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Testimony

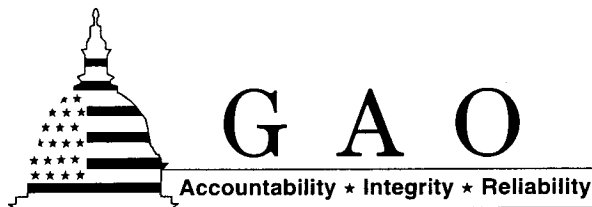
Before the Committee on Armed Services, House of
Representatives

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**DEFENSE
TRANSFORMATION**

**DOD's Proposed Civilian
Personnel System and
Governmentwide Human
Capital Reform**

Statement of David M. Walker
Comptroller General of the United States





Highlights of GAO-03-741T, testimony before the Committee on Armed Services, House of Representatives

DEFENSE TRANSFORMATION

DOD's Proposed Civilian Personnel System and Governmentwide Human Capital Reform

Why GAO Did This Study

DOD is in the midst of a major transformation effort including a number of initiatives to transform its forces and improve its business operations. DOD's legislative initiative would provide for major changes in civilian and military human capital management, make major adjustments in the DOD acquisition process, affect DOD's organization structure, and change DOD's reporting requirements to Congress, among other things.

DOD's proposed National Security Personnel System (NSPS) would provide for wide-ranging changes in DOD's civilian personnel pay and performance management, collective bargaining, rightsizing, and a variety of other human capital areas. The NSPS would enable DOD to develop and implement a consistent DOD-wide civilian personnel system.

This testimony provides GAO's preliminary observations on aspects of DOD's legislative proposal to make changes to its civilian personnel system and discusses the implications of such changes for governmentwide human capital reform. This testimony summarizes many of the issues discussed in detail before the Subcommittee on Civil Service and Agency Organization, Committee on Government Reform, House of Representatives on April 29, 2003.

www.gao.gov/cgi-bin/getrpt?GAO-03-741T.

To view the full testimony, click on the link above. For more information, contact Derek Stewart at (202) 512-5559 or stewartd@gao.gov.

What GAO Found

Many of the basic principles underlying DOD's civilian human capital proposal have merit and deserve serious consideration. The federal personnel system is clearly broken in critical respects—designed for a time and workforce of an earlier era and not able to meet the needs and challenges of our current rapidly changing and knowledge-based environment. DOD's proposal recognizes that, as GAO has stated and the experiences of leading public sector organizations here and abroad have found, strategic human capital management must be the centerpiece of any serious government transformation effort.

More generally, from a conceptual standpoint, GAO strongly supports the need to expand broad banding and pay for performance-based systems in the federal government. However, moving too quickly or prematurely at DOD or elsewhere, can significantly raise the risk of doing it wrong. This could also serve to severely set back the legitimate need to move to a more performance- and results-based system for the federal government as a whole. Thus, while it is imperative that we take steps to better link employee pay and other personnel decisions to performance across the federal government, how it is done, when it is done, and the basis on which it is done, can make all the difference in whether or not we are successful. One key need is to modernize performance management systems in executive agencies so that they are capable of supporting more performance-based pay and other personnel decisions. Unfortunately, based on GAO's past work, most existing federal performance appraisal systems, including a vast majority of DOD's systems, are not currently designed to support a meaningful performance-based pay system.

The critical questions to consider are: should DOD and/or other agencies be granted broad-based exemptions from existing law, and if so, on what basis? Do DOD and other agencies have the institutional infrastructure in place to make effective use of any new authorities? 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 and mission, and desired outcomes; the capabilities to effectively develop and implement a new human capital system; and, importantly, a set of adequate safeguards, including reasonable transparency and appropriate accountability mechanisms to ensure the fair, effective, and credible implementation of a new system.

In GAO's view, as an alternative to DOD's proposed approach, Congress should consider providing governmentwide broad banding and pay for performance authorities that DOD and other federal agencies can use provided they can demonstrate that they have a performance management system in place that meets certain statutory standards, that can be certified to by a qualified and independent party, such as OPM, within prescribed timeframes. Congress should also consider establishing a governmentwide fund whereby agencies, based on a sound business case, could apply for funding to modernize their performance management systems and ensure that those systems have adequate safeguards to prevent abuse. This approach would serve as a positive step to promote high-performing organizations throughout the federal government while avoiding further human capital policy fragmentation.

