



Pay-for-Performance: Lessons from the National Security Personnel System

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Summary

Most federal employees (59.8%) are paid on the General Schedule, a pay scale that consists of 15 pay grades in which an employee's pay increases are to be based on performance and length of service. Some Members of Congress, citizens, and public administration scholars have argued that federal employee pay advancement should be more closely linked to job performance. With explicit congressional authorization enacted in 2003, the Department of Defense (DOD) created the National Security Personnel System (NSPS) as a unique pay scale attempting to more closely link employee pay to job performance.

NSPS has been plagued by criticisms since it went into effect in 2006. The system has faced legal and political challenges from unions and employees who claim it is inconsistently applied and causes undeserved pay inequities, among other concerns.

On October 7, 2009, House and Senate conferees reported a version of the National Defense Authorization Bill for Fiscal Year 2010 that included language to terminate NSPS. On October 8, 2009, the House agreed to the conference report. The Senate agreed to the conference report on October 22, 2009. On October 28, 2009, the President signed the bill into law (P.L. 111-84). DOD must now return the employees currently enrolled in NSPS to the GS or to the pay scale in which they were previously enrolled. The return to the GS or other pay scales must be completed by 2012, pursuant to the legislation.

NSPS was initially intended to cover all DOD employees, but has a current enrollment of roughly 211,000 civilian employees, or 29.4% of the department's 717,000-person workforce.

Like other performance-based pay systems, NSPS makes job performance a predominant factor in determining employee pay. A supervisor and an employee who use NSPS are to work together to create an annual appraisal plan that accurately reflects an employee's performance. A supervisor then is to use the appraisal to evaluate the employee. At the end of each appraisal year, an employee may be assigned a percentage increase in pay based on his or her performance. These increases are called pay shares. Lower-performing employees may receive fewer pay shares or no pay shares. An employee must acquire at least a satisfactory performance rating to be eligible for any performance-based bonuses.

This report reviews the creation of the NSPS, examines how NSPS operates, discusses litigation against it, and analyzes lessons that can be learned from NSPS as Congress decides whether to maintain the GS, create a new federal pay system, or modify existing ones. It will be updated as necessary.

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Introduction

As of June 2009, the General Schedule (GS) covered roughly 59.8% of federal employees.¹ The GS contains 15 pay grades, each of which is divided into 10 steps. The higher an employee's grade and step, the higher his or her pay. Federal employees rise within grades in the GS pay scale based on performance and length of service.

The Department of Defense (DOD), however, operates a pay system called the National Security Personnel System (NSPS), which attempts to link pay increases more closely to employee performance without the use of grades or steps.² NSPS is "the first civilian alternate personnel system to be implemented on a broad basis, across an entire Executive Department," and DOD is "the largest department in the Federal government."³ As of June 2009, DOD employed more than 717,000 civilian employees—about 35.4% of federal civilian executive branch personnel worldwide.⁴ Not every DOD employee, however, is eligible to enter NSPS.⁵ As of June 2009, 211,000 (29.4%) of DOD's 717,000 employees were covered by NSPS.⁶

On October 7, 2009, House and Senate conferees reported a version of the National Defense Authorization Bill for Fiscal Year 2010 that included language to terminate NSPS by 2012. The legislation to eliminate the pay system follows years of complaints of NSPS performance evaluation inconsistencies and litigation related to NSPS payouts.⁷ On October 8, 2009, the

¹ U.S. Office of Personnel Management, Central Personnel Data File, <http://www.fedscope.opm.gov/>. The employee count is from June 2009. The Central Personnel Data File does not include employee counts from several federal agencies, including the Central Intelligence Agency, the Defense Intelligence Agency, the National Geospatial-Intelligence Agency, the Postal Rate Commission, and USPS. The employee count does not include Senior Executive Service employees, administrative judges, or other federal employees who are not paid on the General Schedule.

² The legislation that created NSPS is P.L. 108-136, The National Defense Authorization Act for Fiscal Year 2004.

³ U.S. Office of Personnel Management, *Creating a Foundation for the 21st Century Federal Workforce: An Assessment of the Implementation of the Department of Defense National Security Personnel System* (Washington: May 2007), Appendix H, p. 149. Many government agencies currently operate pay-for-performance systems. For more information on such systems see CRS Report RL34529, *Pay-for-Performance: Linking Employee Pay to Performance Appraisal*, by Wendy R. Ginsberg. On June 18, the Office of Personnel Management published in the *Federal Register* a plan to experiment with performance-based pay at the Department of Veterans Affairs (VA). According to the *Federal Register*, the first performance-based bonuses at VA would be distributed in 2010. For more information, see U.S. Office of Personnel Management, "Proposed Personnel Demonstration Project; Performance-Based Pay Adjustments in the Department of Veterans Affairs," 73 *Federal Register* 34800, June 18, 2008.

⁴ U.S. Office of Personnel Management, Central Personnel Data File, <http://www.fedscope.opm.gov/>. The employee count is from June 2009. Although NSPS was originally designed to include all DOD employees, P.L. 110-181 removed "prevailing rate employees" from NSPS eligibility. Prevailing rate employees, as defined in 5 U.S.C. § 5342(a)(2), include, among others, "an individual employed in or under an agency in a recognized trade or craft, or other skilled mechanical craft, or in an unskilled, semiskilled, or skilled manual labor occupation, and any other individual, including a foreman and a supervisor, in a position having trade, craft, or laboring experience and knowledge as the paramount requirement."

⁵ Bradley Bunn, "Statement Before the Defense Business Board Task Group on the National Security Personnel System," June 25, 2009, at <http://www.defenselink.mil/dbb/pdf/pdf/Bunn%20Written%20Statement%20-%20DBB%20Public%20Meeting%20-%2025June2009.pdf>. P.L. 108-136 exempted some employees in specific laboratories from the system.⁵ P.L. 110-181 cancelled plans to place 145,000 blue-collar workers in NSPS, and most employees with union representation have not been placed in the pay system. According to Bradley Bunn, program executive director for NSPS, 685 of DOD's 267,000 white-collar civilian bargaining employees are currently in NSPS.

⁶ U.S. Office of Personnel Management, Central Personnel Data File, <http://www.fedscope.opm.gov/>. The employee count is from June 2009.

⁷ *Am. Fed'n of Gov't Employees v. Rumsfeld*, 422 F. Supp. 2d 16 (D.D.C. 2006), http://www.afge.org/Documents/2006_02_27RumsfeldDecision.pdf; and *Am. Fed'n of Gov't Employees v. Gates*, 486 F.3d 1316 (D.C. Cir. 2007), (continued...)

House agreed to the conference report. The Senate agreed to the conference report on October 22, 2009. On October 28, 2009, the President signed the bill into law (P.L. 111-84). DOD must now return employees to the pay system in which they were formerly enrolled prior to the installation of NSPS.⁸

This report reviews the creation of the NSPS, examines how NSPS operates, and discusses litigation against it. The report then analyzes lessons that can be learned from NSPS and that may be applied to future attempts to create a federal performance-based pay system. This report will be updated as necessary.

National Security Personnel System History

NSPS grew out of George W. Bush Administration assertions that the GS system was incapable of creating a responsive and flexible national security workforce. In April 2003, DOD sent a proposal, entitled “The Defense Transformation for the 21st Century Act,” to Congress.⁹ The proposal recommended changing the statutory basis for much of DOD’s civilian personnel system to create a “more flexible, mission-driven system of human resources management” that could “adequately address the 21st century national security environment.”¹⁰ Many provisions in the DOD proposal were ultimately included in Title XI of the National Defense Authorization Act for Fiscal Year 2004 (P.L. 108-136)—including personnel flexibilities to create NSPS.¹¹ The act made some DOD personnel policies more flexible than those governed by Title 5 of the U.S. Code, which includes most of the provisions governing civilian employees. The flexibilities, including the authority to eliminate pay grades and steps, gave DOD and Office of Personnel Management (OPM) officials the opportunity to design a pay system that attempted to more closely link employee performance to pay. The new system was to help the department “develop a more flexible civilian personnel management system that would enhance [the department’s] ability to execute [its] national security mission.”¹²

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<http://www.afge.org/Documents/Rehearing%20Response%20FINAL.pdf>.

⁸ Returning federal employees to their previous pay systems may prompt a series of concerns for DOD and its employees. Some NSPS employees, for example, receive a salary that is greater than the GS pay cap for their particular position. The Office of Personnel Management (OPM) develops a position classification standard for each GS job. This standard limits the pay range for a particular position. Employees in NSPS, however, may not have had similar pay standards and limits applied to their jobs. A federal employee in NSPS may have been receiving greater pay for a job that was identical to a job performed by GS employee who had a particular limit on his or her pay. In addition, some employees in NSPS may receive pay greater than the GS’s overall cap (GS-15). It is unclear what will happen to the pay of employees who are required to return to the GS, but who receive pay that is higher than the GS would currently permit. These issues are beyond the scope of this report.

⁹ The text of the DOD proposal can be accessed at <http://www.govexec.com/pdfs/transformation.pdf>.

¹⁰ U.S. Department of Defense and Office of Personnel Management, “Department of Defense Human Resources Management and Labor Relations System; Final Rule,” 70 *Federal Register* 66117.

¹¹ For a more complete history of NSPS implementation, see CRS Report RL31954, *DOD’s National Security Personnel System: Statute, Regulations, and Implementation Plans*, by Barbara L. Schwemle et al. The National Defense Authorization Act for Fiscal Year 2008, P.L. 110-181, modifies P.L. 108-136. Some of these changes will be discussed later in this report.

¹² U.S. Congress, House Committee on Armed Forces, Subcommittee on Readiness, *The National Security Personnel System—Is it Really Working?* oversight hearing, testimony of Michael Dominguez, principal undersecretary of defense for personnel and readiness, 110th Cong., 2nd sess., March 6, 2007, http://armedservices.house.gov/pdfs/Readiness030607/Dominguez_Testimony030607.pdf.

On June 2, 2003, shortly after DOD released its proposed changes in personnel flexibilities for NSPS, Senator Susan Collins, then-chairman of the Senate Committee on Governmental Affairs, introduced S. 1166 (108th Congress). The bill, entitled the National Security Personnel System Act, would have granted DOD additional pay flexibilities for its large civilian workforce. The bill was referred to the Senate Governmental Affairs Committee. On June 4, 2003, the committee conducted a hearing on the bill. Following the hearing, Senators George V. Voinovich and Thomas Carper asked then-Comptroller General David M. Walker to respond to several additional questions about DOD's ability to motivate and control its workforce. Walker's response, submitted on July 3, 2003, included the following comments:

Based on our experience, while DOD's leadership has the intent and the ability to transform the department, the needed institutional infrastructure is not in place in a vast majority of DOD organizations.... In the absence of the right institutional infrastructure, granting additional human capital authorities will provide little advantage and could actually end up doing damage if the authorities are not implemented properly by the respective department or agency.¹³

The bill was reported by the Committee on Governmental Affairs on September 9, 2003, and was placed the Senate Legislative Calendar, but was not passed. Another bill that addressed DOD personnel, however, H.R. 1588, was concurrently moving through the legislative process. H.R. 1588, the National Defense Authorization Act for Fiscal Year 2004, set definitions and provided guidelines for a new DOD personnel system. The Senate passed the bill, as amended, by voice vote on June 4, 2003. Then-President George W. Bush signed the legislation on November 24, 2003, as P.L. 108-136 (117 Stat. 1392).¹⁴

P.L. 108-136, among other things, authorized the director of OPM to "establish, and from time to time adjust, a human resources management system for some or all of the organizational or functional units of the Department of Defense."¹⁵ The law protected employees' collective bargaining rights, and required that the system be "fair, credible, and transparent" and provide "effective safeguards to ensure that the management of the system is fair and equitable and based on employee performance."¹⁶

DOD began transitioning employees to NSPS in 2006. The system has weathered several delays in its implementation, but currently covers 211,000 of DOD's civilian employees.¹⁷

On January 28, 2008, the National Defense Authorization Act for Fiscal Year 2008 (P.L. 110-181) was enacted. The law required the NSPS system to pay annual bonuses and supplements that are closer in value to those given GS employees. More specifically, the law required NSPS employees with satisfactory ratings to receive at least 60% of the annual pay increase given to GS

¹³ U.S. General Accounting Office, *Posthearing Questions Related to Proposed Department of Defense (DOD) Human Capital Reform*, GAO Report GAO-03-965R (Washington: July 3, 2003).

