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# Performance Based Pay: Is it a Functional Alternative in Government?

Jerry Templet  
*University of New Orleans*

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Performance Based Pay:  
Is it a Functional Alternative in Government?

A Thesis

Submitted to the Graduate Faculty of the  
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Master of  
Public Administration

by

Jerry C. Templet

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**Abstract:** The use of performance-based, or incentive based, compensation plans is ubiquitous in the private sector. Private business operates under the belief that the use of incentives leads to increased performance from employees and higher profits for the companies. This study is centered on the function of those performance-based pay plans within the government. Its purpose is to determine if the use of such pay plans is effective, both for the efficiency of government organizations and the motivation of employees. Through the analysis of government documents and organizational plans, and interviews of human resource managers and employees, this study analyzes performance-based pay and its effectiveness in the public sector.

## **Introduction**

Performance-based pay has been utilized in the private sector for many years. The pay scheme is based on an employee's performance, measured by some predetermined means, which then leads to compensation based on that measure. These schemes incorporate a determination of productivity that is communicated to the employee at the onset of each measurement period, yearly, quarterly, or monthly. Once the performance threshold is established, the employee is monitored, continuously or at certain preset intervals, and feedback is given on their progress. Employees who perform above the threshold level are awarded for their performance by incentive pay through either permanent salary increases or one time awards. In the event the employee is failing to perform at the threshold level, management works with the employee to understand the reasons for the shortcomings and ways to correct them. If the employee does not, or cannot, correct their deficiencies, they may be terminated, or in some instances re-assigned.

Performance-based pay is very functional within private industry where the measure of performance is usually based on the company's profitability, or the employee's ability and performance in making the company profitable. Pay systems that incorporate straight commissions on sales, profit sharing, and performance bonuses are all examples of private industry's belief that employees are motivated by incentives, and that given the proper incentives, including attainable goals, employees will perform better.

With the passage of the Civil Service Reform Act of 1978, the federal government began to study the subject of performance-based pay and was given the authority to utilize more modern ways to both classify the duties, and measure the performance, of government employees. As a result, the Office of Personnel Management, in conjunction with the General Accounting Office engaged in a number of experiments to measure the effectiveness of merit

based pay systems within the public sector. Currently, there are government organizations that utilize performance-based pay, and the movement to integrate performance-based pay within the entire public sector continues to gain acceptance and advocacy, as seen through its continuous implementation in that sector.

The concept that employees will perform to a higher level and work harder for incentives is intuitive, but employees within the public arena perceive incentives differently and have different motivations than those in the private sector. Public workers recognize that their jobs are tied to the advancement of the public good, and with that, many look for intrinsic motivation, or that feeling of accomplishment, in addition to monetary rewards.

In addition to differences in motivation, the problem of implementing a functional evaluation process, one that uses private sector measures to evaluate public sector outcomes, can present, in some instances, an overwhelming obstacle. The public sector operates in an environment that recognizes a diverse number of performance measures, which are arrived at, for the most part, subjectively. The problem is that while private sector measures are easily quantitative, based on, as stated earlier, profitability or categories that lead to profitability, the public sector encompasses many different responsibilities, which require performance measures that are complex and thus difficult to determine. This diversity is a challenge for performance based pay schemes that rely on objective determinants of performance. That is, the objective measures used in performance based pay schemes in the private sector are difficult to incorporate into the public sector at the operational level. By operational level, I refer to the point where the employee's performance is measured and that performance measurement is then converted to rewards.

While the movement to performance-based pay systems continues to gain momentum, and with a cursory understanding of the inherent problems in utilizing such systems, it is important to understand the operation of the current federal pay system and how it relates to the changes advocated by performance-based pay proponents. The federal government currently utilizes the General Schedule. This pay system is based on 15 advancing levels of compensation from GS1, low entry level, through GS15, upper management.

Employees enter government service in one of these levels based on the designation of their specific job title and their level of experience. The levels are referred to as GS levels, and although they begin at GS1, many jobs, at entry level, are classified as higher. For instance, many clerical positions enter at the GS2 level and progress through GS8. Within the General Schedule, employee advancement through these levels is based on the position's GS level range, and on yearly evaluations based on the employee's ability to acquire new skills and perform more intricate duties. Additionally, the General Schedule contains provisions that recognize outstanding performance, and has highly structured employee discipline procedures, including an employee grievance process in the event of an adverse employment action. Although the General Schedule contains some of the same concepts of performance-based pay such as increases based on performance and performance bonuses, it is postulated by merit pay advocates that performance-based pay schemes more specifically tie an employee's performance to compensation increases and rewards, unlike the General Schedule which allows for more ambiguity in what constitutes proper performance, and provides even more latitude to management on what basis bonuses may be awarded.

## **Problem Statement**

The Department of Homeland Security was formed in response to the September 11<sup>th</sup> attacks and includes 22 agencies representing a workforce of approximately 170,000 employees. The Department is currently implementing a new human resource system, designated Max HR. The system is built within the construct of pay banding and performance based incentive pay, and is currently beginning to supplant the Department's General Schedule System. While the Department's reasons for the change to a performance based pay system, such as improved employee efficiency and a more effective organization seem compelling, there are inherent problems with Max HR. It is my contention that the full implementation of the pay system, as it is currently conceived, may result in a dysfunctional system that will be detrimental to the organization and the employees. This assessment is not without historical foundation, for in many experiments involving merit pay schemes, involving the public and private sectors, the concept of performance-based pay has not proven to be as sound in operation as in theory.

The information presented in the review of the literature will give insights into the functionality of performance-based pay systems. That information will be used to determine if performance-based pay, as utilized in the private sector, is a functional alternative to the current grade/step system now utilized in the federal government. This determination of functionality will be based on concepts of system equity, ability to fairly evaluate employee performance, system viability, ability to remain financially solvent, the management function of the systems, and the ability of management to effectively administer the system. These questions will be addressed within the context of performance-based pay in general, with specific focus on the Department of Homeland Security's Max HR to determine its ultimate success upon full implementation.



## **Literature Review**

In examining the research concerning performance based pay, information from a diverse array of sources was used. Academic studies, governmental studies, governmental advisory papers, and operational plans provided by governmental agencies that currently utilize performance based pay schemes were all examined to compile a comprehensive representation of the current issues involved in the performance based pay discussion. This review is divided into seven general concepts. The concepts cover the main ideas that influence performance-based pay systems, and are further broken down into subcategories that represent the important issues presented throughout the literature.

The use of performance-based pay is espoused to increase organizational effectiveness by offering incentives to employees. The reasoning being that as employees work to earn the incentives, they will be more productive, and in turn that will benefit the organization. In considering the need for transition to a performance-based pay system, it is important to understand the reasons for the proposed change, and what the organization expects to gain. The literature views those reasons from four different perspectives.

### **The Theoretical Perspective**

The theoretical perspective proposes that the need for performance-based pay is precipitated by the change in government function. That is, that society is constantly evolving, and government must make changes to adjust to that change.

The theoretical perspective is furthered by David Osborne and Ted Gaebler in their book Reinventing Government, How the Entrepreneurial Spirit Is Transforming the Public Sector, in which they propose that the huge government of the past, containing highly structured and complex bureaucracies, which was needed during the Great Depression and both world wars, has

outlasted its usefulness (Pg 13). Instead, the authors postulate that a new government, focused on flexibility and imagination, is needed to address society's current issues (Pg 14-16).

The authors also espouse the idea that the new government needs to be led by incentives and possess the ability to use persuasion and a feeling of personal ownership to complete its mission (Pg 31). Out of these concepts, came the introduction of merit-based compensation within the government, and with it, the effect of a dramatic change in the way that government operates. The concepts espoused by the authors are important in that they illustrate a historical evolution of theoretical approaches to government and the idea that change is needed to address the new government culture. These ideas are profound in they present a radical departure from the current approach to government operation. While the ideas do hint of the ubiquitous "government should be run like a business", even more, they clarify the need for change to address change, and not a movement to a pure business model.

### **The Competitive Perspective**

The competitive perspective encompasses the idea that the need for change is based on the need of business to stay competitive in the market place. The drive to stay competitive leads to the need for incentives to increase production.

In their study "Promise and Peril in Implementing Pay for Performance: A Report on Thirteen Natural Experiments," Michael Beer and Mark Cannon introduce the competitive perspective. The authors state that the driving force behind the advent of performance incentives is the fact that companies are continually searching for ways to enhance their competitiveness in a given market (Pg 3). In fact, the authors point to studies that show a majority of private companies have implemented some type of performance-based compensation philosophy in order to enhance the productivity of their employees (Pg 4). Beer and Cannon further support

the intuitive belief that employees will work harder for incentives, and with that, the company will realize the benefit of higher efficiency. They believe that the need for performance-based pay lies in the company's or organization's need for goal attainment, whether monetary or some other measure.

Additionally, in an online article from the Colorado State University Cooperative Extension, Agriculture and Business Management, entitled "Labor Management: Issues and Strategies for Incentive Pay Programs," the competitive perspective is examined with respect to the environment of unskilled, low paid, migrant workers. The authors state the primary reason a business would introduce performance-based pay is productivity. They also state that the worker's ability to produce, above and beyond a predetermined set standard, affects the company's bottom line. This is the paramount consideration in introducing performance-based pay (Pg 1).

### **Economic Perspective**

Workers react to incentives. When incentives are attached to increased production, employees identify that as a way to enhance their compensation and work to attain set goals. The economic perspective introduces the concept of change based on the need of employees for economic gain.

Iris Bohnet and Susan Eaton in the book, "For the People," Chapter 13, Does Performance Pay Perform? Conditions for Success in the Public Sector, introduce the economic perspective. They state that the federal government, over the past decade, has been debating the issue of introducing performance-based pay into the government (Pg 1). The authors describe the need for the system from a purely economic perspective, by stating that if employee pay is tied to output in a proportional way, workers will work harder, and the greater output produced,

the more compensation earned (Pg 2). They continue by advising that the concept of merit pay is derived from scientific management, where there is a most efficient way to do each job, and the employee is motivated, by external forces, to do the job more efficiently (Pg 2). The authors use scientific reasoning to indicate the motivation behind the implementation of performance-based pay and the need for incentives. They present the argument that employees perform better when incentives are offered, and that companies use these incentive to achieve their ultimate goals (Pg 2).

The authors of the Colorado study, in the same manner, express the view that the economic perspective is a viable reason for change. They explain that performance-based incentives provide potential benefits including lowering employee turnover and improving employee morale (Pg 1). Additionally, they state that in agriculture, hiring seasonal workers is a necessity, and with that, the employee pool comes with diverse worker capabilities. The introduction of incentives, as postulated by the authors, can mitigate the diversity issue and enhance the possibility of hiring the best workers (Pg 1). The reasoning is that more motivated employees, those who understand that the harder you work the more money there is to be made, will naturally gravitate to those companies that utilize pay based on performance and will increase their income.

### **The Government Perspective**

Within the government there are forces that drive the movement to performance-based pay systems. The need for more responsive government and government accountability, are among those. The government perspective is an amalgam of how government views the need for the change to performance-based pay.

The government has studied the implementation of performance-based pay for some time, and as a practical matter, has participated in performance-based pay schemes. Therefore, government has its own perspective on the implementation of performance-based pay. That perspective is represented first in a report from the United States General Accounting Office, Human Capital: Implementing Pay for Performance at Selected Personnel Demonstration Projects, in which the GAO strongly supports the implementation of performance management systems, finding that its demonstration projects implemented operationally effective alternative pay systems using a variety of performance-based designs (Pg 4). The organization has engaged in the study of such pay schemes, on a limited basis, but encompassing a diverse array of projects. GAO has found that the use of incentives, if tailored to the organizational culture, will result in a positive outcome for the organization, and will lead to better efficiency (Pg 4).

Another illustration of the government perspective can be found in a summary report on a forum sponsored by the National Academy of Public Administration and the National Commission on Public Service (NCPS), “Conversations on Public Service; Performance-Based Pay in the Federal Government: How do we get there,” the forum participants advocated the continued implementation of performance-based pay systems in the public sector, stating that while the differences in organizational missions, employee pay, and skill levels throughout the government are hurdles, the federal government has the ability to implement a functional performance-based pay system if the proper ground work is completed ( Pg 4-5). This statement reflects the belief of the Academy that the use of performance-based pay is integral to the effective operation of the government, and that it is possible to overcome current problems and implement a workable system.

The forum participants then discussed several examples of government initiatives, which they believe solidify performance-based pay in the future of the federal workforce. They explain that individual agencies such as the Internal Revenue Service, Federal Aviation Administration, Federal Deposit Insurance Corporation, and the General Accounting Office have instituted various forms of performance pay schemes. Furthermore, the Department of Homeland Security is in the process of implementing a performance-based pay system (Pg 6). Additionally, they advise that Congress has authorized the Department of Defense to implement a performance pay system for 300,000 of its civilian employees, and the current Bush Administration has also proposed the creation of a 500 million dollar, Human Capital Performance Fund, to give federal agencies the ability to compensate their top performers (Pg 6). The forum participants believe that with these initiatives, more than half the federal workforce, excluding the Postal Service, will be working in a performance-based pay system within the next two years (Pg 6-7).

In addressing additional aspects of the government perspective, a report by the Human Resources Management Panel (HRMP) of the National Academy of Public Administration, "Recommending Performance-Based Federal Pay," states that the General Schedule is outdated, and that for the government to continue to both hire and retain high performers the implementation of a performance-based pay system is imperative (Pg 4-5). The basis of the panel's belief is that the government, through the General Schedule's rigid and highly structured policies, is at a disadvantage when attempting to hire and retain valuable human resources. The panel further suggests that a system, which allows government organizations some latitude in hiring salaries and positions will be more effective and function better.

