay band as determined by the Congressional Budget Office.

Table C-1.**Pay Bands for the Four Career Groups in the National Security Personnel System**

	Minimum Salary (2008 dollars)	Equivalent GS Grade/Step	Maximum Salary (2008 dollars)	Equivalent GS Grade/Step	Percentage over Minimum
Standard Career Group					
Professional/Analytical					
Pay band 1	26,008	5/1	62,593	11/10	141
Pay band 2	39,407	9/1	89,217	13/10	126
Pay band 3	77,018	13/5	130,211	> 15/10	69
Technician/Support					
Pay band 1	16,880	1/1	38,060	6/10	125
Pay band 2	32,217	7/1	56,973	10/10	77
Pay band 3	47,679	11/1	75,025	12/10	57
Supervisor/Manager					
Pay band 1	32,217	7/1	62,593	11/10	94
Pay band 2	57,146	12/1	110,691	15/6 ^a	94
Pay band 3	80,302	14/1	130,211	> 15/10	62
Student					
Pay band 1	16,880	1/1	62,593	11/10	271
Scientific and Engineering Career Group					
Professional					
Pay band 1	26,008	5/1	62,593	11/10	141
Pay band 2	39,407	9/1	89,217	13/10	126
Pay band 3	77,018	13/5	130,211	> 15/10	69
Technician/Support					
Pay band 1	16,880	1/1	38,060	6/10	125
Pay band 2	32,217	7/1	56,973	10/10	77
Pay band 3	47,679	11/1	75,025	12/10	57
Pay band 4	64,767	12/5	89,217	13/10	38
Supervisor/Manager					
Pay band 1	32,217	7/1	62,593	11/10	94
Pay band 2	57,146	11/1	110,691	15/6 ^a	94
Pay band 3	77,018	12/5	130,211	> 15/10	69
Investigative and Protective Services Career Group					
Investigative					
Pay band 1	26,008	5/1	62,593	11/10	141
Pay band 2	39,407	9/1	89,217	13/10	126
Pay band 3	77,018	13/5	130,211	> 15/10	69
Fire Protection					
Pay band 1	16,880	1/1	38,060	6/10	125
Pay band 2	32,217	7/1	56,973	10/10	77
Pay band 3	47,679	11/1	75,025	12/10	57
Pay band 4	64,767	12/5	105,420	14/10	63
Police/Security Guard					
Pay band 1	16,880	1/1	38,060	6/10	125
Pay band 2	32,217	7/1	56,973	10/10	77
Supervisor/Manager					
Pay band 1	32,217	7/1	62,593	11/10	94
Pay band 2	57,146	12/1	110,691	15/6 ^a	94
Pay band 3	80,302	14/1	130,211	> 15/10	62

Continued

Table C-1. **Continued**
Pay Bands for the Four Career Groups in the National Security Personnel System

	Minimum Salary (2008 dollars)	Equivalent GS Grade/Step	Maximum Salary (2008 dollars)	Equivalent GS Grade/Step	Percentage over Minimum
Medical Career Group					
Physician/Dentist					
Pay band 2	87,742	14/4 ^a	175,000	> 15/10	99
Pay band 3	113,173	15/7 ^a	225,000	> 15/11	99
Professional					
Pay band 1	26,008	5/1	62,593	11/10	141
Pay band 2	39,407	9/1	105,420	14/10	168
Pay band 3	77,018	13/5	130,211	> 15/11	69
Technician/Support					
Pay band 1	16,880	1/1	38,060	6/10	125
Pay band 2	32,217	7/1	56,973	10/10	77
Pay band 3	47,679	11/1	75,025	12/10	57
Supervisor/Manager					
Pay band 1	32,217	7/1	62,593	11/10	94
Pay band 2	57,146	12/1	110,691	15/6 ^a	94
Pay band 3	80,302	14/1	130,211	> 15/10	62
Pay band 4	103,226	15/4 ^a	200,000	> 15/11	94

Source: Congressional Budget Office based on data from Department of Defense, National Security Personnel System Program Executive Office.

Note: GS = General Schedule; > = greater than.

a. Approximate.