¹⁴ S. 1050 was introduced by Senator John Warner and reported to the Senate (S.Rept. 108-46) by the Senate Committee on Armed Services on May 13, 2003. Earlier, on May 7 and 8, 2003, the Senate Armed Services Committee marked up the bill.

¹⁵ 117 Stat. 1622.

¹⁶ 117 Stat. 1623.

¹⁷ Bradley Bunn, "Statement Before the Defense Business Board Task Group on the National Security Personnel System," June 25, 2009, <http://www.defenselink.mil/dbb/pdf/pdf/Bunn%20Written%20Statement%20-%20DBB%20Public%20Meeting%20-%2025June2009.pdf>

employees, and ensured that all employees receive a pay supplement to keep pace with growing labor costs.¹⁸ Additionally, on May 22, 2008, DOD and the Office of Personnel Management jointly published proposed rules in the *Federal Register* that clarified NSPS labor-management regulations.¹⁹ The July 2009 Review of the National Security Personnel System performed by the Defense Business Board recommended DOD a “reconstruction” of NSPS, saying a “‘fix’ could not address the systemic problems discovered” during the review.²⁰

NSPS Implementation

The timetable for implementing NSPS changed several times. Initially, DOD planned to publish details of the new system by April 2004, and transition 300,000 civilian DOD employees to NSPS by October 1, 2004. In early February 2004, then-Secretary of Defense Donald Rumsfeld named then-Navy Secretary Gordon England as the DOD official responsible for negotiating with labor organizations on the personnel reform effort.²¹ On April 14, 2004, Mr. England announced that implementation of the NSPS would be phased in over several years so that all eligible DOD employees would be covered by October 1, 2006.

Mr. England announced more specific implementation steps and a revised implementation timetable on December 15, 2004.²² Civilian DOD employees converting to NSPS were to be grouped into three “spirals” or phases of implementation. Spirals are further separated into three distinct implementation segments. Spiral One was scheduled for implementation over 18 months beginning around July 2005 and covering some 60,000 employees.²³ On October 26, 2005, DOD

¹⁸ U.S. Congress, Senate Committee on Homeland Security and Governmental Affairs, Subcommittee on Oversight of Government Management, the Federal Workforce, and the District of Columbia, *Improving Performance: A Review of Pay-For-Performance Systems in the Federal Government*, 110th Cong., 2nd sess., testimony of Bradley Bunn, program executive officer of the National Security Personnel System, July 22, 2008, http://hsgac.senate.gov/public/_files/BunnTestimony072208.pdf. GS employees receive locality pay, a pay supplement designed to close the salary gap between federal workers and private sector workers who have similar jobs. NSPS employees receive a similar pay supplement, but it is called a local market supplement (LMS).

¹⁹ U.S. Department of Defense, “National Security Personnel System,” proposed rule, 73 *Federal Register* 29882, May 22, 2008.

²⁰ Defense Business Board, *Report to the Secretary of Defense: Review of the National Security Personnel System*, Report FY09-06, July 2009, p. 4, http://www.defenselink.mil/dbb/pdf/Review_of_National_Security_Personnel_System_Final_Report.pdf. The Defense Board Report included a variety of recommendations for NSPS including a recommendation to reestablish partnerships with relevant unions.

²¹ The National Security Personnel System Program Executive Office was established in April 2004, and Secretary England announced on May 24, 2004, that Mary E. Lacey, a member of the Senior Executive Service, would serve as the program executive officer. Earlier, on February 13, 2004, OPM Director James named George Nesterchuk as a senior advisor, and announced that he would serve as the lead OPM official on design of the NSPS.

²² U.S. Department of Defense, Office of the Assistant Secretary of Defense (Public Affairs), *DOD Selects First Group for National Security Personnel System*, News Release No. 1286-04, December 15, 2004. Available on the Internet at <http://www.defenselink.mil/releases/release.aspx?releaseid=8069>. DOD stated that the reason for postponing implementation was to “provide technical corrections and adjustments to NSPS policies and procedures.”

²³ Spiral 1.1 covered 9,900 employees in the Navy, Army, and Air Force. Many of these employees were involved in human resources within the military branches. An additional 1,200 employees were in management and threat reduction positions at DOD. Spiral 1.2 included 65,000 non-bargaining Army, Navy, Air Force, and other DOD employees. Spiral 1.2 included the Army Corps of Engineers, Office of the Secretary of the Army, Marine Corps, Fleet Forces Command, Air Combat Command, Air Force Materiel Command, and Air Force Space Command. Spiral 1.3 included 35,362 DOD employees, including more employees from the Office of the Secretary of the Army and Army Corps of Engineers. Additionally, employees in the Space and Naval Welfare Systems Command, U.S. Air Forces Europe and Headquarters, and U.S. Army Medical Command were included. Spiral 2 would incorporate an anticipated 72,333 additional employees into NSPS. Spiral 2.1 includes employees at the Headquarters Department of the Army, (continued...)

announced further revised NSPS plans, and pushed back initial implementation of the system to calendar year 2006.²⁴ On January 17, 2006, DOD identified the 11,124 employees in Spiral 1.1, the first employees to enter NSPS.

NSPS began its phase-in of Spiral 1.1 in April 2006.²⁵ Spirals 1.1, 1.2, and 1.3 were completed in March 2007.²⁶ Spiral 2 began in October 2007, and was completed in April 2008, with more than 180,000 of roughly 670,000 DOD employees placed in NSPS.²⁷ The final spiral began in October 2008 and was completed in March 2009, adding 14,000 additional employees to NSPS, bringing the total of DOD employees covered by NSPS to 211,000.²⁸

Concerns of Transparency

At times during NSPS's development, some employees and their representative organizations claimed that OPM and DOD had been reluctant to include them in their planning and roll out processes.²⁹ In addition to exempting blue-collar employees from NSPS, P.L. 108-136 required the Secretary of Defense and the Director of OPM to provide DOD employees and their representatives "a written description of the proposed system" and "at least 30 calendar days (unless extraordinary circumstances require earlier action) to review and make recommendations with respect to the proposal."

Some Members voiced concerns that employees and unions were not given this statutorily required access to the agencies' pay-for-performance plans. A March 12, 2004, letter from Senator Daniel Akaka to Secretary of Defense Rumsfeld, for example, urged DOD and OPM to jointly publish all proposals on the NSPS in the *Federal Register* and not as internal regulations in order to promote "openness, transparency, public comment, and scrutiny of the details."³⁰

Government Executive reported that Senator Edward Kennedy wrote to Secretary of Defense Donald Rumsfeld and OPM Director Kay Coles James on November 19, 2004, to voice opposition to DOD's refusal to share the details of the new personnel plans with union officials representing DOD employees in advance of the publication of regulations in the *Federal*

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U.S. Army Medical Command, Commander Naval Installations Command, and U.S. Army training and Doctrine Command. For more information, see NSPS, "Spiral Implementation," http://www.cpms.osd.mil/nsps/spiralimplementation_archive.html.

²⁴ U.S. Department of Defense, "Department of Defense and Office of Personnel Management Announce New Human Resources System," press release, October 26, 2005, <http://www.defenselink.mil/releases/release.aspx?releaseid=9000>.

²⁵ National Security Personnel System, "May 2006 SOFC Captures Attitudes of NSPS Employees," <http://www.cpms.osd.mil/nsps/sofc.html>.

²⁶ National Security Personnel System, "Spiral Implementation."

²⁷ Ibid.

²⁸ Bradley Bunn, "Statement Before the Defense Business Board Task Group on the National Security Personnel System," June 25, 2009, <http://www.defenselink.mil/dbb/pdf/pdf/Bunn%20Written%20Statement%20-%20DBB%20Public%20Meeting%20-%2025June2009.pdf>.

²⁹ American Federation of Government Employees, "AFGE News for DOD Employees: 10 Reasons NSPS is Bad for You," http://www.afge.org/Documents/2009_07_08_10reasonsNSPSisbadforyou.pdf; International Federation of Professional and Technical Engineers, "What's at Stake?: Say No to NSPS," <http://www.unionvoice.org/campaign/iftensps/explanation>.

³⁰ Senator Daniel Akaka, Press Release, "Akaka Queries Agencies on Personnel System Changes," March 23, 2004, http://akaka.senate.gov/public/index.cfm?FuseAction=pressreleases.home&month=3&year=2004&release_id=270.

Register.³¹ Reportedly, DOD believed that to share its intentions would “depart from the intent of the Administrative Procedure Act.”³² Senator Kennedy, in a December 10, 2004, press release, also emphasized development of the new system “in the most transparent way possible.” According to the Senator:

Congress gave the Department of Defense the authority to make major personnel changes affecting 700,000 defense employees, but only with the understanding that those changes would be made in consultation with representatives of the employees. It’s appalling that the Bush Administration is ignoring that understanding by stonewalling the representatives and refusing to let them review personnel changes before they are published.³³

In a February 10, 2005, press release, Senator Joseph Lieberman expressed his deep disappointment with DOD’s and OPM’s refusal to publish the system’s guidelines and include employees in its creation, stating, “The proposal imposes excessive limits on collective bargaining ... changes the appeals process to interfere with employees’ rights to due process ... and ... contains unduly vague and untested pay and performance provisions.”³⁴

DOD Personnel System Proposal

DOD and OPM published proposed rules for NSPS in the *Federal Register* on February 14, 2005.³⁵ In the November 1, 2005 final rules, which were also published in the *Federal Register*, DOD and OPM stated that the GS personnel system failed to allow the department to keep pace with the George W. Bush Administration’s demands to “transform the way we think, the way we train, the way we exercise, and the way we fight.”³⁶

At best, the current personnel system is based on 20th century assumptions about the nature of public service and cannot adequately address the 21st century national security environment. Although the current Federal personnel management system is based on important core principles, those principles are operationalized in an inflexible, one-size-fits-all system of defining work, hiring staff, managing people, assessing and rewarding performance, and advancing personnel. These inherent weaknesses make support of DoD’s mission complex, costly, and ultimately risky. Currently, pay and the movement of personnel are pegged to outdated, narrowly defined work definitions; hiring processes are cumbersome; high performers and low performers are paid alike; and the labor system encourages a dispute-oriented, adversarial relationship between management and labor. These systemic inefficiencies detract from the potential effectiveness of the Total Force. A more flexible, mission-driven system of human resources management that retains those core principles will provide a more cohesive Total Force....

³¹ David McGlinchey, “Legislator Says Withholding Pentagon Personnel Plans Violates Laws,” *Government Executive*, November 29, 2004, <http://www.govexec.com/dailyfed/1104/112904d1.htm>; and David McGlinchey, “Back and Forth,” *Government Executive*, December 16, 2004, <http://www.govexec.com/dailyfed/1204/121604pb.htm>.

³² Ibid.

³³ Senator Edward M. Kennedy, Press Release, “Senator Edward M. Kennedy Statement on Response By Bush Administration on Transparency in National Security Personnel Regulations,” December 10, 2004.

³⁴ Senator Joe Lieberman, “Lieberman Condemns Proposed DOD Personnel Rules,” Press Release, February 10, 2005.

³⁵ U.S. Office of Personnel Management, “National Security Personnel System,” 70 *Federal Register* 7552, February 14, 2005.