Chairman Hunter, Mr. Skelton, and Members of the Committee:

It is a pleasure to appear before you today to provide our preliminary observations on the Department of Defense's (DOD) proposed National Security Personnel System (NSPS) included as part of the Defense Transformation for the 21st Century Act of 2003. As you know, I testified on Tuesday on the NSPS before the Subcommittee on Civil Service and Agency Organization, House Committee on Government Reform.¹ We have provided the statement prepared for that hearing to the Armed Services Committee for the record for today's hearing. Therefore, in the interests of brevity this morning, I will highlight some of the major points covered in that statement.

DOD is in the midst of a major transformation and it has undertaken a number of related initiatives to transform its forces and fundamentally improve its business operations. As part of DOD's transformation process, the Secretary of Defense and senior civilian and military leaders have committed to adopt a capabilities-based approach to acquisition planning and to improve the linkage between overall strategy and individual investments. At the same time, DOD has embarked on a series of efforts to achieve strategic savings and improve its business processes, including strengthened financial management, support infrastructure reforms to include base closures, information technology modernization, logistics reengineering, and more strategic human capital management. In that regard, I am pleased to serve as an observer to the Defense Business Practice Implementation Board. Notwithstanding these ongoing efforts, GAO has reported a range of DOD challenges for many years. Importantly, DOD also is covered by 9 of the 25 areas on our January 2003 high-risk list, including the area of strategic human capital management.

The proposed Defense Transformation for the 21st Century Act of 2003 represents a substantive legislative proposal that has far-reaching implications for the way DOD is managed. DOD's legislative initiative would, among other things, provide for major changes in civilian and military human capital management, make important adjustments to the DOD acquisition process, affect DOD's organization structure, and change DOD's reporting requirements to Congress. While my written statement today covers just the proposed civilian personnel reforms, I have some serious concerns with other sections of the proposed legislation especially in connection with the acquisition reform and reporting requirements parts of the DOD proposal, and I look forward to discussing those concerns with the Committee.

DOD's NSPS proposal recognizes that, as GAO has stated and the experiences of leading public sector organizations here and abroad have found, strategic human capital management must be the centerpiece of any serious government transformation effort. Many of the basic principles underlying DOD's civilian human capital proposals have merit and deserve serious consideration. The federal personnel system is clearly broken in critical respects—designed for a time and workforce of an earlier era and not able to meet the needs and challenges of our current rapidly changing and knowledge-based

¹ U.S. General Accounting Office, *Defense Transformation: Preliminary Observations on DOD's Proposed Civilian Personnel Reforms*, GAO-03-717T (Washington, D.C.: Apr. 29, 2003).

environment. The proposed NSPS would provide for wide-ranging changes in DOD's civilian personnel pay and performance management, collective bargaining, rightsizing, and a variety of other human capital areas. The NSPS would enable DOD to develop and implement a consistent, DOD-wide civilian personnel system bringing together the many disparate systems that exist today. DOD officials have said that the Department's current thinking is that NSPS will be based on the work done by DOD's Human Resources Best Practices Task Force. The Task Force reviewed federal personnel demonstration projects and selected alternative personnel systems to identify practices that it considered promising for a DOD civilian human resources strategy. These practices were outlined in a April 2, 2003, *Federal Register* notice asking for comment on DOD's plan to integrate all of its current science and technology reinvention laboratory demonstration projects under a single human capital framework consistent with the best practices DOD identified.²

Given the massive size of DOD and the nature and scope of the changes that are being considered, DOD's proposal also has important precedent-setting implications for federal human capital management in general, and the Office of Personnel Management (OPM), in particular. As a result, NSPS should be considered in that context. Several critical questions are raised by the Department's proposal, including should DOD and/or other agencies be granted broad-based exemptions from existing law, and if so, on what basis; and whether they have the institutional infrastructure in place to make effective use of the new authorities. 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 and mission, and desired outcomes; the capabilities to effectively develop and implement a new human capital system; and importantly, the existence of a modern, effective, and credible performance management system that includes adequate safeguards, including reasonable transparency and appropriate accountability mechanisms, to ensure the fair, effective, and non-discriminatory implementation of a new system. Based on our experience, while the DOD leadership has the intent and the ability to implement the needed infrastructure, it is not consistently in place across DOD at the present time.