The ultimate success of a performance-based pay system is contingent on a large number of variables, from proper implementation procedures, to effective management, and

organizational attitude toward change. The research has examined the most significant variables, and presents them as three general tenets.

### **Organizational Impact**

While it is important for any new system to fit the organizational structure, that is especially true for performance-based pay systems. The increased apprehension that accompanies new compensation schemes must be mitigated by insuring proper alignment with organizational goals and strategies before implementation occurs. The tenet of organizational impact encompasses the belief that any change must fit within the current organizational construct.

In a paper by the International Labour Office, Geneva, entitled “Performance–Related and Skill Based Pay: An Introduction,” Sriyan de Silva explains the importance of this tenet when he states that before the shift of an organization to a performance based pay scheme, a company pay expert, or management in general, must analyze the existing pay structure and ensure that changes in compensation would not negatively impact company strategies, its overall organizational objectives, or its human resource management (Pg 5). Here de Silva forwards the idea that the organization must be prepared for change, and that any change must fit within the organizational construct.

Additionally, in an internet article from Advantage Home, February 2005, Volume 1, Issue 10, “Measurable Goals, Clear Communication Key to Performance-Based Incentive Programs,” the RSM McGladrey Company continues to examine the principles of organizational impact. The article cites a 2004 study by WorldatWork, a not for profit trade association, concerning the overall success of performance-based pay systems, which showed that of the companies utilizing performance-based pay, 83% described their programs as “somewhat

successful (Pg 1).” The article then presented a concept to lessen the possibility of implementing a dysfunctional system. The use of Strategic Consistency, or insuring a new incentive plan fits within the overall strategy of the company (Pg 1-2), was presented as a significant way to ensure a functional merit pay system. In other words, understanding the company’s short and long-term goals, and the future effects of the performance-based scheme on those goals, is a paramount consideration.

In the National Commission on Public Service study clear communication and a linkage between organizational goals and individual performance measures were deemed important (Pg 8). The study panel recommended that the system be implemented with an understanding of the mission and culture of the organization. The systems should be tailored to fit the unique organizational structure.

To that end, the panel participants suggested two processes that could be used for effective implementation. The first is incremental implementation of the new system, agency by agency, over time. The second more radical process would involve changing the system across the entire federal government all at once, including the total abolishment of the current civil service system (Pg 16). In relation to the implementation choices, the forum participants noted that while some organizations are ready for change, others, due to organizational culture, need more time to adjust. The NCPS forum recommended using a combination of both processes in order to facilitate a smooth transition. The concept of incrementalism versus radical change gives the tenet of organizational impact a new prospective. The ideas presented offer management different, but equally effective ways, if the implementation process is fitting for the organization, to effect change and ensure the new system is functional.



In the Colorado State University article, the authors examine organizational impact as it relates to the agricultural industry. They state that a new system must be based on the company's unique operating, marketing and financial objectives, including the concepts of expected market share, growth, and quality (Pg 2). Here again the idea that the system must fit within an organization's parameters is examined, and it becomes clear that any change must be preceded by an examination of the ultimate organizational impact.

### **Communication**

The inability, or worst, the unwillingness to communicate in an organization can have disastrous effects. For a system to remain effective, the flow of ideas must continue. The tenet of communication is based on the ideas that management and employees must engage in ongoing dialogue to ensure a new system is successful.

In relation to communication, de Silva points out that the objectives of a new system should be clearly identified, and that employees should have an input in determining whether those proposed objectives could be achieved via the new system (Pg 5). In relation to the operation of the system, de Silva communicates that all changes in the workplace that accompany the new system must be identified and that the new system must be introduced to the stakeholders (Pg 6). These concepts for the effective implementation of a new pay system are important. They set the ground rules for how change will occur, and in doing so make changes easier for those involved. de Silva also makes the point that stakeholder involvement in the process is a major factor. Change is naturally difficult, but the ability to have input and influence the changes lessens its untoward effects (Pg 6). In a paper by Yves Emery, "In Rewarding Civil Service Performance through Team Bonuses: Findings, Analysis, and Recommendations," Emery includes the significance of employee buy in, and he goes further by espousing a system

that is openly communicated, that ties performance to rewards in a clear manner, and that also is complex enough to cover the gamut of responsibilities (Pg 161). The authors of the Colorado study, in relation to communication, state that gaining the input of long-term workers, even those who are seasonal but return year after year, can give an indication on what factors are important to them, and in turn will add validity to the system (Pg 2). Finally, the authors propose that once the standards are set, it is important to adequately monitor progress, through open communication, to ensure the system is working as designed (Pg 3-4). Even in the environment of low paid, migrant workers, the fundamentals remain. The concepts of stakeholder buy in, including providing input from the workers, fit within the communication tenet. In an Internet article from CIPD, "Team Rewards, Pay and Reward," the article provides some of the same communication fundamentals. The authors propose that for a performance-based pay system to function, every member of the group must understand and accept the goals set forth in the system (Pg 3). That is, as discussed earlier, the stakeholders must "buy in" to the ultimate motivation and process contained in a new pay system. The NSPS panel also touts the tenet of communication by stating that any new system must be properly communicated to the stakeholders (Pg 9). The panel then presents some new ideas. They first propose that the involvement of top-level management and individual employees in the system is paramount to a systems acceptance (Pg 9). The point being, that only through the acceptance of the upper management, and their drive of the system, can individual employees have the ability to provide input. The HRMP panel further states that in establishing a performance management system, that communication from the employees and management is central to the development of a functional system (Pg xi). They state that the core of performance-based compensation is the ability of managers and employees to work together to define performance standards and ensure

the fairness of the process (xiii). Here again is an illustration that communication, the ability of management and the employees to work together, is one of the core concepts of a functional system.

### **Performance Recognition**

For a performance-based pay system to be effective, it must accomplish what it proposes, and recognize performance. The tenet of performance recognition entails the concepts that the new system will adequately identify high performing individuals, but will also address the lack of performance in others.

In the Internet article from Advantage Home, two concepts are introduced that the authors believe are central to performance recognition; Structural Integrity, that is, insuring that the performance goals within the system will be able to give a true account of the individual employee's performance, and Cultural Relevance, insuring the incentive program within the system fits into the companies overall rewards structure (Pg 1-2). Both involve the ability of the system to measure and reward employees as a result of their performance. They involve the system's ability to function as prescribed.

Emery also explains the performance recognition tenet. He states that for the performance incentives to be attractive to workers they must be positively viewed and of sufficient quantity, in excess of 10% more than currently offered (Pg 160). Emery also states that there must be a clear link between performance achieved and reward allocation, this point is especially salient in the public arena (Pg 160). Emery also postulates that the visibility of rewards, a subject that is vehemently controlled in private firms, must be included in the public sector in order to establish and continue the legitimacy of the system (Pg 161). Additionally, the clear link between individual, team, and organizational objectives must be established in order to

ensure congruency within the process, and the performance measure must be complex, yet transparent, in order to allow for understanding but not manipulation (Pg 161). Here Emery advances the concepts that performance recognition is more than a rating on a form, but that there is a quantifiable percentage that must be met. Additionally, Emery explains that the performance recognition must be visible, that is, all employees should know what rewards are given. Emery also states that the clear link between performance and rewards are important, and that in the end a congruency of goals, in addition to a functional performance measure, are central to a functional system. In the CIPD article, the authors also state that rewards must be clearly linked to effort and achievement, that performance measures must be fair and consistent, and that the pay scheme must be carefully designed to incorporate monitoring of the program, attainable goals, and clarity (Pg 3). Here again, the concepts that effect performance recognition are clear.

The NSPS panel also discussed performance recognition, but from a different perspective. The panel stated that the availability of development and training for poor performers, and the necessity of holding managers accountable for performance-based management, must be included in any system (Pg 14-15). With regard to poor performers, the panel states that a merit pay system, while it needs to reward the best and brightest, must also provide an instrument to assist those employees who are failing to reach their potential. The panel also explains that, as with most performance pay systems, the first line supervisors are the catalysts. In order for a system to function properly, the managers at the operational level, must be properly trained and held accountable. In this change of perspective, negative performance actions are examined. This is a particularly salient point in the public sector. In the General Schedule there are instruments to deal with poor performers, but the management of the system

has rendered those instruments useless. It the responsibility of a performance-based pay system to promoted those who perform, but it is equally important for the system to address the poor performers.

The examination of the literature has resulted in the recognition that organizational change is a key to the implementation of a performance-based system. The concept of organizational change should not be confused with organizational impact, an issue that has already been addressed. Organizational change refers those issues within an organization that must be changed, and ways to implement those changes, before implementation can occur. The literature has illuminated two aspects of organizational change.

### **Communication of Change**

When change is imminent, the need for communication becomes that much more important. All stakeholders must understand the needs for change, and have the opportunity to provide input. Communication of change addresses the exchange of ideas between management and employees as that change occurs.

The HRMP panel discusses the importance of communication and organizational change. They explain the proper steps to implement a new system, explaining that the organization must first introduce the idea of change, explain the significance and need for the change, and ultimately present an acceptable system to the supervisors and employees (Pg 30-31). This is difficult given the organizational culture in most government agencies. For many agencies, the concepts included in performance-based pay schemes seem incongruent with their organizational missions. For example, in the case of the Department of Homeland Security, how can investigating terrorist organizations, a convoluted concept to begin with, be tied to a performance measure? This separation between mission outcome and individual pay is a major concern for

the public workforce and the introduction of performance-based pay. In addition, the dismay that accompanies all change, even more so when that change addresses drastic modifications involving compensation, can easily overwhelm an organization and lead to adverse reactions.

To mitigate the effects of this adverse action, or culture shock, the panel poses that in order to truly facilitate organizational acceptance, a “psychological contract” must be established between supervisors and staff (Pg 12). This contract, which is unwritten, establishes the acceptable behaviors for members of each group as to the implementation and management of a new pay system. The point here is the importance of the employees’ belief that they will be treated fairly and that all involved will conduct themselves appropriately. Additionally, the GAO states that organizational change should include the use of a new management system that perpetuates this new culture, including the concept of top-down management to support effective communication throughout the organization (Pg 3). In these ideas on organizational change, there are some of the same ideas presented as tenets for success, yet in the present context the ideas precipitate an understanding of the changes needed in the organizational culture of most governmental agencies.

### **Employee and Management Based Change**

For change to occur, all stakeholders, management, employees, and the organization as a whole, must accept the need for change, and engage in change themselves. Employee and management based change incorporates all the changes that must be engaged in by the members of an organization in preparation for the implementation of a new system.

de Silva contends that the concept of seniority, as a measure of compensation, is becoming less important, and that an individual’s presence in the workplace year after year is not an accurate measure of their performance (Pg 11). Instead, the concept of seniority is being

replaced with more knowledge and performance based measures (Pg 12). Incumbent in that divergent shift is the understanding that such changes in performance measures must be accompanied by the behavioral changes in employees and a shift in the way employees perceive their work. The pervasive culture of seniority, the belief in many organizations that having “time on the job” entitles an individual to certain treatment, and that the person’s performance is based on that seniority, must be changed. Cultural shifts can occur, but only through proper training for employees and management. The GAO forum, in discussing employee change, also states that in order to cultivate this cultural evolution, in preparation for the implementation of performance-based pay, the mentality of government employees towards their work, and as a consequence, a change in the overall culture of government employment is essential (Pg 1). Here we see the idea that the change to a new system must be preceded by the change in mentality of government workers, and that change must involve a meaningful understanding on behalf of the employees that for the system to be implemented properly, they must accept organizational change. The GAO study stated that any functional performance-based pay system had to be created within a results oriented management scheme, a scheme which takes into account the outcomes or outputs of its employees (Pg 39). This type of management scheme stands in stark contrast to the current entitlement based management culture so ingrained in the federal government. As presented here, an understanding of the issue involving cultural change, from both employees and management, gives insight into the importance of those changes in preparation for a new system.

The manner in which a performance-based pay schemes evaluate employee performance is of great consequence. The evaluation system must be easily understandable and clearly communicated, and must include an element of transparency. In the examination of the

literature, the concept of evaluation was discussed as a major element in a successful performance-based pay system. The literature presents three factors of evaluation.

### **Evaluation Instruments**

Evaluation instruments refer to the mix of measures used in the actual evaluation of employees within a performance-based pay system. It involves the concept of using subjective measures for evaluation.

de Silva proposes that the use of highly structured evaluation tools to determine pay, does not allow for needed flexibility, in that, it is based on a standardized measures (Pg 15). That is, that an evaluation process should allow the evaluator to use a means, other than standardized evaluation, to measure employee performance. This is necessary due to the diversity of employees who perform different duties. Here de Silva forwards the idea that the use of an evaluation process that does not limit management to a matrix containing standardized, objective, judgments is more functional in determining the true contributions of the individual employee. de Silva posits that the use of an evaluation process that allows these types of subjective measures, although opened to more interpretation, gives the organization the needed flexibility to properly evaluate performance.

### **Evaluation System**

Evaluation systems are complex. This stems from the fact that they must encompass many different work classifications, insuring fairness, while making adjustments as the system evolves. Evaluation systems include the basis for the systems, the effects that modifications can have, and the trust and legitimacy issues involved in an effective system.

In a paper by Sandra J. Reinke, Augusta State University, "Does the Form Really Matter? Leadership, Trust, and Acceptance of the Performance Appraisal Process," Reinke



begins the discussion on evaluation systems and the basis on which they operate. She states that the utilization of performance systems is based on three critical assumptions. First, employees differ in their contributions to the organization, secondly, the cause of this difference is due to their individual performance, and finally the supervisors are actually able and willing to distinguish an employee's performance based on a known number of factors (Pg 23). Here Reinke postulates the idea that evaluation systems are constructed around three central ideas, and states that based on those ideas being constant, the system will operate effectively. While these concepts are clear as they relate to the operation of an evaluation system, Reinke postulates that a fourth concept, legitimacy, plays a much more significant role in the acceptance of an evaluation system. For while the aforementioned concepts play a functional role, legitimacy, or the acceptance of the appraisal system by the supervisors and employees, is essential to the comprehensive implementation of the merit based pay plan (Pg 23-24).