³⁶ U.S. Department of Defense and Office of Personnel Management, “Department of Defense Human Resources Management and Labor Relations Systems; Final Rule,” 70 *Federal Register* 66117.

The immense challenges facing DoD today require a civilian workforce transformation: Civilians are being asked to assume new and different responsibilities, take more risk, and be more innovative, agile, and accountable than ever before. It is critical that DoD supports the entire civilian workforce with modern systems—particularly a human resources management system and a labor relations system that support and protect their critical role in DoD’s Total Force effectiveness. The enabling legislation provides the Department of Defense with the authority to meet this transformation challenge.³⁷

Description of the National Security Personnel System

To date, the vast majority of employees that have transitioned to NSPS are white-collar, non-bargaining DOD personnel.³⁸ Each employee in the NSPS system is assigned to a career group, a pay band, and a pay schedule. Instead of the 15-step GS pay system, those who are in NSPS have pay bands that usually encompass a wider pay range than a single GS grade.³⁹ The wider pay bands are designed to give managers greater flexibility to hire qualified employees at a higher rate of pay than they could under the GS scale, and to retain high-performing employees by increasing their pay at a faster pace than was possible under the GS scale. Pay bands, like GS grades, limit minimum and maximum pay rates. Unlike the GS scale’s pay grades, pay bands do not have steps through which employees advance automatically with satisfactory job performance. Instead, in NSPS, funds formerly used to pay for within-grade, quality-step, and other increases in the general schedule are pooled and used to fund the pay increases determined at the end of the performance appraisal cycle.⁴⁰

NSPS contains four career groups: Standard Career Group; Scientific and Engineering Career Group; Investigative and Protective Services Career Group; and Medical Career Group. According to DOD’s NSPS website, “[c]areer groups are sets of occupations that involve similar types of work and have similar career and pay progression patterns. Career groups are based on mission or function, nature of the work, qualifications or competencies, promotion or pay progression patterns, and relevant labor market features.”⁴¹

³⁷ Ibid., 70 *Federal Register* 66118.

³⁸ P.L. 110-181 removed blue-collar DOD employees from NSPS eligibility. In June 25, 2009 testimony before the Defense Business Board Task Group, Bradley Bunn said 685 bargaining employees were covered by NSPS. Bradley Bunn, “Statement Before the Defense Business Board Task Group on the National Security Personnel System,” June 25, 2009, <http://www.defenselink.mil/dbb/pdf/pdf/Bunn%20Written%20Statement%20-%20DBB%20Public%20Meeting%20-%2025June2009.pdf>.

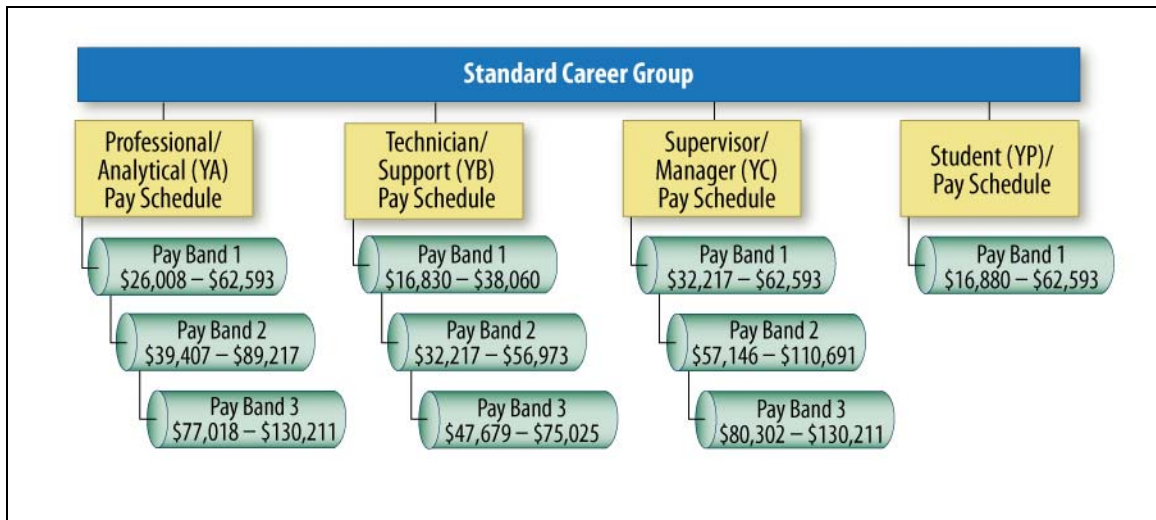
³⁹ The General Schedule contains 15 pay grades, with higher grade levels reserved for employees with higher salary levels. Higher pay grades are those with higher numbers. Within each pay grade are 10 steps through which employees climb based on a job performance that is acceptable or better. The FY2009 GS pay scale is available from the U.S. Office of Personnel Management at <http://www.opm.gov/oca/09tables/pdf/gs.pdf>.

⁴⁰ Under the GS pay scale, within-grade increases (WGIs) are “received by federal employees after they have served a specified amount of time at a certain grade level and demonstrated at least an acceptable level of performance.” These increases are provided for by Chapter 53 of Title 5 of the U.S. Code. Regulations for within-grade increase distributions are at 5 C.F.R. 531, Subpart D. Quality-step increases (QSI) are a single step increase to an employee’s basic pay that can be awarded to recognize GS employees who received the highest available rating record and meet other agency criteria. In short, QSI allow faster than normal progression through the GS steps. QSI are provided for under 5 C.F.R. 531, Subpart E..

⁴¹ National Security Personnel System, “Classification Architecture Fact Sheet,” November 2007, p. 1, (continued...)

Finally, NSPS has four pay schedules: Professional/Analytical; Technician/Support; Supervisor/Manager; and Student. And there are between two and four pay bands within each pay schedule. Pay schedules divide employees into groups by the “types of work being performed, knowledge or skill level, and pay ranges.”⁴² Because of the nature of career groups, some groups have higher starting salaries and higher salary caps than others. A Professional/Analytical employee, for example, has a higher salary cap than a Technician/Support employee. Most pay schedules have three pay bands: Expert; Journey; and Entry/Development.⁴³ **Figure 1** uses the Standard Career Group to demonstrate how pay schedules and pay bands fit within career groups.

Figure 1. Standard Career Group’s Pay Schedule and Pay Bands



Source: Department of Defense, “National Security Personnel System Worldwide Pay Table,” <http://www.cpms.osd.mil/ASSETS/8E60EB0AAEE04E4D8AD58EFCACBD2984/StandardCG.PDF>; NSPS, “Classification Architecture Fact Sheet,” November 2007, <http://www.cpms.osd.mil/nsps/docs.22may08/finalclassificationarchitecturefact.pdf>.

Performance Appraisal

Within 30 days of the start of a new performance-evaluation period—which runs from October 1 through September 30 of each year—each employee is to be issued a performance plan, which outlines his or her performance criteria and goals for the year.⁴⁴ The performance expectations in

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<http://www.cpms.osd.mil/nsps/docs/FinalClassificationArchitectureFact.pdf>. The National Security Personnel System also publishes a list of all DOD occupations and their career group classification at http://www.cpms.osd.mil/nsps/docs/implementing_issuances/1920Classification.pdf.

⁴² National Security Personnel System, “Classification Architecture Fact Sheet,” p. 2.

⁴³ National Security Personnel System, “Frequently Asked Questions,” <http://www.cpms.osd.mil/nsps/faqs.html>. See also the U.S. Department of Defense, “Compensation Architecture Pay Policy,” p. 52, for a complete list of the NSPS pay bands and rate ranges.

⁴⁴ To be eligible for performance review, an employee must be employed for at least 90 days of the current performance appraisal period. For more information on employees who are covered by NSPS see U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.2.2, <http://www.cpms.osd.mil/nsps/docs/1940Performancemanagement2008.pdf>. The 30-day requirement may be extended up to 60 days without affecting employee pay, see SC1940.5.6.1, p. 8.

the plan “shall support and align with the DoD mission and its strategic goals, organizational program and policy objectives, annual performance plans, and other measures of performance.”⁴⁵ These goals can be generalized across the department, or they can be specific to an individual employee.⁴⁶ Performance elements can include knowledge of the department’s standard operating procedures, specific goals or objectives, contributions to the department that are expected of the employee, and overall employee conduct and behavior.⁴⁷ An employee is required to meet with his or her supervisor at least one time during his or her performance-appraisal period prior to a final evaluation.⁴⁸ The interim evaluation is to “acknowledge achievements and suggest areas for improvement, and provide meaningful dialogue and exchange of concerns.”⁴⁹ A supervisor is responsible for informing an employee which performance criteria are considered more important and may be weighted higher in his or her evaluation.⁵⁰ A supervisor should also communicate “measures of job objective accomplishment (quantitative, qualitative, timeliness).”⁵¹ Performance expectations, or competencies, “should be reviewed regularly,”⁵² and “[s]upervisors are encouraged to involve employees in the development of their job objectives and the identification of applicable contributing factors.”⁵³ Supervisors are encouraged to engage in continued dialogue with employees throughout the performance appraisal period, and to update individual performance plans as necessary.⁵⁴

An employee has 24-hour online access to his or her performance plan through the Performance Appraisal Application (PAA) 2.0.⁵⁵ The application runs through computer programs that already exist on the Defense Civilian Personnel Data System (DCPDS). The online performance plan is available to both employees already in NSPS and those who will transition to NSPS. The DCPDS website also includes a conversion calculator for employees who are scheduled to transition from the GS to NSPS.⁵⁶

At the end of the performance appraisal period, employees are encouraged to provide supervisors with a self assessment in each competency to “better inform the rater of performance and contribution.”⁵⁷ Supervisors are to evaluate narratively each employee using the performance criteria, and then translate the narrative into a five-point numeric scale, with the lowest score of 1

⁴⁵ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.5.1, p. 6.

⁴⁶ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940 5.2.1.1, p. 6.

⁴⁷ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.5.2.1.2 - SC1940 5.2.1.5, pp. 6-7.

⁴⁸ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.5.4.1., p. 7.

⁴⁹ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.6.4.1., p. 11.

⁵⁰ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.5.7.1., p. 8.

⁵¹ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.5.4.5. - SC1940.5.4.8., p. 7.

⁵² U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.5.5., p. 7.

⁵³ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.5.7, p. 8. Management has the final say on what is included in a performance evaluation.

⁵⁴ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.6.1. - SC1940.6.3.1, p. 10. DOD prefers face-to-face dialogue “for performance-based issues.”

⁵⁵ For more information on the PAA, see National Security Personnel System, “Performance Appraisal Application,” <http://www.cpms.osd.mil/nsps/paa.html>.

⁵⁶ National Security Personnel System, “GS to NSPS Conversion Calculator,” <http://www.cpms.osd.mil/nsps/conversion/index.html>.

⁵⁷ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.9.2., p. 14.

and the highest of 5.⁵⁸ When evaluating individual criteria, supervisors may choose to include a “contributing factor” that reflects “the manner of performance important for the accomplishment of the job objective.”⁵⁹ Contributing factors include technical proficiency, critical thinking, cooperation and teamwork, communication, customer focus, resource management, and leadership.⁶⁰ In general, no more than three contributing factors should be considered when evaluating a single criterion, and leadership should be considered when evaluating any supervisory element.⁶¹ Each contributing factor may be used to increase or decrease a competency’s numeric rating by one point. For example, if the employee demonstrated critical thinking when performing a competency, his or her score for that criterion could rise from 3 to 4. In contrast, if the employee failed to use critical thinking, he or she would receive no additional point, or a supervisor may decide to take a point away from his or her numeric assessment, dropping a score from 3 to 2.⁶² Supervisors do not have to use whole numbers when assessing employees, but final ratings—the recommended rating of record—must be rounded to the nearest whole number.