I believe that it would be more prudent and appropriate for the Congress to address the authorities that DOD is seeking on a governmentwide basis and in a manner that assures that appropriate performance management systems and safeguards are in place before the new authorities are implemented in any respective agency. This approach would accelerate needed human capital reform throughout the government in a manner that assures reasonable consistency on key principles within the overall civilian workforce. It also would provide agencies with reasonable flexibility while incorporating key safeguards to help maximize the chances of success and minimize the chances of abuse or significant litigation.

²68 *Fed. Reg.* 16,119-16,142 (2003).

Adequate Safeguards, Reasonable Transparency, Appropriate Accountability, and Governmentwide Reforms

There is growing agreement on the need to better link individual pay to performance. Establishing such linkages is essential if we expect to maximize the performance and assure the accountability of the federal government for the benefit of the American people. As a result, from a conceptual standpoint, we strongly support the need to expand broad banding approaches and pay for performance-based systems in the federal government. However, moving too quickly or prematurely at DOD or elsewhere can significantly raise the risk of doing it wrong. This could also serve to severely set back the legitimate need to move to a more performance- and results-based system for the federal government as a whole. Thus, while it is imperative that we take steps to better link employee pay to performance across the federal government, how it is done, when it is done, and the basis on which it is done can make all the difference in whether or not such efforts are successful. In our view, one key need is to modernize performance management systems in executive agencies so that they are capable of adequately supporting more performance-based pay and other personnel decisions. Unfortunately, based on GAO's past work, most existing federal performance appraisal systems, including a vast majority of DOD's systems, are not designed to support a meaningful performance-based pay system.

At the request of Representative Jo Ann Davis and Senator George Voinovich, we identified key practices leading public sector organizations both here in the United States and abroad have used in their performance management systems to link organizational goals to individual performance and create a "line of sight" between an individual's activities and organizational results.³ These practices can help agencies develop and implement performance management systems with the attributes necessary to effectively support pay for performance.

The bottom line, however, is that in order to implement any additional performance-based pay flexibility for broad based employee groups, agencies should have to demonstrate that they have modern, effective, credible, and, as appropriate, validated performance management systems in place with adequate safeguards, including reasonable transparency and appropriate accountability mechanisms, to ensure fairness and prevent politicalization and abuse. As a result, Congress should consider establishing statutory standards that an agency must have in place before it can implement broad banding or a more performance-based pay program.

At the request of Congressman Danny Davis, we developed an initial list of possible safeguards for Congress to consider to help ensure that any pay for performance systems in the government are fair, effective, and credible:

- Assure that the agency's performance management systems (1) link to the agency's strategic plan, related goals, and desired outcomes, and (2) result in meaningful

³U.S. General Accounting Office, *Results-Oriented Cultures: Creating a Clear Linkage between Individual Performance and Organizational Success*, GAO-03-488 (Washington, D.C.: Mar. 14, 2003).

distinctions in individual employee performance. This should include consideration of critical competencies and achievement of concrete results.

- Involve employees, their representatives, and other stakeholders in the design of the system, including having employees directly involved in validating any related competencies, as appropriate.
- Assure that certain predecisional internal safeguards exist to help achieve the consistency, equity, nondiscrimination, and nonpoliticization of the performance management process (e.g., independent reasonableness reviews by Human Capital Offices and/or Offices of Opportunity and Inclusiveness or their equivalent in connection with the establishment and implementation of a performance appraisal system, as well as reviews of performance rating decisions, pay determinations, and promotion actions before they are finalized to ensure that they are merit-based; internal grievance processes to address employee complaints; and pay panels whose membership is predominately made up of career officials who would consider the results of the performance appraisal process and other information in connection with final pay decisions).
- Assure reasonable transparency and appropriate accountability mechanisms in connection with the results of the performance management process (e.g., publish overall results of performance management and pay decisions while protecting individual confidentiality, and report periodically on internal assessments and employee survey results).