Reinke then examines two additional concepts that impact an evaluation system, trust and relationship between employees and supervisors. In relation to trust, Reinke states that the employee/supervisor relationship is based on trust, and although she examines different definitions of trust, in the end, she defines trust as a belief that one can be counted on to act in an acceptable manner, with stability and order, and with open communication (Pg 26-27). Reinke also conducted a study involving the concept of trust and employee reaction to the implementation of a new evaluation system. Reinke's population was given a survey to determine the attitudes of the employees toward their current evaluation system, in anticipation of a change to a new system. The findings of the survey showed that the employees and managers were unhappy with the current system and that they had their own ideas about the implementation of a new system (Pg 27). This information, as well as other data from the

survey, was then run through statistical analysis. The result of that analysis showed that the concepts of trust and leadership were paramount determinants in the acceptance of a performance appraisal system. In her examination of the trust concept and in the outcome of her study, Rainke shows that the tenets of the trust in relationships, in combination with the legitimacy of the system, results in a functional evaluation system.

In their examination of evaluation systems, Beer and Cannon, discuss the inherent problem of modifications to evaluation system. They state that these modifications are precipitated by technology, learning curves, and changing circumstances, and can lead to the perception of inequity and reduce the validity of the link between pay and performance (Pg 5). Here the authors point to the problem of changing certain aspects of the evaluation system as a result of system evolution. While change is inevitable as the system evolves, the more important issue, and the issue that if addressed can mitigate the negative effects of change, is that the rationale and need for change must be understood by management, and must be clearly explained to the employees.

de Silva then comments on evaluation systems, yet he takes a different approach by examining inappropriate appraisal systems. He states that these systems are those in which the objectives of the appraisal system do not match the objectives of the performance pay system (Pg 16-17). That is, the appraisal system's construction, including the measures, does not meet the needs of the overall performance pay system. In this situation, de Silva believes that the incongruence leads the employees to believe that the system has not been properly structured, and thus can lead to distrust in the evaluation process. This idea is important to the understanding of the evaluation process. With the introduction of a new pay system,

stakeholders will, by nature, be hesitant. It is important that the evaluation system, which drives the merit pay system, be free from unclear and incongruent principles.

### **Evaluation Measures**

The measures used in the evaluation process can affect the legitimacy of the outcome. Therefore, it is paramount that the measures fit the work that is being evaluated. Evaluation measures include, among other issues, a discussion of evaluating complex tasks, the connection between measures and job classifications, and ways to ensure the measurements of employee outputs are evaluated correctly.

Bohnet and Eaton begin the discussion on evaluation measures by exploring the problems in measuring more complicated tasks, as opposed to simple jobs. They state that as employees are placed in a position to complete complex projects, and are responsible for multiple tasks, a detrimental effect on overall performance occurs from incentive based schemes (Pg 4). They attribute the effect to the fact that those employees who are responsible for not only piece work, but more complex assignments, for example, developing new ideas or concepts, will ultimately concentrate their time on the completion of the more simplistic work leaving no time for the complex assignments. This point is evidenced by the concept of higherarchy of tasks. A worker sets the priority of tasks and attempts to complete those tasks in the proper order. Intuitively, a conscientious worker will complete the easiest work first. However, tasks expand to fill time and the worker, no matter their motives, has difficulty completing the later, complex tasks. Here the authors explain the importance of work type as it applies to evaluation measures, and make the point that measures must be congruent with level of the work being evaluated.

The authors then discuss the subject of measuring employee outputs. They state that there are three key characteristics in determining the applicability of output measurement. The

output is based on a single task; here the idea of a single task is important, for when employees are evaluated for the completion of multiple responsibilities, and some of the duties are more easily observable and measurable, the workers will concentrate on those tasks (Pg 5). Secondly, the task must be clearly measurable (Pg 5); this is important due to the fact that in the absence of clear measures, the authors contend a moral hazard arises (Pg 7). In that, the employer, unable to evaluate based on a true measure, must base the evaluation of some random outcome that may, or may not, be linked to employee effort. Lastly, the measured task must be linked to a single individual (Pg 5). This is important in that the evaluation measure must have the ability to differentiate the input of a diverse group of employees, with diverse abilities. The authors then examine the notion that performance-based pay systems are most successful when implemented in non-professional environments, where output can be easily measured (Pg 7). They give the examples of number of phone calls answered in a given period, or number of heads of lettuce picked, duties that are easily quantifiable. They point out, however, that while best suited for non-professional occupations, performance-based pay schemes are used to a great extent in the highest level of employees, corporate CEO's (Pg 7). The authors state that although the efforts of CEO's are difficult to measure and thus hard to incorporate into performance pay, it has been the common practice to reward them with stock options (Pg 7). Consequently, the CEO's profit if stock prices increase and lose if they decrease. This is to ensure that they make decisions in the best interest of the company. However, in the end, a CEO's pay is usually based on luck. If the company thrives because of high oil prices, the CEO profits from the companies performance although he or she had no effect of the price of oil. The authors then discuss measurement as it relates to the public sector specifically. They state that output in the public sector is even more difficult to measure, explaining that outputs are more vaguely defined than in the private sector

(Pg 8). They use the example of the U.S. Department of State, whose goal is to “Promote the long range security and well-being of the United States,” the author’s state, in relation to this goal, that any measurement would be ineffective at arriving at a performance goal (Pg 8).

In relation to evaluation measures, Beer and Cannon contend that there are several distinct barriers inherent to the proper function of a performance-based system and in their measurement components (Pg 4). They state that the difficulty in evaluating performance when the measurement increments are small or fine distinctions are being made is a problem when measuring complex tasks (Pg 4-5). They continue by advising that this can be mitigated somewhat by the use of an unambiguous measurement instrument, but also state that whenever complex tasks are being evaluated, the problem will persist. Secondly, they espouse the idea that performance can, and often is, affected by factors that are not within the individual’s or group’s control (Pg 4). This can be seen in environmental changes in certain businesses or interdependence on other parts of the organization. Whatever the cause, it is difficult to hold persons accountable for issues over which they have no control, and this poses a problem for an evaluation measure. Additionally, managers, as a function of their duties, need to make decisions based on their best judgment. This is also problematic, according to the authors, in that many managers do not feel comfortable in having to differentiate between their subordinates (Pg 4). The human factor in any relationship cannot be ignored, and most managers do not want to create a hostile work environment. In this, managers will usually find a way to make the system work to the benefit of the majority of workers.

Finally, de Silva initiates his discussion on evaluation measures by introducing the concepts of dysfunctional measurement criteria. This type of measurement criterion is not functional due to the fact that it is difficult for either management, employees, or both, to

understand, communicate, or accept (Pg 12-13), and in the end is of no use. He states that the inclusion of such a criterion has a negative effect on the legitimacy of the entire system, and causes questioning of the evaluation measure.

In examining the literature, the concept of rewards, both monetary and intrinsic, was explored by many of the authors. This idea of rewards, including employee motivations, can be discussed from different perspectives, and is viewed differently by employees and employers. To the end, the literature provided three basic means to examine the concepts of rewards.

### **Differential Rewards**

Differential rewards are significant in that the concept of rewards is very convoluted. Within the rewards structure, there are delineations for intrinsic and extrinsic, public sector and private sector, and employee/employer considerations.

de Silva introduces the idea of differential reward systems and their effects on both organizations and employees. He states that although it seems incongruent, an increase in employee rewards does not necessarily lead to higher operating cost for the organization (Pg 5). de Silva points out, that the use of intrinsic rewards, those rewards based on fringe benefits; the ability of the employees to reorganize work processes, attend training, be involved in decision-making and goal setting, and having the opportunity for career development, are all recognized as motivational factors for employees to perform at higher levels with little or no additional cost to the organization (Pg 15-16).

Emery also examines the differential motivations for employee performance and states that intrinsic rewards, those feelings of accomplishment one gets from completing or engaging in a task, are much more important and longer lasting than extrinsic rewards, monetary or otherwise (Pg 159). de Silva postulates that the use of monetary incentives alone may only have an effect

on employee performance for a short period of time, but a system that incorporates both intrinsic and monetary components is more likely to affect the performance of employees, and the organization, over the long run (Pg 13). As an example, de Silva points to a study by Gerald E. Ledford, Edward Lawson, and Susan Mohrman, which showed that of a sample drawn from fortune 500 companies, the most widely used rewards for employee performance, over 90%, was non-monetary rewards (qtd in Creating High Performance).

Emery also discusses the issue of differential motivation between private and public workers by stating that public workers are not motivated by the monetary rewards as their corporate counterparts, but that public workers are motivated more by the possibility of making decisions, having a stable future, and putting their knowledge to work (Pg 160-161). Emery concludes by stating that for incentive systems to be effective all levels must be involved; individual, teams, if applicable, agency, and organizational (Pg 163-164). He states that for the successful implementation of a system, there must be diversification in the rewards that the system offers (Pg 164). That is, the system must offer extrinsic financial incentives, those contingent on performance or acquired skills, and intrinsic non financial incentives, those that offer a feeling of accomplishment so important to workers in the public sector.

The HRMP also found that differential rewards were a factor in the dichotomy in pay philosophy that exists between the public and private sector, discussing the fact that federal employees are given regular and significant pay raises at the start of their careers, before most have the knowledge and ability to positively affect their organizations, while the private sector awards significant pay increases as an employee progresses in their career and acquires the knowledge and skills that benefit the company (Pg 9-10). The panel believes that this dichotomy

in management theory indicates that the public sector places less emphasis on compensation based on actual skill and knowledge, and is more concerned with rewards for longevity.

### **Meaningful Rewards**

Meaningful rewards are the basis for any performance-based pay system. Before the system can be implemented to encourage employees to produce at higher levels, it must offer the proper motivation. The inclusion of meaningful rewards is central to that function.

In the NCPS report, the forum discussed the use of meaningful rewards. The members focused on monetary rewards and agreed that managers must have sufficient resources allocated to pay employees for their performance at significant levels. Members stated that if an employee is going to be evaluated by predetermined objectives, within a recognized and standardized system, the pay they receive as a result should be meaningful (Pg 14). Fernie and Metcalf found, that in relation to performance-based pay, the larger proportion of an employee's salary that is comprised of incentives, the higher their performance will be (Pg 4). That is, the higher the employee's pay is based on incentives, the more motivation the employee has to perform. The NCPS then espoused the idea that base salary is important factor in meaningful rewards. They stated that while the use of one time awards, awards given on a single occasion and in lieu of base salary increases, should be incorporated into a performance-based pay system, employees are concerned, and rightly so, as to how their continued performance effects base salaries (Pg 14). In this, the panel believes it is important that a functional rewards system have a mixture of one time performance rewards, based on an employee's isolated performance outcomes and overall performance, in combination with base salary increases.



## **Reward Motivation**

Motivation is important to any discussion on rewards. It is central to the belief that individuals will work harder, perform better, if a proper motivating factor is introduced. Motivation is also the key to performance pay. For a system to function, to actually motivate employees to achieve increased productivity, there must be that motivational factor.

Bohnet and Eaton agree that employees are motivated by rewards. They state that incentives, other than money, have a more motivating effect in many cases (Pg 10). As they explore the subject further, the authors refer to Douglas McGregor's ideas and concepts on worker motivation. McGregor's "Theory X", states that employees are adverse to effort and would prefer not to work at all if they could get away with it. This leads to the need for incentives to motivate employees to attain the goals for the good of the company. Theory X postulates an intrinsic aversion to work, and states that workers need incentives, motivations, to accomplish any task. McGregor also postulates that "Theory Y," which assumes that most people like to work, gain a psychic and financial reward from working, and want to do a good job, is a more beneficial way of conceptualizing the worker psyche, and is a better base to implement incentive pay. Although the authors explore both divergent theories, the importance lies in the fact that they believe employee performance is affected by the factors of motivation and incentives (Pg 33-57).

Beer and Cannon continue the discussion on motivation as it relates to the debate over the nature of human beings and their motivations, including the various arguments for and against the use of incentives. In relation to incentives, they believe that individual workers respond constructively to financial incentives, and thus the worker's behavior, their performance, can be controlled by extrinsic incentives (Pg 3). The authors then address traditional compensation

plans, those systems that offer compensation of monthly or weekly wages with no built in incentives. The authors argue that the systems are detrimental to their organizations in that they inhibit attempts to establish a more competitive, adaptive, and collaborative work environment (Pg 3). It is important to separate the concepts of incentive driven, performance pay, from salaried pay systems, and understanding that while salaried compensation provides a steady rate of form of payment, the use of performance incentives allows the organization latitude in compensation and allows employees, through motivation, the ability to increase their earnings. Beer and Cannon then look to additional scholars that believe merit pay, and the use of incentives, is inherently dysfunctional. These authors, including Kohn, Amabile, and Meyer, propose that incentive systems, and the motivation they produce, are theoretically flawed, they also believe that individuals do not respond to incentives in predictable ways, and thus any compensation system grounded on that premises is misguided (qtd in Kohn 54; Amabile 10; Meyer 39-50). They also postulate that monetary incentives have a destructive affect on employee self worth, intrinsic motivation, and creativity. They state that even if incentives do work as designed, and productivity is positively affected, the result is that the employees are more motivated by the possibility of gaining the reward than accomplishing other things that would enhance the organization (qtd in Kohn 54; Amabile 10; Meyer 39-50). Here these scholars illuminate the idea that the concept of using incentives as motivation is ultimately detrimental to worker morale. They propose that the impending positives of the system outweigh the negative results, and that the entire concept is flawed; yet they never discuss the use of intrinsic motivation. While the authors agree that incentives can have a positive effect on employee performance, they also postulate that those same incentives can have negative results on employee morale and the ultimate success of the organization.