Each numeric performance rating matches to a nominal one (Table 1).

Table 1. Numeric Performance Evaluation Rating of Record and Its Corresponding Nominal Descriptor

Numeric Rating of Record	Corresponding Nominal Rating
1	Unacceptable
2	Fair
3	Valued Performer
4	Exceeds Expectations
5	Role Model

Source: U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” available at <http://www.cpms.osd.mil/nsps/docs/1940Performancemanagement2008.pdf>.

An employee must score at least a three—which is equal to a nominal rating of “valued performer”—to be eligible for performance-based pay increases.⁶³ If an employee scored a one on any individual objective, their overall rating is required to be a one.⁶⁴

⁵⁸ Closeout assessments are also required when a supervisor leaves his or her position or if the employee leaves his or her position. For additional information see U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.6.5.- SC1940.6.5.4.3., pp. 11-12.

⁵⁹ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.5.7.5.

⁶⁰ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.5.7.5.1.1. - SC1940.5.7.5.1.7., pp. 9-10.

⁶¹ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.5.7.5.2., p. 10. A contributing factor may not be used to raise the rating score of a competency rated at 2 or lower.

⁶² U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.10.5., p. 17.

⁶³ National Security Personnel System, “Frequently Asked Questions,” <http://www.cpms.osd.mil/nsps/faqs.html>. Basic pay increases are determined annually by the department. For more information see U.S. Department of Defense, SC1930 Subchapter 1930: Compensation Architecture Pay Policy, p. 5, http://www.cpms.osd.mil/nsps/docs/implementing_issuances/1930Compensation.pdf.

⁶⁴ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.10.3.3, pp. 17.

If an employee is performing below expectations at any time throughout the appraisal process, supervisors and management must determine “corrective action,” which may include “remedial training, an improvement period, a reassignment, an oral or written warning, a letter of counseling, a written reprimand, and/or adverse actions.”⁶⁵ As of June 10, 2008, NSPS corrective action may also include reduction in salary as well as retention of pay, so an employee may have his or her pay withheld and/or his or her salary decreased concurrently if his or her performance is deemed unsatisfactory.⁶⁶

Within 10 days of receiving his or her performance evaluation, an employee may request a reconsideration of the rating by submitting “a written request for reconsideration to the pay pool manager.” The request must include a copy of the rating and a statement clarifying which part of the rating is being challenged. A copy of the reconsideration request also may be given to the rating official and the human resources office.⁶⁷ Within 15 days of receiving the request, the pay pool manager is to render a written statement explaining his or her determination. If the employee remains unsatisfied, he or she may—within five days of receiving the pay pool manager’s decision—submit a written request for final review with the Performance Review Authority (PRA),⁶⁸ which oversees all pay pools and ensures consistency in performance and evaluations across the agency. The PRA has 15 days to respond to the request. Bargaining employees may also file a grievance under the agency’s negotiated grievance process.⁶⁹

In a January 1, 2008, *Government Executive.com* article, a DOD executive director said that supervisors and managers in the agency would need to spend 40 to 60 hours per employee per year on performance evaluations and ratings. These hours were to include at least four conversations with each employee annually.⁷⁰ On April 1, 2009, Brenda S. Farrell, director of defense capabilities and management at the Government Accountability Office (GAO), testified that DOD “employees and supervisors were concerned about the excessive amount of time required to navigate the process.”⁷¹

Linking Performance to Pay

The agency-wide performance-based pay pool is comprised of three funding sources:

⁶⁵ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.8 - SC1940.8.3.2.7., pp. 12-13. An employee’s salary may be reduced for unacceptable performance at any time during an evaluation, but employee salary may be reduced only one time in any 12-month period. See SC1940.8.4.3., p. 13.

⁶⁶ National Security Personnel System, “Significant Changes to Approved Implementing Issuances,” <http://www.cpms.osd.mil/nsps/docs/FinalNSPSSigChangesInfoSheet.pdf>.

⁶⁷ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.12.4.1., p. 22.

⁶⁸ A PRA “provides oversight of several pay pools, and addresses the consistency of performance management policies.” See U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.4.1, p. 4.

⁶⁹ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.12.5., p. 24.

⁷⁰ Brittany Ballenstedt, “FEATURES: Freedom to Manage,” *Government Executive.com*, January 1, 2008, <http://www.governmentexecutive.com/features/0108-01/0108-01s1.htm>.

⁷¹ The information came from discussion groups between GAO and DOD employees and supervisors. U.S. Government Accountability Office, *HUMAN CAPITAL: Improved Implementation of Safeguards and an Action Plan to Address Employee Concerns Could Increase Employee Acceptance of the National Security Personnel System*, GAO-09-464T, April 1, 2009, p. Highlights, <http://www.gao.gov/new.items/d09464t.pdf>.

- basic pay funds that ... were historically spent on within-grade increases, quality-step increases, and promotions between general schedule grade levels that no longer exist under NSPS;
- funds (if any) that remain available from the government-wide general pay⁷² increase after the Secretary has exercised his authority to fund any Rate Range Adjustments⁷³ and/or Local Market Supplements⁷⁴; and
- funds spent for performance-based cash awards.⁷⁵

Within the larger pay pool are smaller pay pools for groups of employees “who share in the distribution of a common pay-for-performance fund.”⁷⁶ Group pay pools are divided by organization structure, employee job function, location, and organization mission.⁷⁷

In NSPS, each employee may be assigned a certain number of performance pay shares. Each pay share represents a monetary value that is a predetermined percentage of pay that will be used to calculate performance-based pay increases. The amount of pay shares allocated to each employee reflects his or her numerical performance rating: the higher an employee’s numeric rating, the more shares he or she is allocated. Employees with a performance rating of 1 or 2 are assigned no performance shares. The pay pool panel,⁷⁸ which consists of DOD administrators and senior staff and assigns performance shares to employees, may award an employee with a rating of 3 either one or two shares; a rating of 4 can warrant three or four shares. An employee with a rating of 5 may receive either five or six performance shares. **Table 2** shows the performance shares allowed for each of the 5 possible ratings of record.

Table 2. Performance Shares Available at Each Rating of Record

Rating of Record	Performance Share Available at Rating Level
1	No Shares
2	No Shares
3	1 - 2 Shares

⁷² Normally, a law is passed each year that increases the basic pay of civilian federal employees. The amount of the annual increase is supposed to be based on the percentage change in the Employment Cost Index, which measures changes in private sector labor costs and is maintained by the Bureau of Labor Statistics. For more information on annual federal workforce pay increases see CRS Report RL34463, *Federal White-Collar Pay: FY2009 Salary Adjustments*, by Barbara L. Schwemle.

⁷³ Rate Range Adjustments occur when the minimum and maximum pay levels for each pay range shifts.

⁷⁴ “Local market supplements (LMSs) are additional payments to employees in specified local market areas, occupations, specializations, or pay bands that are not adequate by world-wide pay band rate ranges. LMSs replace locality pay and special salary rates in NSPS. There are no special salary rates in NSPS.” See U.S. Department of Defense, “National Security Personnel System: Local Market Supplement Fact Sheet,” April 2006, <http://www.schriever.af.mil/shared/media/document/AFD-060913-022.pdf>.

⁷⁵ U.S. Department of Defense, “SC1930 Subchapter 1930: Compensation Architecture Pay Policy,” SC1930.9.3 - SC1930.9.4.5., pp. 12-13. Funds for performance based cash awards are available only as pay bonuses and will not impact an employee’s rate of basic pay.

⁷⁶ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.11.1.1. p. 19.

⁷⁷ Ibid.

⁷⁸ The pay pool panel “is a board of management officials who are usually in positions of line authority or in senior staff positions with resource oversight for the organizations, groups, or categories of employees comprising the pay pool membership.” See “SC1940 Subchapter 1940: Performance Management,” SC1940.4.3., p. 4.

Rating of Record	Performance Share Available at Rating Level
4	3 - 4 Shares
5	5 - 6 Shares

Source: U.S. Department of Defense, "SC1940 Subchapter 1930: Compensation Architecture Pay Policy," SC1930-1, p. 9, http://www.dtic.mil/whs/directives/corres/pdf/1400.25_SC1930.pdf.

If a single performance share, for example, equaled 1% of an employee's pay, that employee's pay supplement is calculated by multiplying his or her basic pay by the number of performance shares they have been assigned. An employee with 5 performance shares, therefore, would be entitled to a performance-based pay increase that was equal to 5% of his or her basic pay.⁷⁹ The pay pool manager ensures that the pay performance shares are distributed in a legal and consistent manner.⁸⁰ An employee who is at the maximum level of his or her pay band may receive his or her performance-based bonus as a one-time lump sum paid at the beginning of the following year. The lump sum does not count as basic pay, and is not included when calculating an employee's pension, life insurance, premium pay, or other retirement benefits.⁸¹

NSPS pay also includes a local market supplement (LMS), which functions much like locality pay or special rates on the GS scale. LMS is an "additional payment to employees in specified local market areas, occupations, specializations, or pay bands."⁸² The supplements are used to attract certain employee expertise, bridge the difference in labor costs in the public or private sector, and provide additional pay to employees who work in a hazardous environment. LMSs are added to base salary, and, therefore, are included when calculating pension, life insurance, premium pay, and other retirement benefits. Employees must have been employed by the agency for at least 90 days and have a performance evaluation of 2 ("Fair") or higher to be eligible for the LMS increase.⁸³ Unless the Secretary of Defense deems otherwise, the LMS is usually equal to annual locality pay increases, which are based on cost of labor differences between federal and non-federal employees within the same geographic area.

In addition to pay increases that are awarded based on annual performance evaluations, DOD employees may receive discretionary performance payouts that include Extraordinary Pay Increases (EPI) and Organization Achievement Recognitions (OAR). Only employees who have an annual performance evaluation of 5 are eligible for an EPI, which can be awarded as an increase in basic salary or as a one-time lump sum. OARs award members of a team, organization, or branch that advanced department goals. OARs may be awarded as an increase in basic pay or as a one-time lump sum. Employees must have a numeric performance evaluation of 3 or higher to be eligible for an OAR.⁸⁴

⁷⁹ Ibid., pp. 14-16. The formula is as follows [EMPLOYEE PERFORMANCE PAYOUT = BASIC PAY x PERFORMANCE SHARES x PERFORMANCE SHARE VALUE]

⁸⁰ U.S. Department of Defense, "SC1940 Subchapter 1940: Performance Management," p. 4, http://www.cpms.osd.mil/nsps/docs/implementing_issuances/1940PerformanceManagement.PDF.

⁸¹ U.S. Department of Defense, "SC1930 Subchapter 1930: Compensation Architecture Pay Policy," SC1930.8.2.7.1., p. 11.

⁸² National Security Personnel System, "Local Market Supplements Fact Sheet," <http://www.schriever.af.mil/shared/media/document/AFD-060913-022.pdf>.

⁸³ "SC1930 Subchapter 1930: Compensation Architecture Pay Policy," SC1930.8.1.2.2.1.2., p. 7.

⁸⁴ U.S. Department of Defense, "SC1930 Subchapter 1930: Compensation Architecture Pay Policy," p. 57.

Litigation

On November 7, 2005, a coalition of ten unions that represent DOD employees—including the American Federation of Government Employees (AFGE)—filed a lawsuit in federal district court challenging the DOD’s final regulations for NSPS published in the *Federal Register*.⁸⁵ On February 27, 2006, the court enjoined the regulations, saying they failed to ensure collective bargaining rights; did not provide for independent, third-party review of labor relations decisions; and failed to provide a fair process for appealing adverse actions.⁸⁶ DOD originally stated that it would not appeal the decision, but the Department of Justice—on behalf of DOD and OPM—filed an appeal on April 17, 2006.