The above items should help serve as a starting point for Congress to consider in crafting possible statutory safeguards for executive agencies' performance management systems. OPM would then issue guidance implementing the legislatively defined safeguards. The effort to develop such safeguards could be part of a broad-based expanded pay for performance authority under which whole agencies and/or employee groups could adopt broad-banding and move to more pay for performance oriented systems if certain conditions are met. Specifically, an agency would have to demonstrate, and OPM would have to certify, that a modern, effective, credible, and, as appropriate, validated performance management system with adequate safeguards, including reasonable transparency and appropriate accountability mechanisms, is in place to support more performance-based pay and related personnel decisions, before the agency could implement a new system. OPM should be required to act on any individual certifications within prescribed time frames (e.g., 30-60 days).

This alternative approach would allow for a broader-based yet more conceptually consistent approach to linking federal employee pay and other personnel decisions to performance. It would help to assure that agencies have the reasonable flexibility they need to modernize their human capital policies and practices, while maximizing the chances of success and minimizing the potential for abuse. This alternative approach would also facilitate a phased-implementation approach throughout government.

Congress should also consider establishing a governmentwide fund whereby agencies, based on a sound business case, could apply for funds to modernize their performance

management systems and ensure those systems have adequate safeguards to prevent abuse. This approach would serve as a positive step to promote high-performing organizations throughout the federal government while avoiding human capital policy fragmentation within the executive branch.

Observations on Selected Provisions of the Proposed NSPS

With almost 700,000 civilian employees on its payroll, DOD is the second largest federal employer of civilians in the nation, after the Postal Service. Defense civilian personnel, among other things, develop policy, provide intelligence, manage finances, and acquire and maintain weapon systems. NSPS is intended to be a major component of DOD's efforts to more strategically manage its workforce and respond to current and emerging challenges. This morning I will highlight several of the key provisions of NSPS that in our view are most in need of close scrutiny as Congress considers the DOD proposal:

- The DOD proposal would allow the Secretary of Defense to jointly prescribe regulations with the Director of OPM to establish NSPS. However, unlike the legislation creating Department of Homeland Security (DHS), the Defense Transformation for the 21st Century Act would allow the Secretary of Defense to waive the requirement for joint issuance of regulations if, in his or her judgment, it is "essential to the national security" which is not defined in the act. Therefore, the act would, in substance, provide the Secretary of Defense with significant independent authority to develop a separate and largely autonomous human capital system for DOD.
- As I have noted, performance-based pay flexibility for broad based employee groups should be grounded in performance management systems that are capable of supporting pay and related decisions. DOD's personnel demonstration projects clearly provide helpful insights and valuable lessons learned in connection with broad banding and pay for performance efforts. At the same time these projects and related DOD efforts involve less than 10 percent of DOD's civilian workforce and expanding these approaches to the entire department will require significant effort and likely need to be implemented in phases over several years.
- Similarly, the NSPS would increase the current total allowable annual compensation limit for senior executives up to the Vice President's total annual compensation. The Homeland Security Act provided that OPM, with the concurrence of the Office of Management and Budget, certify that an agency have performance appraisal systems that, as designed and applied, make meaningful distinctions based on relative performance before an agency is allowed to increase the annual compensation limit for senior executives. NSPS does not include such a certification provision. On the other hand, the Senior Executive Service needs to take the lead in matters related to pay for performance.
- The NSPS would include provisions intended to ensure collaboration with employee representatives in the planning, development, and implementation of a human resources management system. As discussed at the Government Reform

Committee hearing on Tuesday, direct employee involvement in the development of the NSPS legislative proposal has thus far been limited. Moving forward, and aside from the specific statutory provisions on consultation, the active involvement of employees will be critical to the success of NSPS, or for any human capital reform for that matter.