The team concept involves the use of a group of individuals, all with diverse backgrounds and different capabilities, working as a unit to accomplish a single, or series, of projects. For a team to be successful, the members must have similar goals and must share a common focus. The literature explained that the use of teams has grown, and is now becoming an accepted practice in both the public and private sectors. While teams can be examined from any number of perspectives, the literature provided for two: team incentives/awards and team functionality.

### **Team Incentive/Awards**

Team incentives and awards affect the motivation and ultimate success of a team in completing assigned tasks. The literature discusses the team concept from the perspective of performance-based pay, including how particular incentive and award schemes effect the over team function. While the teams are certainly driven by other factors, the type of incentives offered, especially within a merit pay system, can have effects on team cohesion and its overall function.

In the Colorado State article, the authors comment on the importance of team awards, and agree that the team should share in all incentives once goals are reached. They postulate that no matter the type of incentive offered, all levels of the organization should share in the accomplishments (Pg 3). That is, once the performance standard has been surpassed, not only the individual workers, but also the management and owners, should share in the rewards. They feel that the shared incentives throughout the organization, including employees, management, and owners, provides congruency in goals and foster teamwork.

Sue Fernie and David Metcalf examine team awards and their relationship with merit based pay. They first comment on individual performance-based pay schemes within the team concept, and state that an individual based incentive plan, one that recognizes individual effort,

lends itself to the problem of worker's putting their concerns for increased earnings over the interests of the team (Pg 3). Here the authors expose the inherent problem with the utilization of individual based pay in the team environment. Emery agrees with that summation as he states that many performance-based pay systems are implemented with a lack of financial resources, insufficient training for managers, and the intrinsic dichotomy of promoting team work while awarding individual performance (Pg 158).

The CIPD authors also address the issue of individual performance and its placement into the team concept. They advise that any incentives that are in place for the team may be affected by individual performance rewards (Pg 3). They also postulate that individual, hierarchical, pay structures are inappropriate for teams, because they make it difficult to foster team spirit when individuals are concentrating on personal gain (Pg 4). In the same vein, the CIPD authors tout the use of team incentives and question the utilization of individual incentives. They explain that while team rewards reinforce proper teamwork, group cohesion, and encourage group endeavors, the use of individual rewards intuitively forces management to look at the team based on the individuals involved, and this inhibits the effectiveness of the team (Pg 5).

Fernie and Metcalf then espouse use of the team concept in not only completing tasks, but by incorporating incentives. They stated that the use of the team concept should allow for incentive payments to workers based, not only on their personal performance, but also on the performance of the team (Pg 3-4). They continue by predicting that the use of the team approach would be more effective than the individual approach in tying incentives to performance (Pg 12). In a study based on that prediction, the authors found that the use of performance-based pay, in itself, does not enhance productivity, but that the use of the team approach, coupled with individual and team incentives, does yield positive effects on performance (Pg 11-13). That is,

the use of a performance-based pay scheme that incorporates both individual and team incentives delivers superior performance. Bohnet and Eaton, as an alternative to individual incentives, promote the idea of a team reward system. They propose a system that can effectively compensate the team members for their efforts and contributions as they relate to the accomplishment of team goals would be an effective alternative (Pg 9). The authors also state the importance of such a system in mitigating the effects of the “free rider” problem, the dilemma in which certain members of a team fail to contribute and force others to do more (Pg 9). In these ideas on teams and incentives, we find the resounding notion that for the work of a group, or team to be fairly evaluated, it must be measured in relation to the team as a whole. Any attempt to judge team performance based on unassociated individual measures, clearly will have inherent problems of equity and will affect the team dynamic.

### **Team Functionality**

For a team to be functional, it must possess certain attributes. The literature addresses the ideas of teams having shared goals and motivations, and the ability of a team to work together in a concerted effort. In addition, the concepts of team stability, peer pressure, and other issues that effect team function are important to the overall success of the team concept.

Emery begins the discussion on team functionality by stating that the growing infatuation with teams, or groups, which began in the 1980’s, has become an accepted, and significant, way to accomplish goals (Pg 158). Emery continues by espousing the collective action of groups over the ability of an individual, and he quotes studies that show that teams make decisive contributions to innovation, quality of service, cost reduction, and productivity (Pg 163). The important point is that the team concept works to accomplish goals while having the ability to incorporate a wide array of ideas and abilities of diverse personnel. Likewise, Fernie and

Metcalf agree with the value of the team concept when the postulate that the team approach internalizes performance norms through which each member expects and values fair treatment, and works for the good of the team and thus the good of the organization (Pg 10). In CIPD article, the authors add that any team incentive should include some from of intrinsic award, for while monetary rewards are important, the recognition of the team at the completion of a project is more gratifying and more sought after (Pg 3). These ideas are important in that they identify some of the core concepts of performance-based pay schemes and couple them with the belief that the use of a team will further develop these concepts and ingrain them in the organization. In further support of the functional team, Fernie and Metcalf point out that the team approach allows for peer pressure in avoiding the free rider problem (Pg 4). The use of “peer pressure,” when employed by group members, maintains group norms and provides the ability to observe all aspects of the individual’s performance to ensure it is congruent with that of the organization. Another important point here is that the team concept controls the behavior of its members, which then leads to a group “buy in,” and the ultimate adaptation of the organization’s performance plan.

Emery then addresses some important ideas relating to the team concept. He states that for a team to be truly functional they must be in a position to influence the result that they produce, that is, that there needs to be causality present for the team to feel it has accomplished something (Pg 161). Additionally, Emery states that a clear link between individual, team, and organizational objectives must be established in order to ensure congruency within the process, and the performance measure must be complex, yet transparent, in order to allow for understanding, but not manipulation (Pg 161). In these ideas, the use of the team concept, when coupled with the ideas contained in performance-based pay systems, provide an instrument for

the efficient management of an organization's human resources. To that end, Emery furthers the notion that the ultimate attainment of organizational goals is positively effected by the use of the team concept.

Funding is an essential element in the functional implementation and management of a performance-based pay system, for even if a system is structured properly, communication is open, the evaluation process is transparent, and all the other core tenets are in place, it will never function without bursary. In much of the literature there was no mention of system funding, this is exceedingly true in the literature from the private sector. It seems that the inclusion of the funding aspect of a new system, escapes the notice of private business. It is understood, by the company and the employees, that any new system will be funded. I think the notion is correct, for it would be ridiculous for a company to invest in a new pay system, including training and implementation costs, only to abandon it for lack of fiscal planning. While this concept fits in the private sector, the public sector, government in particular, has an inherent problem with funding issues. The literature examines these problems and offers some information on mitigating them. The concepts are expressed as preparation and limitations

### **Funding Preparations and Limitations**

Unlike organizations in the private sector, governmental organizations must compete for funding against one another. This has led, and will always lead, to shortfalls in the funding for agency projects. While the private sector utilizes market strategies to ensure fiscal viability, public sector organizations must rely on other, separate entities, for their fiscal concerns. In essence, public organizations can initiate and implement new programs and systems, including performance-based pay, only to have funding for those initiatives withheld or completely denied

by Congress. In the literature, for the most part, only government agencies point to funding as a major issue, and even then, they do not offer many solutions. Funding preparation and limitations examines the concepts of funding, both exploring the outcomes of funding shortfalls and some ways to mitigate them.

Beer and Cannon discussed the issue of funding limitations and its effect on pay systems and employees, stating that very often there are limits on bonus payouts or shortfalls in overall funding, and that any failure to pay promised incentives is perceived by the employees as inconsistent with their agreed upon performance standards (Pg 5). In this we find two of the most important obstacles with funding. The problem of limited resources to pay incentives is important in that once a system is implemented, the goals are set, the evaluation process is conducted, and an employee performs at a level to warrant an incentive payment, failure of the organization to actually pay the incentive is destructive to employee morale and detrimental to the legitimacy of the entire system. The GAO study discussed the issue of funding preparation in mitigation of funding shortfalls and cited that the U.S. Office of Personnel Management reported that the increased cost of any alternative pay system should be budgeted for before its implementation (Pg 5). The GAO also advised in their demonstration projects, the direct cost of salaries, training, automation, and data systems were the major considerations when implementing their respective performance-based schemes, and budget adjustments were needed to address those items (Pg 5). The HRMP panel agrees with advanced funding preparation and believes that it is exceedingly important that agency budgets be set at levels that will allow the full funding of any new pay system, reasoning that, if on any occasion a system is not funded its legitimacy will be in question (Pg 27). This falls in line with the accepted reasoning behind budgeting for the system before hand. In relation to the implementation of merit pay systems,



the panel stated that “agency salary budgets will be set at levels necessary to fully fund the pay systems (Pg 26).” That is, government agencies budget for expenses on an annual basis, and it is paramount that their budgets allow for the payments of performance incentives. Instinctively these considerations are significant, yet government funding for performance-based pay has always been an issue, and very often the problem is not recognized until payments are due. The GAO then points to approaches used in their government demonstration projects using performance-based pay. The GAO states some projects utilized annual, general pay increases and locality pay adjustments for funding (Pg 6). The use of these types of funding streams can be effective, the basis being that those regular, annual, pay increases are automatic and thus the funds will always be available. The GAO also reports that other projects managed cost by considering fiscal conditions and the current labor market conditions in deciding the amount to budget for pay increases in the future (Pg 7). This approach could also be effective for it incorporates planning in advance to ensure appropriate funding is provided. In both these approaches, the GAO gives general approaches to managing funding, but makes no attempt at explaining the central problem of funding control. Public organizations do not control funding. Funding is the responsibility of Congress.

The use of pay banding, that is, the division of employees into bands, containing a maximum and minimum compensation rate, is a general concept in performance-based pay schemes applied in government organizations. The bands range from novice, new hires with little experience, to senior expert, reserved for the most knowledgeable and experienced employees. Employees, upon hire, are placed in a particular band based on job classification, experience, and other considerations. As an integral element of a performance-based pay plan, pay bands provide that the employee is then meritoriously promoted through the bands, or

awarded compensation increases within the bands, as dictated by their performance. The literature examines pay banding based primarily from a governmental perspective, and it is explored both as a functional system and through its implementation.

## **System Function**

Pay bands are an integral feature of performance-based pay. They are utilized as the structure in which the merit pay systems operate, and can be examined as to their function and expected outcomes in supporting those systems.

In reference to pay banding and it being a functional replacement for the General Schedule, the NCPS forum concluded that narrowly defined pay structures like the General Schedule, that set specific perimeters for salaries based on a predetermined measure of time in grade, make it difficult for government organizations to compensate new employees on par with the private sector (Pg 11). The HRMP agrees that the General Schedule is outdated, and that for the government to continue to both hire and retain high performers the implementation of a performance-based pay system is imperative (Pg ix). The NCPS suggest in replacement of the General Schedule utilizing six to eight broad pay bands, involving larger salary ranges within each successive band (Pg 13). They believe that the use of such a system will allow for the managers to have greater discretion in setting salaries based on the market and demand for certain skills. To that end, the HRMP also believes that the use of open salary bands will provide flexibility for agencies to manage their salaries, while being better able to support their individual human resource needs (Pg 4). Both panels see pay bands as central to the operation of a performance-based pay scheme.

## **System Implementation**

The way that pay bands are implemented in an organization can determine the ultimate acceptance and success of the merit pay system they are an element of. Training is also an important aspect of implementation, especially as it relates to those charged with the functional management of the system. In the system implementation, an approach to the proper implementation of pay bands is examined, along with the issue of training the managers that drive the merit pay system.

The HRMP panel addresses the implementation of pay banding and how it should be incorporated into government organizations. The panel suggested initially aligning the new broad pay bands with the pay grades of the General Schedule, but over time using market pay trends for needed skill sets, to make adjustments (Pg 28). The HRMP panel believes that this incremental approach will alleviate the initial discomfort that accompanies change. The initial alignment of the pay bands with the General Schedule mitigates the negative, at least initial negative, results of the change over. It allows employees to remain at their current salary and ease the change in over time. In addressing training concerns as they apply to system implementation, the HRMP panel stated that adequate training must be provided to managers, and that it is important due to the tremendous role that managers play in the implementation process (Pg 6). For the sake of discussion, it seems likely that the same problems inherent in the General Schedule are present in pay banding. The most glaring is the role of first line supervisors as the catalyst for the system. The same managers that implemented the General Schedule, with its problems, will be the same managers charged with the administration of pay banding. This general statement on manager training is important, but it fails to offer solutions.

## **Important Case Studies**

In an effort to understand performance-based pay issues within some context, and in further examining the Beer and Cannon Study and the GAO Study, it became clear that a full examination of the case studies, and the conclusions drawn from them, would enhance an understanding of how varying forms of merit pay systems operate in the public and private sectors. While the case studies in the Beer and Cannon study are real world studies implemented and measured, the cases from the GAO are drawn from test projects and are more open to manipulation. Beer and Cannon begin to discuss the case studies on performance-based systems, but first restated that management is the key to proper implementation, and that in the implementation phase, management usually fails to acknowledge the possible pitfalls and challenges leading to even larger issues (Pg 5-6).

With that in mind, in the mid-1990's Beer and Cannon had the opportunity to study the managerial experience of implementing performance compensation programs at thirteen Hewlett Packard sites. At these sites, the managers had great discretion and autonomy in the implementation and evaluation of the systems (Pg 7). In fact, if managers felt the cost and benefits were not proportional, they could cancel the programs at any time. Additionally, for the most part, groups engaged in blue-collar production work, with the exception of one group of engineers. The performance based pay schemes were implemented based on the need for additional inducements to achieve goals, enhance learning and team behavior, and to provide additional compensation for increased spans of control brought on by restructuring.