The United States Court of Appeals for the District of Columbia reversed the federal district court decision and upheld the DOD’s regulations, saying the National Defense Authorization Act “grants DOD expansive authority to curtail collective bargaining through November 2009.”⁸⁷ The decision also upheld all other regulations that were contested by the unions. On July 2, 2007, the coalition of unions requested a full court review of the appellate court decision. The courts denied the request on August 10, 2007. On August 29, AFGE filed an appeal with the U.S. Supreme Court to stop DOD implementation of NSPS. On September 5, 2007, the Court denied the motion for a stay, and DOD continued its implementation of NSPS.⁸⁸

The 110th Congress

Hearings

Committees in both congressional chambers continued to hold hearings on performance-based-pay systems, with a focus on NSPS. Some common themes throughout the hearings were DOD employees’ mistrust of the system and concerns over how much time the agency would need to fully implement NSPS. On March 6, 2007, the House Committee on Armed Services’ Subcommittee on Readiness, held a hearing on DOD’s NSPS pay, at which Members questioned whether NSPS was “working,” and whether it was adjusting to the challenges it faced. Representatives from DOD stated that the system was effective.

It is early in the journey as it will take years before the Department realizes all of the results NSPS was designed to produce, but we are already showing a powerful return on investment.

⁸⁵ U.S. Congress, House Committee on Armed Services, Subcommittee on Readiness, *The National Security Personnel System of the Department of Defense*, testimony by John Gage, national president of the AFGE, March 6, 2007.

⁸⁶ *Am. Fed’n of Gov’t Employees v. Rumsfeld*, 422 F. Supp. 2d 16 (D.D.C. 2006), http://www.afge.org/Documents/2006_02_27RumsfeldDecision.pdf. The passage of the National Defense Authorization Act for Fiscal Year 2008 on January 28, 2008, prompted AFGE to drop its lawsuit against DOD, saying the legislation “effectively corrected” NSPS’s collective bargaining issues. For more information see American Federation of Government Employees, “Defense Authorization Bill Provides NSPS Fix, press release, January 30, 2008, <http://www.afge.org/index.cfm?page=PressReleases&PressReleaseID=820>.

⁸⁷ *Am. Fed’n of Gov’t Employees v. Gates*, 486 F.3d 1316 (D.C. Cir. 2007), <http://www.afge.org/Documents/Rehearing%20Response%20FINAL.pdf>.

⁸⁸ American Federal of Government Employees, “NSPS Background,” <http://www.afge.org/Index.cfm?Page=NSPSBackground>.

We are seeing an unprecedented training effort focused on performance management for employees and supervisors who are seeing greater communication between supervisors and employees. People are talking about performance, results, and mission alignments. We are seeing increased flexibility and rewarding exceptional performance. Finally, we are seeing positive movement in behaviors and in organizational culture. These early returns are cause for optimism as we continue to deploy the system.⁸⁹

At that hearing, John Gage, the national president of the American Federation of Government Employees, stated that NSPS was “unfair to employees,” and it should be repealed because it violated workers rights to collectively bargain, as well as other protections normally provided to federal employees.⁹⁰

NSPS’s effects on the collective bargaining rights of employees was also considered at a House Committee on Oversight and Government Reform, Subcommittee on the Federal Workforce, Postal Service, and the District of Columbia hearing on March 8, 2007.⁹¹ Kevin Simpson, the executive vice president and general counsel for the Partnership for Public Service, a nonprofit organization that seeks to create a more effective workforce, said that NSPS needed employee support if it were to succeed.

[W]e believe that many (but not all) aspects of NSPS—if implemented with employee involvement and strong congressional oversight—have a potential to make a positive difference and to gain acceptance by the DOD workforce.⁹²

At a February 12, 2008, congressional hearing before the House Subcommittee on the Federal Workforce, Postal Service, and the District of Columbia, Gage said that the NSPS and other merit-based systems were subjective, implemented inconsistently across the agency, and infused with bias. Employees with lower ratings in one office could receive a higher pay bonus than an employee with a higher rating in another, Gage said. Moreover, Gage said, the NSPS system permitted certain managers to determine what percentage of an employee’s pay increase would be distributed as an increase in basic pay or as a one-time lump sum bonus.

Obviously, the more compensation placed in bonuses as opposed to salary increases has profound implications for the employee’s standard of living not only in subsequent years while he or she is still working, but also into retirement.⁹³

⁸⁹ U.S. Congress. House Committee on Armed Forces, Subcommittee on Readiness, *The National Security Personnel System—Is it Really Working?*” oversight hearing, testimony of Michael Dominguez, principal deputy under secretary of defense for personnel and readiness, 110th Cong., 1st sess., March 6, 2007 (Washington: GPO, 2007), http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_house_hearings&docid=f:37887.wais.

⁹⁰ Ibid., testimony of John Gage, national president of the American Federation of Government Employees, 110th Cong., 1st sess., March 6, 2007 (Washington: GPO, 2007), http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_house_hearings&docid=f:37887.wais.

⁹¹ U.S. Congress. House Committee on Oversight and Government Reform, Subcommittee on the Federal Workforce, Postal Service, and the District of Columbia, *The Status of Federal Personnel Reform*, oversight hearing, 110th Cong., 1st sess., March 8, 2007 (GPO: Washington, 2007), http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_house_hearings&docid=f:36547.wais.

⁹² Kevin Simpson, executive vice president and general counsel of the Partnership for Public Service, Testimony before the House Committee on Oversight and Government Reform’s Subcommittee on the Federal Workforce, The Postal Service, and the District of Columbia, oversight hearing on Federal Personnel Systems, 110th Cong., 2nd sess., March 8, 2007, <http://federalworkforce.oversight.house.gov/documents/20070313110929-84384.pdf>.

⁹³ John Gage, National President of the American Federation of Government Employees, AFL-CIO, Testimony Before the House Committee on Oversight and Government Reform, Subcommittee on the Federal Workforce, Postal Service, (continued...)

At a February 29, 2008, hearing before the Senate Committee on Homeland Security and Governmental Affairs' Subcommittee on Oversight of Government Management, the Federal Workforce, and the District of Columbia, then-Comptroller General David M. Walker testified that NSPS could serve as an example for other agencies or departments as they transition to performance-based pay systems.

Most important, we have noted in testimonies and reports that DOD and other federal agencies must ensure that they have the necessary institutional infrastructure in place before implementing major human capital reform efforts, such as NSPS. This institutional infrastructure includes, at a minimum, a human capital planning process that integrates the agency's human capital policies, strategies, and programs with its program goals, mission, and desired outcomes; the capabilities to effectively develop and implement a new human capital system; and the existence of a modern, effective, and credible performance management system that includes adequate safeguards to ensure a fair, effective, nondiscriminatory, and credible implementation of the new system.⁹⁴

At a July 22, 2008 hearing, Bradley Bunn, the program executive officer for NSPS said the pay system was successfully linking employee performance to department goals, but that there were difficulties with the system.

NSPS is a significant change, particularly in the area of performance management, for employees and supervisors. It requires more time and energy than previous systems, and many of our employees are not yet completely comfortable with the system. Performance plans and assessments need improvement, as many are struggling with translating organizational goals into individual, results-oriented, and measurable job objectives. Employees have expressed concern over the pay pool process, and whether it produces fair results. It is clear, however, that employees have a better understanding of how their jobs relate to the mission and goals of the organization, and there is increased communication between employees and supervisors about performance.⁹⁵

At the same hearing, AFGE President John Gage stated that many federal employees "express skepticism about their chances to excel in the workforce" under NSPS. Additionally, Gage stated that "subjectivity and bias pervades the NSPS system."⁹⁶

(...continued)

and the District of Columbia, *Robbing Mary to Pay Peter and Paul: The Administration's Pay-for-Performance System*, oversight hearing, 110th Cong., 2nd sess., February 12, 2008, <http://federalworkforce.oversight.house.gov/documents/20080214121105.pdf>.

⁹⁴ David M. Walker, former comptroller general of the United States, Testimony before the Senate Committee on Homeland Security and Governmental Affairs, Subcommittee on Oversight of Government Management, the Federal Workforce, and the District of Columbia, 110th Cong., 2nd sess., GAO Report, GAO-08-413T, p. 10, February 29, 2008, http://hsgac.senate.gov/public/_files/REVISEDGAO08413T.pdf.

⁹⁵ U.S. Congress, Senate Committee on Homeland Security and Governmental Affairs, Subcommittee on Oversight of Government Management, the Federal Workforce, and the District of Columbia, 110th Cong., 2nd sess., testimony of Bradley Bunn, program executive officer of the National Security Personnel System, July 22, 2008, http://hsgac.senate.gov/public/_files/BunnTestimony072208.pdf.

⁹⁶ U.S. Congress, Senate Committee on Homeland Security and Governmental Affairs, Subcommittee on Oversight of Government Management, the Federal Workforce, and the District of Columbia, 110th Cong., 2nd sess., testimony of John Gage, program executive officer of the National Security Personnel System, July 22, 2008, http://hsgac.senate.gov/public/_files/GageTestimony072208.pdf.

Legislation

On January 28, 2008, the National Defense Authorization Act for Fiscal Year 2008 was enacted (P.L. 110-181). The statute modified certain elements of NSPS, requiring DOD to award every NSPS employee who received a satisfactory rating at least 60% of the pay increase given to GS employees.⁹⁷ The law required NSPS to link “performance management and the agency’s strategic plan”; provide “adequate training and retraining for supervisors, managers, and employees in the implementation and operation of the performance management system”; and create “[a] process for ensuring ongoing performance feedback and dialogue between supervisors, managers, and employees throughout the appraisal period, and setting timetables for review.”⁹⁸ The law also ensures employees’ rights to bargain collectively and establish labor organizations.⁹⁹

Department of Defense Rulemaking

On May 22, 2008, the Department of Defense proposed new rules for NSPS in the *Federal Register*.¹⁰⁰ Some of the proposed new rules include removing references to a new labor-management system in existing NSPS regulations and deleting the prohibition on collective bargaining.¹⁰¹ The proposed rules would flesh out some definitions of pay, and permit employees who were rated “unacceptable” to begin receiving pay increases after they improve their performance—even if the improvement occurs prior to the completion of a full performance appraisal cycle.¹⁰² Comments on the proposed rules were accepted until June 23, 2008. DOD and OPM received more than 500 comments on the proposed regulations.¹⁰³

The 111th Congress

Hearings

On April 1, 2009, the House Committee on Armed Services held a hearing to discuss the future of NSPS. At the hearing, Bradley Bunn, of DOD, testified that NSPS had both some successes and failures. In particular, Mr. Bunn said that the NSPS “performance rating and payout results demonstrate that NSPS organizations are making meaningful distinctions in performance and the associated rewards. We are also seeing improvement in communication between employees and

⁹⁷ P.L. 110-181, sec. 1106. Prior to the enactment of P.L. 110-181, employees with satisfactory performance ratings in the NSPS may have received pay raises that were below those given to federal employee on the general schedule, which is “the federal government’s main pay system that sets the pay rates for federal employees in most white-collar positions not at the senior executive or other senior levels.” See *2006 Federal Employees Almanac*, p. 1.

⁹⁸ P.L. 110-181, sec. 1106.

⁹⁹ The previous labor-relations arrangement prompted litigation from federal employee unions that will be discussed later in this report.

¹⁰⁰ U.S. Department of Defense, “National Security Personnel System,” 73 *Federal Register* 29882, May 22, 2008.

¹⁰¹ *Ibid.*, pp. 28885-29886.