- The legislation has a number of provisions designed to give DOD flexibility to help obtain key critical talent. These authorities give DOD considerable flexibility to obtain and compensate individuals and exempt them from several provisions of current law. While we have strongly endorsed providing agencies with additional tools and flexibilities to attract and retain needed talent, the broad exemption from some existing ethics and other personnel authorities without prescribed limits on their use raises some concern. Congress should consider building into the NSPS appropriate numerical or percentage limitations on the use of these provisions and basic safeguards to ensure such provisions are used appropriately.
- The NSPS proposal would provide DOD with a number of broad authorities related to rightsizing and organizational alignment. Authorities such as voluntary early retirements have proven to be effective tools in strategically managing the shape of the workforce. I have exercised the authority that Congress granted me to offer voluntary early retirements in GAO in both fiscal years 2002 and 2003 as one element of our strategy to shape the GAO workforce. In DOD's case, while it has used existing authorities to mitigate the adverse effects of force reductions in the past, the Department's approach to those reductions was not oriented toward strategically shaping the makeup of the workforce. Given these problems, there is reason to be concerned that DOD may struggle to effectively manage additional authorities that may be provided. Importantly, the NSPS provisions would create an uneven playing field among agencies in competing for experienced talent.
- The legislation would also allow DOD to revise Reduction-in-Force (RIF) rules to place greater emphasis on an employee's performance. I conceptually support revised RIF procedures that involve much greater consideration of an employee's performance. However, as noted above, agencies must have the proper performance management systems in place to effectively and fairly implement such authorities. Furthermore, DOD proposes to lower the degree of preference provided to veterans under current law.
- The proposed NSPS would allow the Secretary, after consultation with the Merit Systems Protection Board, to prescribe regulations providing fair treatment in any appeals brought by DOD employees relating to their employment. The proposal states that the appeals procedures shall ensure due process protections and expeditious handling, to the maximum extent possible. This provision is substantially the same as a similar provision in the Homeland Security Act of 2002 allowing DHS to prescribe regulations for employee appeals related to their employment. Given the transparency of the federal system dispute resolution and its attendant case law, the rights and obligations of the various parties involved are well developed. It is critical that any due process changes that DOD would

make under this authority, are not only fair and efficient but, importantly, minimize any perception of unfairness.

Concluding Observations

In summary, many of the basic principles underlying DOD's civilian human capital proposals have merit and deserve serious consideration. They are, however, unprecedented in their size, scope, and significance. As a result, they should be considered carefully—and not just from a DOD perspective. The DOD proposal has significant precedent-setting implications for the human capital area in government in general, and for OPM in particular.

The DOD civilian human capital proposal raises several critical questions both for DOD as well as governmentwide policies and approaches. Should DOD and/or other federal agencies be granted broad-based exemptions from existing law, and if so, on what basis? Does DOD have the institutional infrastructure in place to make effective use of the new authorities? Our work has shown that while progress is being made, additional efforts are needed by DOD to integrate its human capital planning process with the department's program goals and mission. The practices that have been shown to be critical to the effective use of flexibilities provide a validated roadmap for DOD and Congress to consider. We believe it would be more prudent and appropriate to approve the broad-banding and pay for performance issues on a governmentwide basis. Nevertheless, if additional authorities are granted to DOD, Congress should consider establishing additional safeguards to ensure the fair, merit-based, transparent, and accountable implementation of NSPS. This includes addressing the issues I have raised in this statement.

As I have suggested, Congress should consider providing governmentwide broad banding and pay for performance authorities that DOD and other federal agencies can use provided they can demonstrate that they have a performance management system in place that meets certain statutory standards, which can be certified to by a qualified and independent party, such as OPM. Congress should also consider establishing a governmentwide fund whereby agencies, based on a sound business case, could apply for funds to modernize their performance management systems and ensure that those systems have adequate safeguards to prevent abuse. This would serve as a positive step to promote high-performing organizations throughout the federal government while avoiding further fragmentation within the executive branch in central human capital policies and approaches.

We look forward to continuing to support Congress and work with DOD in addressing the vital transformation challenges it faces.

Chairman Hunter, Mr. Skelton and Members of the Committee, this concludes my prepared statement. I would be pleased to respond to any questions that you may have.

Contacts and Acknowledgments

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