Further Details About the 2008 Performance Evaluation and Payout Under the National Security Personnel System

In January 2008, the Department of Defense (DoD) paid out performance-based pay raises and bonuses to its civilian employees under the National Security Personnel System (NSPS).¹ That payout was based on performance evaluations of employees converted to NSPS in Spirals 1.1, 1.2, and 1.3 for work performed in 2007. The Congressional Budget Office (CBO) obtained and analyzed the performance evaluation and payout data to examine how increases in base pay and bonuses are related to performance and how those increases vary among DoD components as well as by employees' demographic characteristics. The data covered about 102,000 employees.

CBO's analysis revealed some differences in average performance ratings and associated increases in compensation among DoD components and employees. For example, some demographic groups received higher performance ratings and increases in compensation, on average, than others. However, the magnitude of those differences is relatively small. Employees in higher pay bands also received higher performance ratings and increases in compensation than employees in lower pay bands. The fact that the various demographic groups are distributed differently in the pay bands could partly explain the differences among the groups.

1. Those performance-based pay raises and bonuses are separate from the general adjustments to pay bands and increases in local market supplements. In NSPS, funds used for performance-based pay raises include those funds historically spent on within-grade increases, quality step increases, and promotion between grades in the General Schedule system. Only employees with a rating of 3 (valued performer) or higher receive performance-based increases in base pay and bonuses.

According to the data, the average performance rating for all employees was about 3.5 on a 5-point scale (see Table D-1). The overall average increase in base pay and overall average bonus award (as a percentage of base pay) were, respectively, 3.5 percent and 1.8 percent, yielding a total payout of about 5.3 percent.² The performance ratings for employees in the Department of the Army and the Department of the Navy averaged about 3.4; ratings were slightly higher (at 3.5), on average, for employees in the Department of the Air Force and the Office of the Secretary of Defense and other DoD agencies. However, the pattern of the differences in base pay increases and bonuses among DoD components was not the same as that for the performance ratings. For instance, civilian employees of the Department of the Army received a higher percentage increase in base pay and bonuses, on average (3.8 percent and 2.1 percent, respectively) than employees of the Department of the Navy (2.9 percent and 1.2 percent, respectively) who had the same average performance rating (3.4). Employees in the Office of the Secretary of Defense and DoD agencies received the highest average performance rating (3.5) and largest average increases in base pay and bonuses (3.5 percent and 2.6 percent, respectively).

Average performance ratings for white and black employees were 3.5 and 3.3, respectively. Hispanic, Asian, and employees of "other" racial backgrounds received similar average performance ratings of about 3.4.³ In general, the racial categories with higher average performance ratings

2. The average increase in base pay and bonuses may not add up to the total payout because of rounding.

3. The "other" racial category includes Native Americans, Pacific Islanders, and people who identify themselves as multiracial.

Table D-1.**Average Performance Ratings and Pay Increases for Employees in the National Security Personnel System, 2008**

	Performance Rating	Increase in Base Pay (Percent)	Bonus Award (Percentage of base pay)	Total Payout ^a (Percentage of base pay)
All NSPS Employees	3.45	3.46	1.77	5.24
DoD Component				
Department of the Army	3.44	3.76	2.08	5.84
Department of the Navy ^b	3.44	2.90	1.22	4.12
Department of Air Force	3.46	3.45	1.57	5.02
Office of the Secretary of Defense and DoD Agencies	3.51	3.49	2.55	6.04
Race/Ethnicity				
White	3.50	3.54	1.85	5.39
Black	3.30	3.27	1.61	4.88
Hispanic ^c	3.38	3.36	1.65	5.01
Asian	3.36	3.10	1.42	4.52
Other ^d	3.39	3.39	1.55	4.95
Sex				
Male	3.45	3.39	1.80	5.19
Female	3.45	3.57	1.74	5.31
Age				
Under 40 years	3.44	3.48	1.56	5.04
40 years or older	3.45	3.46	1.82	5.28
Pay Band				
1	3.25	2.57	1.81	4.38
2	3.42	3.48	1.63	5.10
3	3.70	3.95	2.34	6.29
4 ^e	3.54	2.30	1.54	3.84

Source: Congressional Budget Office based on data from Department of Defense, National Security Personnel System Program Executive Office.