¹⁰² *Ibid.*, p. 29889

¹⁰³ Congress, Senate Committee on Homeland Security and Governmental Affairs, Subcommittee on Oversight of Government Management, the Federal Workforce, and the District of Columbia, 110th Cong., 2nd sess., testimony of John Gage, program executive officer of the National Security Personnel System, July 22, 2008, http://hsgac.senate.gov/public/_files/GageTestimony072208.pdf.

supervisors, and better alignment between performance plans and organizational mission and goals.”¹⁰⁴ Mr. Bunn also said,

“[e]mployees and supervisors are struggling with the more stringent performance measures used in the evaluation process, and employees are questioning whether the ratings are fair. Some of the concern is over whether supervisors have the skills necessary to fairly assess performance, while others question the appropriateness of the pay pool panels being involved in performance ratings. Employees and supervisors, particularly those who are new in the system, often struggle to define measurable, results-oriented job objectives, and have difficulty in writing narrative assessments.”¹⁰⁵

Also at the hearing, Darryl Perkinson, the national president of the Federal Managers Association, testified that rewarding federal employees for quality performance was a desirable goal, but NSPS was not always an effective tool to execute that goal.

Overall, FMA managers and supervisors believe a switch to pay-for-performance is necessary not only to compete with the private sector for talent, but also to encourage and reward high performance. The time for rewarding employees simply for longevity has passed. Many of the hard-working federal managers entering NSPS want to be rewarded for the job they do. However, the system is not without its flaws.¹⁰⁶

Among the concerns Perkinson expressed from employees was a belief that their evaluations were unfair or inaccurate.

Many employees continue to feel uncomfortable in the assessment of their own work as required under NSPS. Inadequate training in this area has contributed to employees’ lack of confidence in the delivery of their own rating, as they are not sure how to properly convey the value of the work they perform each day.¹⁰⁷

Legislation

Both the House and Senate included language to eliminate NSPS in their versions of the National Defense Authorization Act for Fiscal Year 2010 (H.R. 2647, introduced on June 2, 2009; S. 1390, introduced on July 2, 2009). The defense authorization act’s conference report (H.R. 2647, H.Rept. 111-288), in Section 1113, also included these provisions. Pursuant to the legislation, NSPS will be eliminated by 2012, and DOD would begin removing employees from the pay system six months after the October 28, 2009, enactment of the bill. DOD employees currently in NSPS will be returned to the GS or to whichever pay scale they were on prior to their transition into NSPS. Moreover, the bill required DOD to ensure that no employee’s pay would be reduced as a result of the elimination of NSPS. The bill also afforded the Secretary of Defense the authority to establish a “Department of Defense Civilian Workforce Incentive Fund,” from which

¹⁰⁴ U.S. Congress, House Committee on Armed Services, Subcommittee on Readiness, *Hearing on the National Security Personnel System*, testimony of Bradley Bunn, 111th Cong., 1st sess., April 1, 2009, http://armedservices.house.gov/pdfs/READ040109/Bunn_Testimony040109.pdf.

¹⁰⁵ *Ibid.*, p. 9

¹⁰⁶ U.S. Congress, House Committee on Armed Services, Subcommittee on Readiness, *Hearing on the National Security Personnel System*, testimony of Darryl Perkinson, 111th Cong., 1st sess., April 1, 2009, p. 4 http://armedservices.house.gov/pdfs/READ040109/Perkinson_Testimony040109.pdf.

¹⁰⁷ *Ibid.*, p. 6.

agency officials could provide additional pay incentives to individual employees or employee teams “for purposes of the employment and retention as employees of qualified individuals with particular competencies or qualifications.”¹⁰⁸

On October 7, 2009, House and Senate conferees reported a version of the National Defense Authorization Bill for Fiscal Year 2010 that included language to terminate NSPS. On October 8, 2009, the House agreed to the conference report. The Senate agreed to the conference report on October 22, 2009. On October 28, 2009, the President signed the bill into law.

NSPS Assessments

NSPS has been assessed by both the federal government and private entities. A 2007 OPM assessment of NSPS implementation, for example, concluded that DOD was successfully transitioning to the new system, but found continued measurement of the department’s ability to retain key employees and hire quality workers was needed.¹⁰⁹ In October 2007, three Members of the Virginia congressional delegation—Representatives Tom Davis, Frank Wolf, and James Moran—sent Defense Secretary Robert Gates a letter condemning DOD’s announcement that 110,000 NSPS employees with satisfactory performance ratings would receive pay increases that were equal to only half of the annual pay increase given to GS employees. “[T]hese employees ... reportedly were informed from the outset that for the first year in NSPS they would at least receive their base pay increase.” The Members added:

It would be difficult if not impossible to recruit or retain employees if they could not rely on their promised salaries. But an even more difficult task will be meeting the cost of replacing employees or increasing hiring efforts in general if employees do not have confidence in the personnel system.¹¹⁰

According to media reports, the average raise for employees covered by the NSPS in 2008 was 7.6%—more than double the average raise for employees on the GS pay scale (3.5%—2.5% across the board, and a 1% increase in locality pay).¹¹¹ AFGE President John Gage told the *Federal Times* that he believed the high percentage pay increases will drop in the future because it would cost too much to continue them. NSPS Program Executive Officer Mary Lacy responded by saying the pay system does not cost more to run because some employees get no pay increases, while others receive large ones.¹¹²

In April 2008 media reports, unions criticized NSPS for its lack of transparency. Greg Junemann, president of the International Federation of Professional and Technical Engineers told *Government Executive* that, “Defense is intentionally misleading employees by simply releasing a

¹⁰⁸ H.R. 2647, Sec. 1101(c)(2)(A).

¹⁰⁹ U.S. Office of Personnel Management, *Creating a Foundation for the 21st Century Federal Workforce: An Assessment of the Implementation of the Department of Defense National Security Personnel System*, May 2007.

¹¹⁰ Brittany R. Ballenstedt, “Lawmakers urge Pentagon to hold off on new pay policy,” *Government Executive.com*, October 16, 2007, <http://www.governmentexecutive.com/dailyfed/1007/101607b1.htm>.

¹¹¹ Stephen Losey, “DOD hands out bigger raises,” *Federal Times*, February, 11, 2008.

¹¹² *Ibid.*

[pay raise] number without releasing the data that supports their number. Congress should ask the DOD to release any and all data relating to their 7.6% payout.”¹¹³

In August 2008, the *Federal Times* acquired performance evaluations of 102,239 civilian DOD employees in the NSPS system and analyzed pay outcomes. In one report, the *Federal Times* claimed NSPS was “living up to its promise of tying bigger raises and bonuses to better performance on the job.”¹¹⁴ The *Federal Times* stated that “all but 165 employees at [rating] [l]evels 1 through 5 receive total pay increases that were equal to or greater than the average 3.5 percent pay raise that General Schedule employees received.” But many of these pay increases were distributed as one-time bonuses, and not as increases to an employee’s basic salary that would be paid to the employee in perpetuity. Moreover, when the local market supplement is not included as a performance-based increase, 5,039 employees who were rated as valued performers (level 3) received a pay increase of less than 1 percent.¹¹⁵ According to another *Federal Times* report that used the same data, “[w]hite employees received higher average performance ratings, salary increases and bonuses ... than employees of other races.” In addition, civilian employees at DOD agencies were assigned overall higher performance ratings than civilian personnel in the Air Force, Navy, and Marine Corps. Finally, employees who received similar rating scores were, in some cases, given different pay increases.¹¹⁶

The Government Accountability Office released a report on NSPS in September 2008 stating that DOD had “taken some steps to implement internal safeguards to ensure that NSPS is fair, effective, and credible,” but added “some safeguards could be improved.”¹¹⁷ Specifically, GAO cited nine “safeguards” currently in place that aim to improve NSPS operation, including linking “employee objectives and the agency’s strategic goals and mission,” and requiring “ongoing performance feedback between supervisors and employees.”¹¹⁸ GAO added that DOD could improve the implementation of some of the safeguards by having an uninvested third-party analysis performed on NSPS’s pay determinations as well as requiring publication of department-wide rating results to increase the system’s transparency. Additionally, the report recommended DOD give pay pool administrators and supervisors more guidance on rating employees “appropriately” and charged DOD with creating a plan to combat the increasingly negative perception employees have of NSPS.¹¹⁹

Bradley Bunn responded to GAO’s recommendations on behalf of DOD in September 2008 saying “the [d]epartment does not concur with all the finding and recommendations in the ... report” but “[a]s we have implemented NSPS, we have heard many of the same concerns as your auditors and have attempted to differentiate between those that warrant prompt action, and those that reflect the uncertainty and skepticism that typically accompany major changes.”¹²⁰ Further, DOD disagreed with GAO’s recommendation to require third-party analysis of pay pool

¹¹³ Brittany Ballenstedt, “Management Matters: Pay Potential,” *Government Executive*, April 23, 2008, <http://governmentexecutive.com/dailyfed/0408/042308mm.htm>.

¹¹⁴ Stephen Losey, “Better performers net bigger payouts, NSPS numbers show,” *Federal Times*, August 25, 2008, p. 6.

¹¹⁵ *Ibid.*

¹¹⁶ Stephen Losey, “Is DoD’s New Pay System Fair?” *Federal Times*, August. 10, 2008.

¹¹⁷ U.S. Government Accountability Office, *Human Capital: DOD Needs to Improve Implementation of and Address Employee Concerns about Its National Security Personnel System*, GAO Report GAO-08-773, September 2008, p.3.

¹¹⁸ *Ibid.*, pp. 5-6.

¹¹⁹ *Ibid.*, p. 42,

¹²⁰ *Ibid.*, p. 69.

decisions, saying that NSPS was “fair, equitable, and based on employee performance,” and had clear grievance procedures in place for an employee who disagreed with his or her rating. DOD also disagreed with GAO’s assertion that some rating scores may not have made “meaningful distinctions” among employees’ performances.¹²¹ GAO agreed that it should publish its agency-wide rating results, and said it would take steps to accomplish that goal.¹²²

Prior to his election on November 4, 2008, then-presidential candidate Barack Obama wrote a letter to AFGE President John Gage saying that he had “several concerns about the NSPS pay system,” including “restrictions of bargaining rights, the disconnection between pay and performance despite what employees have been told, the requirement that performance ratings be pushed into a forced distribution, or bell curve, the suppression of wages by permitting bonuses to be paid instead of base salary increases, and the virtual elimination of merit consideration in the promotion process.”¹²³ On October 28, 2009, President Obama signed into law a bill that eliminated NSPS (P.L. 111-84).

For 2009, NSPS employees who were rated a “2” or above were eligible to receive a 1.74% pay increase, or 60% of the GS pay increase for 2009.¹²⁴ Employees rated “3” or higher were additionally eligible to receive a performance-based pay increase.¹²⁵

On April 1, 2009, Brenda S. Farrell, director of defense capabilities and defense management at GAO testified at a congressional hearing on NSPS, and reiterated some of the same concerns about the pay system that were previously reported by GAO.¹²⁶ In her testimony, Ms. Farrell said that DOD had “taken some steps to implement internal safeguards to ensure that the NSPS performance management system is fair, effective, and credible,” but added that implementation of other safeguards could be improved.¹²⁷ The areas cited for possible improvement were as follows:

- to involve employees in the system’s design and implementation;
- to link employee objectives and the agency’s strategic goals and mission;
- to train and retrain employees in the system’s operation;
- to provide ongoing performance feedback between supervisors and employees;
- to better link individual pay to performance in an equitable manner;
- to allocate agency resources for the system’s design, implementation, and administration;

¹²¹ Ibid., p. 72,

¹²² Ibid.

¹²³ Letter from Barack Obama, Candidate for U.S. President, to John Gage, National President of the American Federation of Government Employees, AFL-CIO, September 9, 2008.

¹²⁴ National Security Personnel System, “January 2009 NSPS Payout Fact Sheet” January 2009, <http://www.cpms.osd.mil/nsps/docs/FactSheets/2009payouts.pdf>.

¹²⁵ Ibid. Employees rated “1” were not eligible for any pay increase.

¹²⁶ U.S. Government Accountability Office, *HUMAN CAPITAL: Improved Implementation of Safeguards and an Action Plan to Address Employee Concerns Could Increase Employee Acceptance of the National Security Personnel System*, GAO-09-464T, April 1, 2009, testimony before the Subcommittee on Readiness, Committee on Armed Services, House of Representatives.