Beer and Cannon were allowed to review documents and to interview managers who sponsored those incentive programs. The incentive programs involved team and skill based pay systems, including profit sharing from group gains, cash incentives and bonuses (Pg 7). Of the

sites in the study, half were located outside the United States, spread throughout five countries. The authors also found it important, as I do, to place the study in context. They advise that at the time, Hewlett Packard's human resource management policies included the use of decentralized business units, a strong commitment to management by objectives, participative management, and delegation of responsibility to the lowest level, including extensive communication, recruitment and hiring policies focused on technical and interpersonal skills, and a career system based on internal promotion and cross-functional, or divisional movement (Pg 7-8). The authors continue by reporting on five of the thirteen sites, and extrapolating their findings.

At the San Diego site, which initially utilized a performance-based pay system in which managers would divide work group objectives into individual assignments, monitor the individual contributions, and pay incentives on an individual basis, a new team pay for performance was established. The new system was implemented to motivate performance and the achievement of work goals, such as team process improvement, production, and quality. The system provided for teams of workers to be monitored as they attempted to achieve their set goals. The system set three levels of pay increases, with no "take away" for failing to meet team goals (Pg 9). With the achievement of level three, the highest level, group members received \$150-\$200 additional pay per month. In addition, the new system had a component, Pay for Contribution, which allowed for additional compensation based on the employee's ability to demonstrate competence in performing additional tasks within the group. As the employees showed proficiency in a more diverse array of skills, their base salary was increased. The reasoning was that this contribution component produced a continuously learning workforce capable of adapting to new situations. After six months, the teams operated well within the system, with the majority outperforming goals and reaching the level II or III, yet with such a

high level of achievement, the company felt the original goals were set too low and modified the program (Pg 10). The modifications met with resistance from the employees who had begun to rely on the additional compensation, and this led management to conclude that the workers were concentrating on their pay and not the actual work (Pg 10). In addition, management found that certain circumstances, outside the team's control, had affected their performance, and that the teams began to engage in team exclusivity (Pg 11). That is, the team would exclude any new member that they perceived as a weak link. Relative to the Pay for Contribution, the workers felt that the program placed an inordinate amount of stress on them (Pg 11). The need for testing and evaluation, coupled with the company's initiation of lowering base pay for an unsatisfactory score during initial testing, ultimately culminated in the employees refusing to take on new tasks and the system becoming dysfunctional. In the end, both the team performance and pay for contribution systems were discontinued after a year in the largest division, and at the whole site shortly thereafter. The manager's felt that the systems did little to motivate employees, and that the constant necessity of re-engineering the pay system to overcome continuing problems was too costly both in manpower and employee moral (Pg 11-12). At this site, the problems discussed throughout the literature were realized. The use of the team concept, while functional as to increased production, was affected by modifications in the system once implemented. As well, the team's practiced exclusivity and the effect of external factors on the team's overall production were negative outcomes. These unforeseen consequences of the team concept ultimately led to the demise of the entire system.

At the second site discussed, the Boise Print Shop, HP had recently switched to self-managed teams, and management implemented a pay system, Skill Based Pay, which they felt would complement the individual and team performance (Pg 12). The system allowed for

increased pay based on skill level if the team, and individuals, reached their performance objectives. If the team was among the highest performers for the month, they received a bonus. If the team continued to perform well, above average, the individuals were allowed to pursue development and advancement to the next skill level, bringing enhanced compensation. As stated earlier, the teams were designed to be self managing, therefore if a team experienced any performance problems, as determined by peers and management, its members were not allowed to seek new training opportunities until they were corrected. The program was designed to provide additional pay without negative repercussions for lagging team performance. The results of the system were similar to those in San Diego (Pg 13). After months, teams received more performance based pay than expected by management. As a result, although management attempted, they found it very difficult to reset the pre-established goals. The teams, as experienced in San Diego, also engaged in exclusivity. External factors also affected the ultimate goal accomplishments and caused problems with employee moral. The self-management portion of the system, in which management, as well as, peers judged performance proved too problematic as well. The team members found it difficult to judge their peers. If negative feedback was received, tempers flared, and in the end bad evaluations were attributed to ineffective measurement tools and the subjectivity of coworkers (Pg 13). In the end, the system was dropped. Managers decided that employees had become too focused on pay and less on tasks. In this case there are some of the same issues already discussed. However, the concept of self-management was examined. Self-management in this context encompasses the same ideas as manager-worker issues. The point here is that the human condition is constant, and that just as managers were adverse to documenting negative outcomes in performance, we see that peers have the same problems.

PRCO Loveland was the next site examined. The fabrication shop had been slow in reaching performance goals, and manager's felt the utilization of performance incentives could increase production to 95% of their target output (Pg 13). Managers implemented a bonus program in which everyone at the site would earn a performance bonus of \$250 if the goal was reached (Pg 13). In the end, the site failed to reach its goal and no bonuses were paid. The workers showed no discontentment with this; though many felt insulted that the company had attempted to bribe them to work harder towards a goal they were already motivated to achieve (Pg 13). Managers did state, however, that the bonus plan did highlight to the employees, management's commitment to achieve the goal. In the final analysis, the managers decided it would have been more effective to coach and train their employees in ways to achieve the production goals, then to offer the bonuses (Pg 13). In this case, though not specifically referred to, the issue of intrinsic versus extrinsic rewards is apparent. The workers felt "bribed" by the offer of monetary compensation to achieve a goal that they were intrinsically motivated to achieve.

The Colorado Memory Systems site, which was taken over by Hewlett Packard, had never utilized a profit sharing program. CMS management felt that allowing the new employees to benefit from the stock prices when the company was taken public would enhance performance (Pg 14). Although the company was never taken public, CMS management attempted, but failed because of cost prohibitions, to implement the HP profit sharing system. Instead, the company implemented a local gain-sharing program separate from HP. The program's goals were to increase individual initiative, individual responsibility, willingness to learn, team building, collaboration, willingness to confront conflict, and increased focus on attentiveness (Pg 14). The program centered around bonuses, which would be paid on a quarterly basis, based on the



attainment of certain levels of operating profit. In the end, management reported that the program increased visibility between departments, or the effective use of diverse teams to achieve goals, heightened awareness of business fundamentals and financials, clearly defined and communicated objectives, and created a uniformed company wide focus (Pg 14-15). However, the program also resulted in employee perception that the program was utilized to promote short-term behavior. The employees also felt alienated from their new parent company because they were not afforded the same profit sharing as other HP employees (Pg 15). In the end, management decided that the program's failure to bring CMS employees even close to the compensation level of other HP employees, and the employee's loss of confidence in the program as a result, was enough to discontinue its use (Pg 15). The use of this type of incentive system is directly related to concept of meaningful rewards. The use of any incentive system, as found in the literature, must be based in an award payment that is perceived as both fair and equitable. In this case, the inability of CMS to offer the same level of incentive pay as HP led to a lack of equity, and a doubt as to the validity of the system itself.

The final site, The Workstation Group, was centered on the introduction of UNIX-based workstations in the 1990's (Pg 15). Performance with high technology products, and in the high technology arena for that matter, is contingent upon speed. Management was therefore concerned that the UNIX product be completed, with high quality, and with all the support services established, in a timely manner. With that, management attempted to motivate, in this case software engineers, to be more efficient and effective by the use of experimental pay. This system offered two bonus packages, one for managers and the other for the engineers, both of which were to be paid after the completion of the project (Pg 15-16). The performance goal was that the project would be completed by a preset target date. The mangers were offered cash and

stock option rewards due to the importance of their decision-making, and the engineers were offered cash incentives only.

The program was implemented for the short-term goal of completing the project, and managers would be paid their stock options six months after completion, in order to benefit from the expected positive effect on share prices as a result of the project (Pg 16). Engineers would be paid their bonuses based on individual contributions as determined by a nomination and approval process upon project completion. The project was completed six months ahead of schedule. The success of the project may be attributed to the performance-based pay, however, management believes that the simple implementation of the plan communicated the project's importance, and thus acted as an inherent motivating factor (Pg 16). While 70% of the employees stated that they would have worked just as hard on the project had incentives not been offered, 60% stated that they would recommend the use of performance incentives on future projects (Pg 16). In the final analysis, as stated by a local personal manager, the pay system was a great catalyst in the project (Pg 16). In this case, the concept of using performance-based pay for complex tasks is exemplified. The engineers were charged with completing a project that entailed a tremendous amount of abstract thought, complex skills, and mission specific knowledge, all of which, as discussed in the literature, can cause problems in the evaluation process. In order to mitigate these potential problems, management used a simplistic incentive measure based not on individual performance, but on the team's ability to complete a task. Additionally, as espoused in the literature, this type of performance measure allows for the members of the entire organization to share in goal attainment.

Some of the significant findings Beer and Cannon discovered about performance-based pay in the Hewlett Packard experiments, are that team based environments tend to produce

increasing performance results, while the implementation of other alternative pay systems have not proven necessary to produce those same outcomes (Pg 17). As a result, HP decided that its current pay system and other tools, were sufficient to support the work team environment. Furthermore, even though HP gained valuable organizational learning from alternative pay experiments, the resource commitment necessary to design and implement pay system, changes, and the limited return so far, indicates the HP does not need additional experiments unless they are markedly different (Pg 18).

In addition to those findings, the authors point out that the managers in the study had difficulty in relating level of performance to compensation at the operational level. The cause in some ways is due to the subjective nature of measurement. In the end, managers concluded that they could achieve the same result with proper coaching and the use of other management tools (Pg 19). The need to make adjustments to the system also proved problematic. Once performance levels are set, any change has a negative effect on legitimacy. Additionally, if the workforce is constantly expecting additional pay for additional progress it is intuitive that problems may result.

In continuing on to the case studies provided by the GAO, it is important to stress that these studies are somewhat controlled by their very nature. However, they offer some very progressive concepts in relation to functional performance-based pay schemes in the public sector. The projects included: the Navy Demonstration Project at China Lake (China Lake), the National Institute of Standards and Technology (NIST), the Department of Commerce (DOC), the Naval Research Laboratory (NRL), the Naval Sea Systems Command Warfare Center (NAVSEA), and the Civilian Acquisition Workforce Personnel Demonstration Project

(AcqDemo). These demonstration projects were diverse in their respective missions, personnel, and organizational culture.

In that diversity, the projects were able to test the functionality of a number of pay schemes. The demonstration projects utilized different concepts as they implemented their respective performance-based pay systems. With respect to measuring employee competencies, AcqDemo decided to evaluate its employees against one set of factors utilized across the organization (Pg 10). AcqDemo also used “Discriminators” and “Descriptors”, two tools that help define the performance factors (Pg 10). The project used six factors in determining employee performance, problem solving, teamwork cooperation, customer relations, leadership/supervision, communication, and resource management (Pg 11). In furtherance of those factors, discriminators were used to give a more in-depth description of what constituted each factor, while descriptors were used to measure the level of performance that was expected from an employee within each level, or pay band. AcqDemo also implemented the concept of weighting the competencies, that is giving one more importance over another, and while they did institute a process, they also decided that all factors would be weighted evenly across all positions, that no one factor would be weighted less than half its original weight, and that all employees were to be advised of weights at the start of the evaluation period (Pg 11). The concept of weighting can affect the perceived equity of the system, but here that is mitigated by the transparent nature of the evaluation process and the communication of the system’s central tenets.

While organizational wide competencies can be functional, the NRL project chose to utilize “critical elements,” specific competencies that were applied to each individual career path (Pg 11). In addition, supervisors were given the ability to develop additional individual

performance standards as they felt were needed. As in AcqDemo, descriptors and discriminators were utilized. An example of the NRL project's competency assessment based on a Science/Engineering Professional career path was explained. Within that career path, the critical element is scientific and technical problem solving, while the discriminators are level of oversight needed, creativity, technical communication, and recognition. The descriptors included "recognized within own organization for technical ability" and "recognized internally and externally by peers for technical expertise," both representing a different level of pay grades or bands. Management used the critical elements, measured them by the discriminators, determined the level of performance within the employees pay level, assessed any additional performance measures placed on the employee by their supervisor, and arrived at a performance achievement measure (Pg 55). While NRL did utilize weighting, the project decided that only the critical elements should be weighted, and that most often weighting was used for the scientific/engineering career path (Pg 11). Here the use of critical elements specifically addresses the performance of each employee's competency as applied to job performance. The continued use of the defining tools, descriptors and discriminators, add even more specificity to the evaluation process, and provides the system with internal consistency.

Both the NIST and DOC projects decided to utilize the critical elements, yet they applied them differently than NRL. Instead of basing the critical elements on career paths, the NIST and DOC tailored the elements to each occupational position. The DOC determined that the diversity of their workforce, each position had varying degrees of responsibilities and duties, required a system that could differentiate between those factors (Pg 11-12). The DOC's plan utilized a minimum of two, and maximum of six, critical elements, along with major activities to perform the elements (Pg 12). The supervisors would then weight the critical elements based on

time on task and importance. The weighting was accomplished at the supervisory level, with no tracking at the organizational level. The ultimate evaluation was done using a Benchmark Performance Standards. The standards ranged from the highest standard, “objectives were achieved with maximum impact, through exemplary work that demonstrated exceptional originality, versatility, and creativity,” to the lowest, “objectives and activities were not successfully completed, because failures in quality, quantity, completeness, and timelines of work (Pg 12). The China Lake project also used competencies tailored to individual responsibilities. In that project, the general rule that all criteria must be consistent with the employee’s work unit goals and objectives was central (Pg 12). Additionally, the competency objectives could be set in two ways; the Task Approach, which measures the employee’s output, and the Functional Approach, which determines employee’s required skills and how well they are to be performed (Pg 12). The employees and supervisors then choose from a prescribed set of skills including planning, analysis, coordination, and reporting/documentation. In the end, employee performance was measured based on those agreed upon factors. In utilizing the concept of critical elements in the evaluation process, these three projects found that it was more simplistic and an easily administered process. Though each used some variations in conjunction with critical elements, all grounded their system in the concept of differential measures for diverse employee responsibilities.