Note: NSPS = National Security Personnel System; DoD = Department of Defense.

- The total payout is the sum of the percentage increase in base pay and the bonus award. Numbers may not add up to totals because of rounding.
- Includes the Marine Corps.
- Hispanics can be of any race. For example, under this definition, white and black hispanics would not be included in the respective white or black racial categories.
- Includes Native Americans, Pacific Islanders, and people who identify themselves as multiracial.
- Less than one-half of 1 percent of the employees in the data are in pay band 4.

received larger increases in base pay and bonuses, with the exception of blacks, who had a slightly lower average performance rating than Asians (3.3 compared with 3.4) but received a larger average base pay increase and bonuses (3.3 percent and 1.6 percent, compared with 3.1 percent and 1.4 percent, respectively).

Men and women received the same average performance rating (3.5). However, women received a larger increase in base pay than men (3.6 percent compared with 3.4 percent). Also, although employees who were under 40 years old received ratings similar to their counterparts who were 40 years or older (about 3.5), the older employ-

ees received larger bonuses (1.8 percent compared with 1.6 percent).

On average, employees in higher pay bands received higher performance ratings and associated increases in base pay and bonuses. For example, employees in pay bands 1, 2, and 3 received average performance ratings of 3.3, 3.4, and 3.7, respectively. The corresponding increases in base pay and bonuses for those pay bands were, respectively, 2.6 percent and 1.8 percent; 3.5 percent and 1.6 percent; and 4.0 percent and 2.3 percent (see Table D-1). Employees in pay band 4 are an exception to that finding because they received a lower average performance rating than employees in pay band 3 (3.5 compared with 3.7) and the smallest increase in base pay and bonuses compared with employees in the other pay bands. However, relatively few (less than one-half of 1 percent) of employees are in pay band 4, according to the data. Also, the fact that employees in pay band 4 received a lower average percentage increase in base pay and bonuses might indicate that DoD has less flexibility to award large pay raises at the top end of the pay range for the NSPS career groups.

That pattern of higher average performance ratings and pay increases for higher pay bands partly explains the differences among groups of employees. For example, relatively more white employees (the racial group with the highest average performance ratings and increases in compensation) are in pay band 3 than are employees of the other races: About 21 percent of white employees are in that pay band compared with 10 percent to 12 percent of blacks, Hispanics, Asians, and employees of other races (see Table D-2). Conversely, relatively fewer white employees (9 percent) are in pay band 1 than are employees of the other races (between 13 percent and 17 percent). Similarly, the proportion of employees who are 40 years of age or older (the group with the larger bonus award percentage) is greater in pay band 3 (20 percent) than the proportion of employees who are younger than age 40 (7 percent). Lastly, even though men tend to be in higher pay bands than women, they received a smaller increase in base pay than women despite a similar average performance rating.

Table D-2.

Demographic Analysis of Employees in the National Security Personnel System, by Pay Band, 2008

(Percent)

	Pay Band 1	Pay Band 2	Pay Band 3	Pay Band 4	Total	Number of Employees
Race/Ethnicity						
White	9.01	69.98	20.73	0.29	100	73,600
Black	16.85	72.75	10.32	0.07	100	14,700
Hispanic ^a	16.58	72.45	10.88	0.08	100	6,000
Asian	13.47	74.75	11.52	0.26	100	5,800
Other ^b	15.51	71.75	12.43	0.30	100	2,000
Sex						
Male	7.92	69.42	22.28	0.38	100	60,600
Female	15.41	72.88	11.66	0.05	100	41,400
Age						
Under 40 years	28.14	64.97	6.80	0.10	100	17,400
40 years or older	7.42	72.03	20.27	0.28	100	84,500

Source: Congressional Budget Office based on data from Department of Defense, National Security Personnel System Program Executive Office.

Note: Numbers may not add up to totals because of rounding.

- a. Hispanics can be of any race. For example, under this definition, white and black hispanics would not be included in the respective white or black racial categories.
- b. Includes Native Americans, Pacific Islanders, and people who identify themselves as multiracial.

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