¹²⁷ Ibid., p. 5.

- to include predecisional internal safeguards to determine whether rating results are consistent, equitable, and nondiscriminatory;
- to provide reasonable transparency of the system and its operation; and
- to impart meaningful distinctions in individual employee performance.¹²⁸

In July 2009, the Defense Business Board, a federal entity that advises the Secretary of Defense on ways to adopt private sector employee practices in DOD, released its Review of the National Security Personnel System.¹²⁹ The review, which was drafted after the board collected public comment and administered a series of interviews and public meetings, recommended a “reconstruction” of NSPS “that begins with a challenge to the assumptions and design” of the pay scale.¹³⁰ The report also recommended that DOD “reestablish ... a commitment to partnership” by “collaborating with employees through their unions,” “establish DoD’s commitment to strategic management and investment in career civil servants,” and stop moving additional employees into the NSPS system.¹³¹

Although he has not addressed NSPS directly, OPM Director John Berry has called the multitude of performance-based pay structures across the federal government “balkanized.”¹³² Mr. Berry has reportedly stated his desire to create a government-wide performance-based pay system.¹³³

Analysis of Options

DOD is one of many federal departments and agencies seeking to create a more effective workforce. The elimination of NSPS will affect the pay system of more than 200,000 federal employees, all within DOD. Modifying Title 5 of the *U.S. Code*,¹³⁴ another approach, could affect more than 2 million federal employees.¹³⁵ Although Congress has mandated the elimination of NSPS, it has not eliminated all performance-based pay systems across the federal government.¹³⁶ Congress may choose to keep the GS as the primary pay system for federal employees, or it may choose to create a new performance-based pay system in the future. This section analyzes possible legislative, oversight, and policy options for the future of performance-based pay, using examples from DOD’s experience with NSPS.

¹²⁸ *Ibid.*

¹²⁹ Defense Business Board, *Report to the Secretary of Defense: Review of the National Security Personnel System*, Report FY09-06, July 2009, http://dbb.defense.gov/pdf/Review_of_National_Security_Personnel_System_Final_Report.pdf.

¹³⁰ *Ibid.*, p. 4

¹³¹ *Ibid.*

¹³² Information provided electronically to the author by OPM on September 30, 2009.

¹³³ Alyssa Rosenberg, “Administration Will Push for Governmentwide Pay for Performance,” *Government Executive*, May 27, 2009, <http://www.govexec.com/dailyfed/0509/052709ar1.htm>; Tim Kauffman, “OPM: Pay Reform by 2011,” *Federal Times*, June 29, 2009.

¹³⁴ Title 5 of the *U.S. Code* is comprised largely of statutes that govern the federal workforce.

¹³⁵ According to OPM’s Central Personnel Data File, there were at least 2,023,626 employees in federal government as of June 2009.

¹³⁶ For more information on performance-based pay systems in the federal government, see U.S. Office of Personnel Management, *Alternative Personnel Systems in the Federal Government*, Washington, DC, December 2008, <http://www.opm.gov/aps/about/reports/2008APSSstatusReport.pdf>.

Flexibilities

DOD officials have stated that one particularly beneficial flexibility of NSPS is the ability of the department to use higher starting salaries than are available under the GS scale to attract a higher caliber of college graduates to the workforce. Under Title 5 statutes, federal agencies and departments may offer a one-time lump sum recruitment bonus to employees “if the agency has determined that the position is likely to be difficult to fill in the absence of an incentive.”¹³⁷ In contrast, the pay banding system under NSPS allows a department or agency to offer a new recruit a higher starting salary because the bands include a range of pay options that are much wider than the spectrum within individual GS pay grades. Although DOD has cited this pay flexibility as an advantage of the NSPS, the department has presented no data on how many DOD employees were recruited under the NSPS flexibility, the pay levels at which such recruits were hired, or whether these recruits received higher performance appraisal ratings than similar employees hired without (or prior to) use of the NSPS pay flexibilities.

Recruitment and Retention

Prior to the phase out of NSPS, Congress may choose to require DOD to collect data on how it used pay flexibilities to recruit—and possibly retain—effective and efficient federal employees under NSPS. Such information may be useful to Congress in the future if it chooses to authorize a new performance-based pay system. The information could show whether NSPS flexibilities aided in recruitment and retention of effective employees. Measuring effective employee performance, however, is a controversial topic. Sometimes the executive and legislative branches disagree on how an agency’s workforce can best achieve its mission. Congress may need to specifically identify how it would want DOD to define the term “effective employee,” to ensure that any data collected would reflect the policy designs of Congress.

P.L. 108-136 statutorily required DOD to create a pay system that linked pay to employee performance. The performance appraisal system could be used to measure and compare performance ratings among its employees, and provide the federal government an opportunity to record how many employees were recruited or retained with use of this performance-based pay system’s flexibilities. Moreover, the system could be used to compare performance ratings between employees recruited or retained with use of the flexibilities to those NSPS employees who were already in the pay system and were not recruited or retained as a result of new pay flexibilities. Such a comparison may identify whether NSPS attracted and retained more effective government employees than other pay systems—a primary goal of the more flexible pay system. Such analyses may be useful as both Congress and the Administration face whether to maintain the GS pay scale or create a new pay scale that more directly links pay to an employee’s performance.

Employee Resignation

Prior to the NSPS phase out, data could also be collected to determine whether NSPS encouraged employees who did not receive successful performance ratings to leave their positions. NSPS does not give supervisors any additional flexibilities from Title 5 to fire employees. An employee

¹³⁷ U.S. Office of Personnel Management, “Recruitment Incentives,” <http://www.opm.gov/oca/pay/html/recbonfs.asp>. See also 5 U.S.C. § 5753.

rated a “2” under the NSPS rating system, however, does not receive a performance-based pay increase. An employee who is rated “1” receives neither a performance-based pay increase nor the annual across-the-board pay adjustment that is annually enacted. Mr. Bunn suggested that an employee who does not receive performance-based or other pay increases would be likely to resign from his or her position. Congress may consider requiring DOD to compile records on employees with low ratings, and study whether NSPS’s policies to deny such pay increases were, in fact, prompting low performers to resign. Such information may be useful to Congress and the Administration in future determinations of how federal employees should be paid.

Costs

NSPS currently covers approximately one-third of the personnel coverage initially planned. DOD estimated that \$158 million was spent implementing the new pay system from 2005 through 2008.¹³⁸ In September 2008, DOD and OPM estimated that \$143 million will be spent on NSPS from 2009 through 2011.¹³⁹ According to Mr. Bunn, the NSPS pay system does not receive congressional appropriations in excess of what it would have received if it had remained the GS pay system. Instead, any needed additional funding comes from within the DOD’s overall appropriations.¹⁴⁰ Additional costs for NSPS, therefore, consist mainly of the expenses to run the NSPS resources office in Arlington, VA, and costs to create and install performance appraisal software.

DOD employees are covered by a variety of pay scales. The complete cost of running several pay systems within one department has not been calculated. Congress might consider requiring DOD to calculate the costs of creating software for, and implementation of, each unique pay system.¹⁴¹ This cost could then be compared to costs for pay systems of other agencies (e.g., the Department of Veterans Affairs, the Department of Homeland Security, the Department of Treasury, or the Department of Transportation).¹⁴² Congress would then have more thorough information on the costs of running a variety of pay systems, and may gain a greater understanding of which pay systems are more efficient and effective for the federal workforce.

¹³⁸ U.S. Government Accountability Office, *Human Capital: DOD Needs Better Internal Controls and Visibility over Costs for Implementing Its National Security Personnel System*, GAO-07-851, July 2007, Summary, <http://www.gao.gov/new.items/d07851.pdf>. GAO’s investigation found that the actual costs for NSPS could “not be determined because DOD has not established an oversight mechanism to ensure that these costs are fully captured.”

¹³⁹ Department of Defense and the Office of Personnel Management, “National Security Personnel System; Final Rule,” 73 *Federal Register* 56389, September 26, 2008.

¹⁴⁰ Information provided to the author by Bradley Bunn during a face-to-face interview on October 28, 2008.

¹⁴¹ *Ibid.*

¹⁴² DOD is the largest department in the federal government. The Department of Veterans Affairs, which has more than 400,000 fewer employees than DOD, is the second largest federal department. Adding the pay system costs for all four of the other departments mentioned above might offer the most accurate cost comparison. Other federal departments also host a variety of pay systems. The comparison between DOD and the other agencies, therefore, would test whether the costs at DOD are much higher than those at the other departments. For more information on employee counts at federal agencies, see the U.S. Office of Personnel Management’s Central Personnel Data File, *FedScope*, at <http://www.fedscope.opm.gov/>.

Pay Pools

The 211,000 employees currently in NSPS are divided into roughly 1,600 “pay pools.” Each pay pool consists of between 35 and 150 employees.¹⁴³ Employees assigned to a pay pool draw their performance-based pay increases from the same funds. In NSPS, pay pool managers have the authority to increase the size of the funding pot by adding an overall performance bonus to the pool if, for example, the pool’s members as a whole accomplish pre-set goals as a unit.¹⁴⁴ The bonus increase may be small, but could increase the pay of all employees who qualify for performance-based pay increases at the end of the year.

Authorities granted to pay pool managers can help the manager use pay to further motivate employees to perform their jobs. Allowing individual pay pool managers to influence the size of the pay pool pot, however, may prompt employees to believe the payout process is unfair – especially if they are in a pay pool with a manager that does not increase the funding pot. Moreover, if an employee is assigned to a pay pool with colleagues who have disparate job assignments, it may be difficult for a pay pool manager to define overall pay pool goals to which all employees could contribute equally. Some employees may believe that their job assignment may not affect whether pay pool goals are reached. Other employees may believe that their job assignment carries most of the burden toward reaching their assigned pay pool’s goals. If Congress decides to authorize a performance-based pay system in the future, it may choose to remove the ability of pay pool managers to change the size of the funding pot for employees.

Anonymous Pay Pool Ratings

Performance-based bonus amounts in NSPS are determined by both a pay pool manager and pay pool panel, which is a collection of higher-level supervisors within DOD. Each pay pool is assigned its own pay pool panel. Employees are informed of which supervisors serve on their pay pool’s panel.¹⁴⁵ Some employees may personally know members of the pay pool panel or the pay pool manager, while other employees may not. NSPS policies do not require pay pool managers or panel members to remove employees’ names from performance appraisals when they are using the rating scores to determine individual annual payouts.¹⁴⁶ Keeping the names of employees visible during payout determination may cause certain employees to believe favoritism may influence pay pool panel decisions. If Congress chose to create a performance-based pay system in the future, it may consider removing the employee’s name from a performance appraisal to eliminate concerns of favoritism toward a well-known and well-liked employee. Such action may also eliminate concerns of an employee who believes knowledge of his or her identity could harm the payout determination.

Outlier Ratings

Certain organizations within DOD may be staffed with employees who collectively perform either much higher, or much lower, than average units. These outlier units may be assigned to their own pay pool. If an outlier group consists of extraordinarily high-performing employees,

¹⁴³ Information provided to the author by Bradley Bunn during a face-to-face interview on October 28, 2008.

¹⁴⁴ The size of the performance bonus would be relatively small when compared to the size of the overall pay pool pot.