In translating performance ratings into actual pay increases, the GAO provided that a typical high performing organization seeks to achieve three objectives through the use of performance management; provide candid and constructive feedback to individual employees and maximize their potential in realizing the goals and objectives of the agency, provide management with the objectives and fact-based information it needs to reward top performers,

and provide the necessary information and documentation to deal with poor performers (Pg 12-13). With that in mind, The China Lake Project used a predetermined range of pay increases to reward employee performance (Pg 13). The supervisors utilized a numerical rating system, based on three assessment categories predicated on the employee's performance, which translated into "increments." These individual increments corresponded to a permanent pay increase of approximately 1.5 percent of the employee's base salary. The numerical rating ran from a 1, highly successful to a 5, less than fully successful. Increments were rewarded beginning at a 3 rating and continuing to a 5. The results of this measure were that 11.3 % of employees received a 1 rating, 44.6% received a 2 rating, 44.0% received a 3 rating, while only 0.2% received 4 and 5 ratings (Pg 14-16). The average permanent pay increase was 3.5%. In a similar system, NAVSEA used a performance system in which an employee's performance rating was tied directly to predetermined permanent pay increases, one time rewards, or a combination of both.

The system used three steps to translate ratings into pay increases. Initially, the supervisor rated the employee's performance as either acceptable or unacceptable. Those rated as unacceptable would get no further consideration (Pg 17-18). Upon rating an employee acceptable, the supervisor would then rate the employee as a contributor, major contributor, or exceptional contributor, and recommend a number of pay points (Pg 19). Pay points are a numerical rating from 0-4, which are dependent on the employee's rating and current salary, and equaled approximately 1.5% of the midpoint salary within a pay band. Pay points could then be translated into permanent pay or one time rewards beginning with 0-2 points for a contributor, 1-3 points for a major contributor, and 2-4 points for an exceptional contributor (Pg 17). NAVSEA used some subjectivity in deciding who would receive permanent increases or awards, but most

often those who were deemed top performers were awarded with permanent increases, with the caveat that those employees whose salaries were below the midpoint of their current pay band were given permanent increases as well (Pg 17). The one-time awards were reserved for those employees whose contributions were equaled to their base salaries. The results showed that 39.6% of employees were rated as exceptional contributors, 40.3% were rated as major contributors, and 20% were rated as contributors. No employee was rated as unacceptable (Pg 18). The average permanent increase was 1.3% and the average one time award was \$1100.00 (Pg 18).

The use of these evaluation and rewards schemes show the diversity that can be incorporated into performance-based pay systems. While both of the projects concentrated on managing employee movement and incentive payment amounts, they also utilized the band system to facilitate their individual merit systems. An interesting point lies in the evaluation outcomes of both schemes. The NAVSEA project had no employees rated unacceptable and China Lake had a miniscule percentage. While it is possible that all employees performed at acceptable levels, there could be some intervening issue that caused these outcomes.

In using a different system to tie performance ratings to actual pay, the DOC project delegated ratings evaluation, and their translation to pay, to individual pay pools. These pay pools were inter-agency organizations that determined the amount of money that was to be paid for performance within a group or the entire organization. In this system, the supervisors evaluated employees on a range of performance elements from 0-100. Employees with less than 40 were deemed unsatisfactory were not eligible to receive any form of permanent pay increase, reward, or locality pay. Those employees rated above 40 were eligible for general pay increases and locality adjustments, and were also eligible, at the discretion of the pay pool managers, for



performance based pay increases and rewards. The pool managers then made decisions on performance increases based on an employee's performance score and current salary. Employees with lower salaries within their respective pay bands were eligible for higher increases and usually were awarded permanent pay increases, while those who were at the top of their pay bands were awarded one time rewards. In this evaluation and reward scheme, the concept of incentive pay in proportion to base salary is exemplified. As stated earlier, for a reward to be meaningful, it must be perceived as so. The use of proportional incentives addresses that issue. The results showed that 41.7% of employees were rated 90-100, 45.1% were rated 80-89, and 11% were rated 70-79. Of the remaining employees, 1.7% rated 60-69, .2% rated 50-59, 03% rated 40-49. No employee was rated unsatisfactory. Here again managing the amount of employee payments is a central motivation, yet the additional use of pay pools and proportional incentives incorporate a diverse array of management tools to that end.

The GAO then pointed to the issue of managing an employee's movement through the pay bands as an important factor in maintaining a performance management system. This concern is grounded in the possibility that, if unregulated, employee's may very quickly progress through pay bands, and the organizations would be unable to absorb the resulting costs. The NIST project managed movement through pay bands by awarding higher pay increases to employees who are at the bottom of the pay band, and gradually tapering off the amounts of permanent increases as the employee progressed within the band (Pg 29). Within each pay band, five intervals determined the maximum percentage that could be received from permanent pay increases at any one time (Pg 30). Similarly, China Lake and NAVSEA utilized checkpoints, or "speed bumps," within their pay bands (Pg 30). These measures were used to manage the cost of salary increases, while ensuring that that the performance system accurately portrayed salaries as

employees moved through the pay bands. An example provided at China Lake was that when an employee advances to the midpoint of his or her pay band, any further permanent pay increase must be accompanied by a rating of highly successful and be authorized by a senior management review board (Pg 30). A kin to managing employee movement and pay is the idea of utilizing one-time rewards in the place of permanent increases. It is intuitive that a one-time reward will be less costly in the long run than a permanent increase, and the NAVSEA project incorporated that concept when it utilized a system that paid one-time awards as employee's progressed higher within their bands (Pg 31). Additionally, the China Lake project allowed pay pools to transfer budgets for awards to those for permanent increases (Pg 31). The concepts utilized by these projects to control employee promotions, incentive payments, and increases are necessary to manage pay banded systems, yet these same management tools can also have negative effects on the ability of employees to progress, at acceptable intervals, in the event of funding problems, or as discussed earlier, the bastardization of the system.

In examining the research, there was an inherent delineation between public and private organizations and their approaches to, and motivations for, performance-based pay schemes. In the private sector merit pay is ingrained in the capitalist philosophy where monetary incentives drive production, while the public sector is motivated by a different set of incentives that are related to serving the public and feeling involved in the process.

The research initially focused on the reasons for the advent of merit pay systems in the public sector. The idea that government must change to meet the changing environment, and current societal problems, was espoused in a great deal of the literature. The entrepreneurial spirit that is central to the private sector, that belief that incentives drive production, was touted as a solution to lagging performance in public organizations.

The concept of organizational culture was examined throughout the literature as well. Academic and government sponsored studies espoused the need for any performance-based pay system to fit the core beliefs of the organization. Also mentioned, was the understanding that the stakeholders must 'buy in' to the system for it to be effective. These two ideas are conjoined. For the effective implementation of merit pay into an organization, there must be compatibility with the core beliefs and goals of the organization, and the system must also be acceptable to the managers and employees.

The team concept and its relation to performance-based pay yielded some interesting information. Much of the literature touted the use of teams as a more efficient way to achieve diverse goals, and included the idea that a team must be evaluated as such. Explaining that, attempts to measure team performance, based on individual performance, had the inherent problem of incongruent goals. In the end, the literature on the subject espoused the use of both team and individual incentive schemes, reasoning that teamwork can be measured by outcome, and individual rewards can be given in relation to that success based on seniority, responsibilities, or other factors. The concept of peer pressure, as it relates to the free rider problem, was explored as well. The literature made the point that in the team environment, the pressure exerted on members by the team to conform has a highly motivating effect.

The concept of funding, a major problem in the implementation of merit pay systems in the public sector, was explored in the literature. This problem is central to government's implementation of performance-based pay. Remarkably, the government will expend large amounts of capital in the planning and implementation phases of new systems, but fail to continue funding the systems once they are initiated. This is due to funding being under the jurisdiction of Congress, while the implementation and planning are controlled by the individual

organizations. In all the literature, the problem was addressed, with the consensus being that for a system to be effective funding was a necessity. That is, funding the incentive payments in an incentive pay plan is essential to the legitimacy and continuation of the system.

Pay banding, as a system, was introduced in the literature. Pay banding, as theorized, would give the public sector the ability to respond to changes in demands for certain skill groups, which in turn, would allow for higher pay for certain workers, and the ability of high performing workers to continue earning increased salaries. The system is espoused as a replacement for the General Schedule, used by the federal government. The literature, without exception, was positive concerning the pay banding systems, yet the literature was also skewed. Since pay banding is fundamentally a replacement for the General Schedule, a government system, and most, if not all, of the literature on the subject was provided by government entities or studies by groups on behalf of government organizations, the information must be examined in that context.

## **Methodology**

In the process of this study, I reviewed the organizational documents of public sector institutions and interviewed their human resource managers and employees in an attempt to determine the functionality of their particular performance-based pay systems. The study is drawn from performance-based pay systems currently in use in the public sector and is qualitative in nature.

The study focused on four organizations, three in the federal government and one within county government. I examined and analyzed public documents, including the Federal Register and available organizational plans, which describe the pay for performance systems of each organization. Additionally, I was granted permission, and interviewed a human resource manager from two of the organizations and one employee from each organization. I questioned

the managers to clarify any confusing points found in the system and collected their opinions on the functionality of their particular system. Once the managers had been interviewed, I spoke with an employee currently working under each system. During that interview, I collected information on the employee's opinions of the functionality of the system and how it was working for the organization and individual employees.

The cases were chosen on the basis of the organizational type and the availability of information. The federal organizations were selected due to their number of employees, their organizational responsibilities, and their use of performance pay, while the county organization was selected due to its progressive management plan in incorporating performance-based pay.

The managers were chosen because they were the human resource representative for the organization. The purpose of the study was explained to them, along with the reasons that their organization had been selected. The managers then agreed to participate in the study.

The employees were chosen from a list provided by the managers. After contacting several of the employees, the employee who was selected for the interview had been employed in the system for at least two years and had an interest in assisting in the study.

The confidentiality of one of the federal organizations and the county organization, including the individuals that granted interviews, has been ensured. At no point in the study did I refer to any of those organizations, human resource managers, or employees by name. In referencing the organizations and individuals I utilized an alphanumeric system. Example, a HR manager in Public Organization 1 is referred to as SPUBORG1, and an employee in Public Organization 2 is referred to as WPUBORG2. The only organizations that I did refer to by name are the Department of Defense, and being that the Department of Homeland Security (DHS) and

its performance-based pay scheme, Max HR, are the subject of the study, I referenced both of those specifically.

The information I provided on the Department of Defense came from published government documents. Most of the information I presented in reference to the Department of Homeland Security and Max HR came from my personal knowledge or from published information. In addition I interviewed a manager from DHS in order to gain the perspective of someone who had been trained in, and was operating under, the Max HR system. The manager's confidentiality has been protected as stated above, referenced only alphanumerically.

I examined the documents first. The documents were analyzed from the reference of each organization's performance-based pay system. I examined the general tenets of each system, the implementation process, the evaluation system, each system's use of pay bands, rewards, teams, and finally the issue of funding. I then searched for patterns that indicated the success or failure of performance-based systems functioning within those organizations.

I then examined the interview data. The interview data were collected using open ended questions to elicit subjects' opinions on and attitudes toward their current performance-based pay system. The interviews were conducted in person or on the telephone, depending on the location of the subject. Some individuals were in other states. The data were analyzed by categorizing the subjects' opinions and attitudes based on four general concepts: the equity of the performance pay system, the success of the organization at implementing the system, the function of the system, and any other issues they felt were important.

The information learned from the analysis of the interview data, coupled with the patterns from the document analysis and input from the DHS manager was then used to assess

the impending implementation of Max HR and the possible affects on the DHS and its employees.

### **Study Limitations**

As this study begins and continues, it will become clear that the only information on the private sector was provided earlier in the research. Here I feel I must qualify the reasons for my ultimate decision to exclude the private sector. As I began my study, I attempted to gain the involvement of private businesses to show real world examples and collect valuable information on the diversity of performance-based pay schemes currently in use in that sector. However, though my attempts were assiduous, I was unable to find one company that would allow me to examine their current merit pay plan, or discuss it for that matter. Initially, I felt that my approach was lacking and changed it several times. First, using a “lead in” from the university, then keeping the fact that the study was for academic reasons masked, and finally by using the connections network to gain contact with management. In the end, none of my approaches were successful, and although a friend did get me an interview with a general manager for a large corporation, once I mentioned a study of his merit pay systems, he uttered the same word espoused by all who wish to keep their information private. He stated that the information was proprietary. On every occasion, without exception, no private company would give me the data needed for the study. In the end, I acquired an impressive document, on university letterhead, asking for cooperation for the purpose of an academic study. Though I sent many of the letters out, not one was returned. After three weeks, it became clear that the private sector was not interested in my study, and I was forced to abandon my attempts.

I feel it is also important to discuss the fact that I attempted to include some data from the third sector, non- profit organizations. The information discovered in relation to non-profits and

performance-based pay was theoretical in nature. In all the literature I examined, and in discussions with individuals involved in that sector, I discovered a good amount of theory as to how a system would operate, but found no functional systems that were able to provide sufficient data for the purposes of this study. In the future, I am sure the sector will begin to implement merit pay, but presently more study and examination is needed.

As a result of the small sample used in this study, its extrapolation to the other elements of performance-based pay not covered here is limited. While the study does yield compelling issues to be considered in the discussion of merit pay, it is not comprehensive enough to be considered conclusive.