¹⁴⁵ *Ibid.*

¹⁴⁶ *Ibid.*

then the performance-based pay increases for these employees may be less than that of employees with similar ratings in pay pools with colleagues who receive average rating scores.¹⁴⁷ The pay pool is a finite amount of money from which to draw pay increases.¹⁴⁸ If every employee achieves high ratings, the size of the pay pool remains the same. The size of an individual's share, however, may be less than an employee with a similar rating in a different pay pool if his or her pay pool colleagues all receive high ratings. The size of the pay pool's funding pot would remain constant whether the pool was high-performing or low performing. A pay pool that received comparatively low ratings (mostly 2s and 3s), therefore, may have members that receive a disproportionately high payout when compared to a colleague with a similar performance rating from an average or high-performing pay pool. An employee who received a rating of 3 in a low-performing pay pool may receive a payout equal to or greater than an employee who received a 4 in a higher-performing pay pool.¹⁴⁹

Congress may consider NSPS's payout process the appropriate payout process, or it may choose to consider a different payout process if a performance-based pay system is authorized in the future. Performance-based pay system administrators may consider adding or subtracting funding from individual pay pools based on the average performance ratings of the individuals that compose the pay pool. In the case of a comparatively high-performing collection of workers, they could have additional funding added to their pay pool because their ratings were statistically higher than those of average or underperforming divisions. This pay increase would increase the payouts for those high-performing employees. Conversely, employees in comparatively low-performing divisions could have funding removed from their pay pool and decrease the payout for employees with statistically lower performance ratings. Money taken away from pay pools of lower-performing divisions could be reallocated into the pay pools of higher performing divisions. Adding such a provision to a performance-based pay system, however, may cause confusion and frustration among employees. The provision could prompt employees to believe that payout results are inconsistent and arbitrary, and based more on variations among supervisors' ratings approaches than on the relative strengths of individual pools. If employees do not believe their performance will lead to a pay increase of a sizeable value, the system may not operate properly. Additionally, because employee performance may stay consistent from year to year while payouts vary, employees may fail to see a solid link between their performance and their pay increase.

Opportunities for Employee Grievance

Pursuant to NSPS policy, an employee who is dissatisfied with his or her performance appraisal may request a reconsideration of the employee's rating within 10 days of receiving his or her

¹⁴⁷ The size of the NSPS pay pool is constant for each individual pool, unless a pay pool manager chooses to increase the pay pool pot. All money allocated to a pay pool at the beginning of a performance-appraisal cycle must be distributed at the end of the cycle. If employees in a pay pool all receive the highest performance, they must split the pot of money equally and receive a smaller pay increase than if some employees had received lower ratings and had, therefore, qualified for a smaller portion of the pot. Conversely, if all employees received mediocre ratings, they may receive higher payouts because no employees with high performance ratings qualified for a larger performance-based increase.

¹⁴⁸ Although the size of the pay pool funding pot itself is finite, pay pool managers—as noted earlier in this memorandum—can increase the pot size by adding a performance bonus.

¹⁴⁹ DOD officials are currently re-examining NSPS policies on whether an entire allocated funding pot must be used each performance-appraisal year. If, for example, all employees in an assigned pay pool scored a 1—which would not qualify them for a pay increase—it is unclear what would happen to the performance-based pay pot.

rating by submitting “a written request for reconsideration to the pay pool manager.” The request must include a copy of the rating and a statement clarifying which part of the rating is being challenged.¹⁵⁰ Within 15 days of receiving the request, the pay pool manager is to render a written statement that explains his or her determination. If the employee remains unsatisfied, he or she may—within five days of receiving the pay pool manager’s decision—submit a written request for final review with the Performance Review Authority (PRA),¹⁵¹ which oversees all pay pools and ensures consistency in performance and evaluations across the agency. The PRA has 15 days to respond to the request. Bargaining employees may also file a grievance under the agency’s negotiated grievance process.

Congress may consider the NSPS reconsideration process appropriate, or it may choose to consider other options for reconsideration in any future performance-based pay system. Some government agencies have created complaint-handling or internal ombudsman offices. Creation of an ombudsman-like office could serve as a resource for employees who believe the pay system is flawed or treated them unfairly. These offices can be designed in a variety of ways.¹⁵² Among the most essential design decisions are determining the powers and duties of the office, the jurisdiction of the office, and the office’s location within a department or agency. The office’s location would determine to whom the ombudsman would report any findings or recommendations. If, for example, the ombudsman reported to DOD officials, the office may have less influence than if it reported to the Secretary of Defense, President, or Congress. Other decisions to consider when designing an ombudsman’s office are determining who would select and appoint the ombudsman, whether the ombudsman would serve as a neutral fact-finder or an employee advocate, and the office’s annual budget.

New Hires

NSPS requires employees to work with supervisors at the beginning of the performance-appraisal year to determine goals for the year.¹⁵³ A new hire, who serves at least his or her first year of federal service on a probationary period,¹⁵⁴ may not have the necessary information available to determine achievable and effective work goals. Congress may consider the policies adopted by NSPS appropriate. On the other hand, Congress may choose to consider a different performance-based pay system design for future pay systems that could include additional performance-appraisal consultations for new hires during their probationary period. The additional consultations could be used to give probationary employees opportunities to discuss and modify the goals that they and their supervisor create. Congress also may consider requiring additional training for supervisors on how to help acclimate new hires to any federal pay system.

¹⁵⁰ U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.12.4.1., p. 22.

¹⁵¹ A PRA “provides oversight of several pay pools, and addresses the consistency of performance management policies.” See U.S. Department of Defense, “SC1940 Subchapter 1940: Performance Management,” SC1940.4.1, p 4.

¹⁵² For a framework on how ombudsman offices can be designed as well as examples of some operating federal ombudsman offices see CRS Report RL34606, *Federal Complaint-Handling, Ombudsman, and Advocacy Offices*, by Wendy R. Ginsberg and Frederick M. Kaiser. The report focuses on external ombudsman and complaint-handling offices, which serve the public. Office designs for an internal ombudsman, however, may parallel those of an external ombudsman.

¹⁵³ Information provided to the author by Bradley Bunn during a face-to-face interview on October 28, 2008.

¹⁵⁴ 5 C.F.R. § 315, Subpart H.

Measuring Success

DOD asked Congress to grant the department flexibilities from Title 5 of the *U.S. Code* to make the workforce more agile and effective.¹⁵⁵ DOD, however, has not provided to Congress data that would clearly demonstrate the agency has been working toward the goals it sought to achieve when requesting workforce flexibilities.¹⁵⁶ Congress may choose to directly ask for aggregate data on how many employees have been recruited under the NSPS pay system, how quickly employee pay increased in the pay band structure, and how many applications for promotion into a new pay band were processed.¹⁵⁷

In addition, NSPS administrators could aggregate data on information already collected. For example, the Performance Appraisal Application requires supervisors to select the method by which they conduct each of the three annually required employee meetings. These data could demonstrate whether NSPS met its goal of encouraging employee-supervisor face-to-face interaction if they were looked at over time.¹⁵⁸ NSPS has not aggregated such data to determine what percentage of employee performance appraisals are performed face-to-face, via telephone, or via computer. Such information may be helpful when attempting to design a more effective performance-based pay system.

Workplace Incentives

Currently, the federal government can offer its employees a variety of incentives to enhance job performance other than pay increases (5 U.S.C. 5753 and 5754), including retention, recruitment, and relocation incentives. As noted earlier, Congress could enact legislation that would modify Title 5 and create additional recruitment, retention, and relocation flexibilities for a majority of federal departments and agencies.¹⁵⁹ Congress may choose to allocate more funding for existing incentives or enact laws that would create new incentives, giving agencies a variety of rewards for effective employee performance. Among many options is the possibility of permitting departments and agencies to offer additional vacation days or sick leave in order to attract and retain employees. Congress could also require federal employers to offer programs that help

¹⁵⁵ See U.S. Congress, Senate Committee on Governmental Affairs, *Transforming the Department of Defense Personnel System: finding the Right Approach*, testimony of Donald Rumsfeld, 108th Cong., 1st sess., June 4, 2003, S.Hrg. 108-185 (Washington: GPO, 2003), p. 59; and U.S. Congress, House Committee on Government Reform, *Instilling Agility, Flexibility and a Culture of Achievement in Critical Federal Agencies: A Review of H.R. 1836, the Civil Service and National Security Personnel Improvement Act of 2003*, testimony of Paul Wolfowitz, H.R. 1836, 108th Cong., 1st sess., May 4, 2003, H.Hrg. 108-25 (Washington: GPO, 2003), p. 101.

¹⁵⁶ Congress has not statutorily required DOD to submit such data.

¹⁵⁷ NSPS eliminated pay grades, which remain an essential design of the General Schedule. NSPS has fewer pay bands than the GS scale has grades. NSPS, therefore, was designed to cut down on the amount of applications for promotion that would have to be processed each year if the DOD employees remained on the GS scale.

¹⁵⁸ Some employee performance appraisals must be performed via telephone or via computer because the supervisor and the employee are not located in the same geographic area.

¹⁵⁹ Title 5 already includes a variety of pay options including the ability to offer new employees recruitment bonuses in pay (5 U.S.C. § 5753) or offering current employees retention pay (5 U.S.C. § 5754) among other flexibilities. According to the Office of Personnel Management, recruitment and retention incentives are sometimes not used because they lacked the funding to pay for their use. See U.S. Office of Personnel Management, *Recruitment, Retention, and Relocation Incentives: Fiscal Year 2007*, Report to the Congress, Washington, DC, September 2008, p. 4, <http://www.opm.gov/oca/pay/html/3RsReportToCongressCY07.pdf>.

employees pay back school loans.¹⁶⁰ Such programs may attract more recent graduates to federal service. Congress could also consider creating programs that would make child care more accessible to federal employees. Making child care more accessible to federal employees could make federal government an attractive option for potential employees starting a family.¹⁶¹ President Obama and the Office of Personnel Management have also announced their intention to seek health and other benefits for the domestic partners of employees involved in same-sex relationships.¹⁶² Adding new flexibilities to Title 5 could give all government agencies and departments a variety of new options to attract and retain effective federal employees. All of these options may require additional congressional appropriations, as well as changes or additions to existing federal statutes. Congress may also be concerned that such additional incentives may not be necessary during a time of increasing unemployment rates.¹⁶³ Instead, the additional incentives could be made available only in federal agencies where there has been difficulty hiring or maintaining staff.

Concluding Observations

Congress created NSPS and granted DOD pay flexibilities to run the performance-based system. Many members have consistently been interested in ensuring that the federal government maintains a transparent and fair pay system that is trusted by administrators, supervisors, and employees. Unions have, historically, not favored pay-for-performance systems, and DOD's NSPS was no exception. Congress may use NSPS as a model—evidencing both good and bad experiences—for a federal workforce that may transition to a performance-based pay system in the future. NSPS has faced, solved, and failed to solve a variety of challenges in its attempt to attract and retain a high-quality workforce. Overall, NSPS serves as a demonstration of how elements of a performance-based pay system can work or cannot work in certain large federal agencies.

¹⁶⁰ Many federal agencies already have school-loan payback programs, but federal agencies are not required to institute such programs.

¹⁶¹ For more information on vacation time and sick leave within both the public and the private sector in the United States see CRS Report RL34088, *Leave Benefits in the United States*, by Linda Levine.

¹⁶² U.S. President (Obama), "Memorandum for the Heads of Executive Departments and Agencies, Subject: Federal Benefits and Non-discrimination," June 17, 2009, at http://www.whitehouse.gov/the_press_office/Memorandum-for-the-Heads-of-Executive-Departments-and-Agencies-on-Federal-Benefits-and-Non-Discrimination-6-17-09/; and John Berry, *Memorandum for Heads of Executive Departments and Agencies*, Office of Personnel Management, Subject: Federal Benefits for Same-Sex Domestic Partners, July 10, 2009, <http://www.chcoc.gov/Transmittals/TransmittalDetails.aspx?TransmittalId=2384>.

¹⁶³ See U.S. Department of Labor, Bureau of Labor Statistics, "Databases, Tables, and Calculators by Subject," http://data.bls.gov/PDQ/servlet/SurveyOutputServlet?data_tool=latest_numbers&series_id=LNS14000000.

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