My next attempt at collecting organizational data was enlightening. I will use the name of the organization due to the fact that the only information I was able to obtain was through literature that was published on the Internet. The Department of Defense has 300,000 civilian employees, and all are currently being converted to a new merit based pay system. In many attempts, both by telephone and E-mails, I was unable to reach a representative that would speak with me on this subject. While it is true that the system, dubbed the National Security Personnel System, has been embroiled in a number of court challenges, I felt that the organization would be willing to contribute to a study of performance-based pay within the government, but I was mistaken. On one occasion, a contact person, a relatively high ranking individual in human resources for the department, stated that it would be difficult to gain the information because the department was not forthcoming with any particulars at the time.

I then acquired government documents, via the internet, that explain the general tenets of the Department of Defense's new pay program and how it is intended to function. In this, I intend to document the main concepts of the system due to its significance in the present



discussion on performance-based pay. While I will have no input from human resource managers or employees, I believe that the DOD and DHS systems include the same general concepts, and feel the inclusion of this system is important to the outcome of my study.

## **Results**

The initial Department of Defense document I examined, the National Security Personnel System (NSPS) Proposed Regulations, stated the reasons for the proposed, impending, change. The DOD stated that the current, General Schedule, is inadequate to manage the civilian workforce in today's environment, stating that the hiring system is too slow, which inhibits the organization's ability to attract and retain quality employees. Additionally, the DOD explained that the current pay system fails to compensate outstanding performers over poor performers, and that the rigid, highly structured, current system hinders the DOD's ability to manage its employees (Pg 3). Here we find some of the same reasons for change as forwarded in the literature.

The DOD points to the changing environment and the need to attract and retain high performers. Inherent in those issues are the ideas of better efficiency by hiring and retaining better personnel and enhancing the effectiveness and efficiency of the organization. The DOD then stated the general tenets of the NSPS: Produce a high performing workforce and management, where employees and supervisors will be compensated and retained based on their performance; create an agile and responsive workforce, a workforce that can be easily sized, shaped, and deployed to meet mission requirements; ensure a credible and trusted system, a system which assures openness, clarity, accountability and adherence to the public employment principles of merit and fitness, and formulate a fiscally sound system, a system in which aggregate increases in civilian payroll, at the appropriations level, will conform to fiscal guidance, with a supportive infrastructure system, in which information technology support and

training will be available and funded(Requirements Pg 7). In these principles are the foundation for the system, and many allude to concepts already discussed. The NSPS will ensure that the system is clear and open, insuring that all employees understand the evaluation and rewards process, and are aware of all the important issues. This is good practice and will facilitate trust and validity in the system. The system also will ensure funding is available at the time of the appropriation, and will ensure training and technical support are available and properly funded. This statement is problematic in that the appropriations for the system will be decided by Congress and not the DOD. As a result of instituting the new system, the DOD expects to have high performing employees, who are motivated. The DOD also expects that it will gain the ability to react to mission critical issues in a more timely manner. While these expectations may be realized, it follows the ideas of a utopia, as alluded too in the literature, which is unrealistic. The system will initially experience difficulty, as all new merit systems will, and after needed modifications there is the possibility that the DOD could realize the positive effects it seeks.

As pointed to in the NSPS proposed regulations, an initial concern for the DOD in the implementation of the system was if the organizational culture, that of the civilian employee's, was prepared for the change (Pg 3). To that end, the DOD found that the employees had a strong sense of mission, understood how their work contributed to that mission (Pg 3), and with that, decided that the organizational culture was ready for the implementation of the merit based pay system. The document also pointed to experimental projects, and work studies, initiated by the General Accounting Office and the Office of Personnel Management, and engaged by the Department of Defense. The DOD stated that the success of those experiments led to the current implementation of the NSPS (Pg 2). The document then stated that the senior leadership of the organization, including Secretary of Defense Donald Rumsfeld, was supporting the new system

and that he had approved the NSPS regulations (Pg 2). Here again the principles found in the literature surface. The DOD understands that the system must fit the organizational culture and that support from senior management is also a determining factor of ultimate success.

In the NSPS Proposed Regulations , the DOD states that the system will operate utilizing pay bands. The system will group positions in broad career groups and will incorporate pay schedules that are based on the nature of the work, the mission, career patterns and competencies (Pg 7). Additionally, the General Schedule's pay grades will be expanded to include larger salary ranges based on level of experience and time on the job, ranging from entry level, to full performance, and ultimately, senior expert (pg 7). The DOD reasons that use of the band system will allow for more flexibility in assigning employees, the elimination of the need for specific, detailed, job descriptions, and that movement through the bands will be based primarily on performance and contribution. (Pg 7). Here the DOD, a government agency, follows the literature information verbatim. The positive outcomes expected from the pay band system are listed, the system is touted to result in those outcomes, but in the end there is no conclusive evidence that the results will be realized. As with all systems, the results will become evident as implementation and administration continue over time.

The NSPS system also includes an evaluation management element. The cornerstone of the element is the evaluation system. This measurement system is centered on first line supervisors working with employees to establish performance goals and expectations, all aligned with the department's mission. In addition, there will be a conduct recognition measure (Regulations Pg 7). That is, the system will incorporate a measure of the employee's behavior and professional demeanor, and that will be included as part of the employee's performance rating. Additionally, the element will involve intensive training for managers and employees,

ongoing communication and feedback between managers and employees, and will result in ultimate performance ratings reflecting meaningful distinctions in employee performance (Regulations Pg 7). This performance element of the NSPS again contains the imperative concepts listed in the literature. It first mentions the role of the first line supervisors in driving the system. While the inherent problems with human relationships in management, the inability or unwillingness of managers to properly implement negative aspects of management systems, have been explored in the literature, the NSPS ignores the problem and states that the supervisors will be trained intensively and will have communication and feedback, bottom up and top down, with employees. Once again a utopian view of the system. The human factor, as related to in the literature, is ubiquitous. While training can mitigate the problem to an extent, the use of communication and feedback will only be functional if, and only if, all involved are willing participants, the system proves to be legitimate, and the supervisors are engaged in positive, and more importantly, negative feedback, with their subordinates. Additionally, the inclusion of a conduct measure seems a bit abstract. With the discussion of subjectivity in performance measures, unless the measure is concrete, for example number of adverse actions or written reprimands, this measurement will be difficult to qualify and as a result could negatively impact the entire system.

The NSPS also contains elements of pay and compensation, which in turn effects the hiring and staffing of the organization. In relation to pay, the system will allow the DOD to move towards market sensitive pay, considering local demand for certain skill sets, and will facilitate greater flexibility in setting employee salaries (Regulation Pg 7). Additionally, the increase in an employee's pay will be based on performance and contribution, rather than longevity (Regulation Pg 7). The point being that the larger pay increases would go to the higher

performers, with no increases for unacceptable performers. The effect on staffing will be a streamlined hiring process due to the flexibility in salary assignment, the ability of the DOD, in conjunction with the Office of Personnel Management, to establish new hiring authority, tailored to the needs of the organization, and the ability to have direct hire authority for critical needs (Regulation Pg 7). These ideas exemplify the concepts that are realistic in performance-based pay, and in the NSPS particularly. The implementation of merit pay will allow more freedom in hiring, for it allows the organization the ability to make decisions previously controlled by the regulations of the General Schedule. The ability to make salary assignments, ensure that your organization is competitive in recruiting, and award your high performers, are all important attributes in performance-based pay. Additionally, the concept of paying for performance versus longevity is important in that it enables the organization to grow with the highest quality human resources. This, in turn, makes recruiting, hiring, and the system in general, much easier to manage.

The continued implementation for the NSPS has additional, paramount consideration. The problems of funding, discussed briefly in the discussion of the system, but more in depth in the literature, is a great concern for the DOD. While the DOD proposes that the additional costs of the current implementation process will be funded through training and current budget systems (Requirements Pg 14), the future of program funding is not as clear. In fact, with an understanding of the importance that funding has on the ultimate success of the NSPS, the DOD refers to the possibility of drawing funds from programs that may, or may not, be funded in the future. The Human Capital Performance Fund, a 500 million dollar fund to facilitate performance-based pay in the government, which was proposed by the current Bush Administration and was examined in the literature, has never been activated or funded, and is

one such resource referred to by the DOD as a source to offset the continued cost of the system (Requirement Pg 14).

In addition to the points already examined, and in regards to my study, the DOD considers interaction with DHS, due to the common features of their appeals and labor systems, to be important. The DOD believes that a collaborative relationship between the two organizations will benefit both (Requirements Pg 16). This idea of this relationship is interesting, but not surprising. Both agencies are in the process of implementation, both are being challenged in litigation and suffering defeats, and both are attempting to change the entrenched General Schedule. In addition, both organizations have large numbers of employees with a diverse array of job titles. While these issues are factual, the problem with a unified front, from the perspective of the employees, is that the two organizations have a great deal of power. In the event that both systems are fully implemented, employee perception of implementation equity may be negative.

This examination of the National Security Personnel System has illuminated the general tenets, the operating guidelines, and the elements involved in the system. While it falls short of examining the system in action, it is important to understand the system, how it is being implemented and how it will be managed. The DOD, like DHS, is currently involved in implementing performance-based pay concepts into the federal government. Concepts that are foreign to the culture and are being met with great resistance. The inclusion of this information is valuable to this study.

The next organization, which will be referred to as PUBORG1, involves a federal organization that has been in existence for four decades. It is a large organization involved in transportation, and has employees throughout the United States and abroad. PUBORG1 first

began to implement performance-based pay in the 1990's, and today has a merit based compensation system firmly in place. Like other government organizations, PUBORG1 has diversity in its workforce and encompasses a wide array of job classifications. The organization's current performance pay has the ability to relate to that diversity, while still being functional and reactive.

In the conception phases of the system, PUBORG1 considered the new system a strategic management tool, which would change the organizational paradigm, and assist the organization, both employees and managers, in changing the way business had been done. In addition, the system would allow the organization to be more productive and able to acknowledge the value of individual contribution, accountability, and organizational success (ORG1 Pg1). PUBORG1 spends an inordinate amount of time in the planning phases to ensure that the new system would be fair to all sectors of the organization. In being one of the first organizations to implement a performance-based pay system, they believed that any failure to implement a successful system would be detrimental to the organization and the concept of merit based pay (ORG1 Pg 18). To that end, the organization used a series of study groups and committees, comprised of management, senior executives, and employees to arrive at a workable system that would be accepted by the organization, both by the people and organizational culture (ORG1 Pg 9). PUBORG1 also used the committee concept to arrive at the objectives for the implementation of the system and, the central tenets contained in the system. The objectives; included, among others, the organization's need to recognize value, the ability to place value on the work of employees, the need to compensate workers based on their performance, and the need for increasing productivity were all seen as the motivation for the change. These objectives are important in that they set the ground work for the implementation of the system, and provide a

schematic for its use. While the objectives set the system for implementation, the general tenets of the system actually actuate its functionality. PUBORG1 set as the first tenet, ensuring fairness. This tenet is important in that it reflects a number of the core elements to a successful performance pay system. In discussing fairness, the organization states that treating people fairly is the cornerstone to the system's success (ORG1 Pg 10), and continues by forwarding the idea that the new compensation program ensures that all employees are treated fairly through appropriate practices, guidelines, and policies (ORG1 Pg 10). In this tenet we find a number of ideas communicated in the literature. The concept of equity, both perceived and actual, have a great effect on merit pay systems. The organization realizes that fact, and at the onset of the system, acknowledges it publically. Additionally, the inclusion of the statement that fairness will be reflected in the written policies that govern the system add to its legitimacy. The second tenet, reflecting our culture and values, encompasses more of the ideas presented in the literature. PUBORG1 states, in relation to organizational culture and value, that meeting the needs of their dynamic environment means insuring that their fundamental culture, value, and respect for diversity remains constant, even as the system evolves (ORG1 Pg 11). Here the organization openly expresses that the fundamental culture of the organization, the way the organization and its employees view themselves, will not change. Incumbent in that statement is the understanding that the new system will bring changes, changes that may not all be popular, but changes whose objective is not to fundamentally change the culture, but the way the culture addresses the organizational mission. The third tenet, ensuring fiscal responsibility, once again illuminates one of the most important facets found in the literature and the final factor of the system's ultimate success. The organization states that as a business, it is important to invest in new technologies and in their employees. They continue by espousing the importance of



meeting their fiscal responsibilities, both to the employees and the organizational mission (ORG1 Pg 11). Here the importance of fiscal responsibility is expressed as a general tenet. Normally, the idea is inherent in the concept of implementing a new system, that is, the organizations do not include a statement that they will be financially responsible when initiating a new program, it is understood, but here PUBORG1 finds it necessary to do so. As discussed in the literature, funding can be a large impasse in the management and ultimate success of a merit pay plan, it seems that the organization has addressed that problem, if only as a general concept of the plan.

PUBORG1's performance-based plan is results oriented, that is, all pay increases are linked to individual performance and development, including employee contributions, or outputs, and organizational success (ORG1 Pg17). The plan ties success on the individual level with the overall success of the organization, in fact, there are two components to the plan, within each, there is the possibility of performance awards for the individual employee. The system is driven by the first line supervisors. The employees meet with their supervisors, the measurements and objectives are discussed, and the evaluation is completed, yearly, by the supervisor determining if the agreed upon goals and objectives were met. The system is dependent on the decisions of the first line supervisors in both of the following components. The first component, Organizational Success Increase, is an annual increase, to base salary, that will be awarded to most employees provided PUBORG1 meets its performance goals and the employee maintains an acceptable performance level. The second component, Superior Contribution Increase, provides an additional increase for those employees who make significant contributions to the organization as determined by a structured process, insuring fairness. The increase is awarded to the top 15% of performers based on performance and contribution as determined by management (ORG2 Pg 6). The use of this results driven plan exemplifies the

concepts of measuring employee outputs, utilizing the concepts of teams, and insuring the evaluation process is transparent. In relation to employee outputs, as put forth in the literature, it is important, and easier, to award for performance based on a specific employee contribution, measured at the most basic level. Using a structure, a system, to determine acceptable outputs, and awarding the employees for those outputs, ensures both the perception and actualization of equity. In addition, although not specifically addressed as such, the concept of teams and team work is alluded to in the Organizational Success Component. Here the ideas that the overall success of the group, in this case organization, is important as evidenced by the inclusion of the reward. For the organization to succeed, the members must perform well, insuring their individual outputs add to the increased effectiveness of the organization. Following the best practice explored in the literature of evaluating the team as a team, PUBORG1's evaluation of the individual employee's contribution is amalgamated into a single measure based on team, or organizational, success.

Finally, the issue of perscribing a percentage of the number of employees who will be awarded can result in problems. A merit pay system is limited by financial concern and funding will always be a concern, that is understood, but there is also an inherent problem with limiting the number of employees who can be labeled as high performers. For instance, in the event an organization has 25% of the workforce rated as high performers, how are the decisions on exclusions based? The problem may never come to fruition, but in its eventualization there are two considerations; Will the exclusion be based on a clearly communicated basis, and if not, will that negatively effect the system's integrity?

The plan also incorporates the use of pay banding. In PUBORG1's plan the pay band system involves the use of 12 bands, replacing the General Schedules 15 grade system. Each of

the bands has a salary range of \$9000.00, within entry level to \$43000.00, in the highest level (ORG2 Pg 5). An employee's entry into their particular band is based on their job classification and experience, and their progression from band to band is based on promotional considerations, which include performance, testing, and available vacancies (ORG1 Pg 25). The pay band system eliminates the need for grade increases and quality grade step increases, and instead utilizes the previously examined concepts of performance linked to both organizational success and individual competence. While the use of the pay band system here, and as examined in the literature, will allow flexibility in hiring and retention of top performers, there remains the possibility that high performing employees may be unable to earn any increases. For example, the banding has a 15% cap for awards, it is possible for the same individual to be eliminated from consideration year after year. Additionally, in the event the system is unfunded, there will be no money for any percentage of top performers, and with no automatic step increases, the employees can only hope for yearly increases from the executive branch, usually 2-3%.

PUBORG1's system, in relation to types of rewards, utilizes both base salary increases and one time rewards. The one time rewards are given for isolated performance in certain situations, or in replacement of base salary increases (ORG1 Pg 34). As in the literature, PUBORG1 uses one time payments as a cost managing measure. Intuitively, it is less expensive to give a one time award, then to give a base salary increase that will be realized for years to come. In this, the use of one time awards can be used to substituted for salary increases when needed. The system does not mention non-monetary rewards, or intrinsic rewards, specifically, it instead focuses on the use of monetary compensation. While it could be argued, and has in the literature, that intrinsic rewards have a more far reaching effect on performance, the concepts

of intrinsic rewards in PUBORG1 are found in the conception of its plan, and the organizational culture it perpetuates.

In the conception, planning, and management of its system, PUBORG1 set funding as a high priority, making great efforts to ensure the system continues to be funded during and after implementation. The system uses a management committee that provides advice and counsel to the administration (ORG1 Pg 27). The administration, with the committee's advice, ensures that the organization continues to provide equitable compensation to all employees based on market demands, and is able to meet the continuing challenge of funding for awards payments in both the organizational and superior contributions programs (ORG1 Pg 28). To that end, the administration, on a yearly basis, takes the available information and determines the annual pay increases of all employees based on the two awards programs. The administration examines the percentage of employees expected to receive superior contribution incentives, usually calculated at 15%, and those expected to receive organizational contribution incentives, 85%, then adjusts the percentages based on the available budget. There are two inherent problems with this type of financial management as it relates to the operation of a successful system. While funding is always a problem, most government agencies need more money than they are allotted, in this instance, setting a percentage, as stated earlier, presents the inherent question of equity. If the system is truly performance driven, what of those employees who perform, but are not compensated. Additionally, if 85% of the workforce is being rewarded, the question of system validity is at issue. While it is possible for 85% of workers to warrant awards, it is not probable on a continuing basis. The funding issue is paramount to system sustainability, and PUBORG1 addresses its importance. The major problem is that the organization has no real control over the

issue, and although they understand its importance, in the end, they must compete with other organizations for the same funds.

In an interview with a supervisor for PUBORG1, who will be referred to as SPUBORG1, I clarified the information in the organization's performance-based pay system and garnered information on its functionality from a management perspective. SPUBORG1 stated that in advance of the implementation for the merit pay system, the organization took great efforts in insuring the employees understood the reasoning and need for the change. She stated that the organizational culture facilitated the employee's understanding that a new system was needed and played a large role in the ultimate acceptance of the system (ORG3 Pg1). SPUBORG1 also stated that the employees at first resisted the notion of change, but after the efforts of the organization in communicating the general tenets of the system, were in agreement with its implementation (ORG3 Pg 1). When asked what precipitated the change to the new system, SPUBORG1 advised that the organization felt that the General Schedule had proven to be ineffective, and stated that she agreed, and that it had failed to do poor management. She continued by stating that the use of a performance-based pay scheme was seen as a means to ensure the organization was able to meet the challenges of the future without the restrictions of the General Schedule (ORG3 Pg 1). When asked if the implementation process was lacking in any way, SPUBORG1 stated that the implementation process needed more planning from the management side, advising that human resources, planning, and budgeting should have been intergrated to avoid turf wars (ORG3 Pg 1). When asked her beliefs on the effectiveness of performance-based pay, SPUBORG1 advised that the system's business model, in which the goals are competitive pay, increased productivity, and increased intellectual capital, is useful, but is not always able to be intergrated into the public sector (ORG3 Pg 1). SPUBORG1 went on to

state that her organization did a good job at intergrating the business model, but the system continued to have problems although it had been in place for a decade (ORG3 Pg 1). When asked to expound on the problems, she stated that funding was a big issue, along with the problem of limiting the amount of awards (ORG3 Pg 2). SPUBORG1 explained that the organization is very large and that funds are limited. She stated that the award amounts are small, and that they are insufficient motivation for employees. Additionally, SPUBORG1 stated that the organization has not funded the awards portion of the performance-pay system for the past few years, which has resulted in no performance increases, but only yearly pay raises from the president, approximately 3% per year (ORG3 Pg 2). I then asked about the use of paybands. SPUBORG1 advised that the pay band system worked to give flexibility in hiring new workers. She stated that is was functional to that end, but also advised that the compensation ranges within the bands were not adjusted regularly, and that the promotion from one pay band to the next was limited by available vacancies, which had been scarce (ORG3 Pg 2). When asked about the actual evaluation process, SPUBORG1 informed that the evaluation process was conducted on a quarterly bases, an adjustment from the program's implementation, and she felt it was fair and equitable. She stated that the employees are given their objectives by their managers, they converse concerning them, and there are four meetings throughout the year to confer on individual progress (ORG3 Pg 2). When asked what she would change about the system, SPUBORG1 stated that the number of those employees who can be rated as top performers were limited by the organization, this led to the unpalatable situation of arbitrarily picking the employees to be awarded. She stated that this had negative ramifications on employee morale and trust in the system (ORG3 Pg 2). Additionally, she stated that the lack of funding for the system undermined the idea of performance-based pay, and left the employees questioning the

system (ORG3 Pg2). When asked if she felt the system was functional, SPUBORG1 stated that while certain facets of the system served a significant purpose, the funding issues overshadowed the effectiveness of those elements. She stated that the system, as proposed is a good concept, but that the problem is putting the concept into practice (ORG 3 Pg2).

In an interview with an employee of the organization, referred to as WPUBORG1, I attempted to ascertain his feelings on the implementation and management of the performance-based pay systems. I first asked if he felt the implementation of the new system was handled properly. WPUBORG1 stated that he was hired following the attacks of September 11<sup>th</sup>, and that the organizational culture at the time was unclear. He stated that the massive hiring of personnel following the attacks, and the attacks themselves, had in effect changed the culture. He stated that the advent of the performance-based pay system seemed positive to all the new employees (ORG4 Pg 1). I then asked if he felt the system was fair. WPUBORG1 answered that he felt the system was fair to new hires, but that it became less fair as his career continued. He qualified that by explaining that upon hire, an employee is placed in a pay band depending on job classification, training, and experience. He continued by stating that after the initial hire, the employee is very quickly promoted through the bands to a predetermined point, similar to the General Schedule's journeyman level, and in approximately two years the employee caps out. He stated that once the employee "caps out", there are no guaranteed increases. WPUBORG1 stated the organization's stand is that all raises above that point are budget driven, and he advised that the budget rarely allows for any increases (ORG4 Pg 1). I then asked if he felt the rewards of the system provided proper motivation. He stated that the rewards were insufficient motivation due to the fact that they were rarely awarded, and when awarded, only a few individuals received them. He added that the fact that a limited amount of employees received

awards caused him, and other employees, to question the equity of the system (ORG4 Pg 1). I then asked if the pay band system worked as designed. WPUBORG1 stated that upon hire, employee band placement is done on an arbitrary basis. For example, he advised that individuals he attended training with, who were hired a higher band levels, were obviously less qualified, or able, than he and others. He stated throughout the organization he experienced the problem (ORG4 Pg 1). I then asked if the evaluation process was fairly managed. WPUBORG1 explained that while the managers did evaluate in a fair manner, the basis of the evaluation was unclear. He stated that in his evaluation conferences, little time was spent reviewing his performance, and more time was spent talking about other things. He also stated that employees he had spoken with had experienced the same thing. He ended by stating he felt management did not take the evaluation process serious since increases were not usually rewarded (ORG4 Pg 1).

The question of teamwork and intrinsic rewards was then broached. When asked if the organization promoted team work, WPUBORG1 stated that he very often had to work in two person teams, but the organization never specifically rewarded those teams. Additionally, when asked about intrinsic rewards, he stated that the organization promised a great deal in the way of job satisfaction, self management, and other rewards, but failed to deliver, causing many people to become disgruntled (ORG4 Pg 1). I then asked if the funding issue was a problem for morale. WPUBORG1 stated that the lack of funding effected the entire organization, management and employees, and ultimately made the performance pay system dysfunctional (ORG4 Pg 2). In closing, I asked what he would change about the system. WPUBORG1 stated that the funding issue was important, but that he would also change the probationary period so that the organization had more power to dismiss those who were unable to perform. He stated that the current probationary period is nothing more than a longevity measure. He also advised that



placing step increases within pay bands would be a good change. To that end, he stated the General Schedule was still viable if managed properly (ORG4 Pg 2).

In my examination of PUBORG1, there was large differences between the system schematic and the actual operation. The organization took a good approach at preparing the employees, at implementing a system that fit the culture, and at insuring important issues were addressed. The problem of funding seems to be pervasive in every problem area , and the performance element with its lack of consequences is problematic also. While the SPUBORG1 had positive comments on the evaluaton system and organization's efforts during the planning and implementation phases, she agrees that the performance-based pay plan continues to have problems in the organization. She also states that funding is a major concern, and that it is detrimental to the function of the system. In examining the interview with WPUBORG1, it is clear that the system is not working from the employee's perspective. The most contentios issue being the lack of proper funding for the system. WPUBORG1 also states that the evaluation system is fair, but the evaluations mean nothing. In addition, he stated that limiting award funds leads to limited persons receiving awards, which leads to questions of equity. In examing this case for major themes, funding, or the lack of funding, in effect has diminished the good intentions and indepth planning of the organization, and has limited, if not eliminated, the performance incentive that the system was implmented to promote.

The second organization, PUBORG2 was studied to include a local agency, in this case a county level organization, into my study. The organization is progressive as evidenced by its implementation of a comprehensive performance-based pay plan, and it was the only organization at the county level that I discovered using merit pay. The organization is involved

in the criminal justice system, and it handles the adjudication of criminal offenders within a county.

In giving the reasons for the initiation of performance-based pay, PUBORG2 states that the change to performance based pay was predicated on the belief that salary structures based on automatic pay increases, regardless of employee performance, are detrimental to organizational morale. They also state that the public has a right to demand accountability from public organizations, and that the organization's old pay structure, based on longevity and standard adjustments, did not provide that responsibility (ORG5 Pg1). Here the organization is stating the ideas in the literature on response government, or government that is reactive to the new challenges of the time. It is important that the organization realizes that change is needed for agency advancement, and it is clear the organization feels strongly about fulfilling the public trust.

The concepts of organization culture and equity as they relate to the implementation and acceptance of the new system are then explained by the organization. While PUBORG2 does state that there was considerable resistance on behalf of employees at the onset of the change, in great part due to the change effecting compensation, they also explain that they worked diligently to develop a fair and understandable system. They state that the ability to communicate the tenets of the system to the employees, including the ability to have the unions and employees, buy in, was paramount (ORG5 Pg1). Additionally, PUBORG2 stated that change is never easy, but that the organizational culture, one of mutual trust and reliance, made the transition much easier and more expeditious (ORG5 Pg1).

In these statements, we again find ideas provided in the literature. The new system was implemented once the organization, employees and managers, accepted it. Additionally, in this

case, the unions had to be swayed as well. Without an organizational culture that involved trust and intrinsic motivation, the system may have never been implemented. Also, the organization realizes that equity plays a large part in the success of the new plan. To that end, they took great strides to ensure the system is fair, and that the facts were communicated to, and understood by, the employees.

In relation to the guiding principles of the new system, PUBORG2 explained that it incorporated five basic ideas on which the performance system was based. The first is that each years appraisal stands alone, that is the current year's evaluation is in no way based on previous measurements (ORG5 Pg1). This frees the employee from any lingering effects of pass shortfalls. The second principle, no forced distribution, is important in that there is no limit on how many employees will be awarded increases (ORG5 Pg 1). No forced distribution ensures all the employees have an equal chance at awards. The third principle, the fact that caseload and positions are considered is important because the diversity of assignments within the organization can affect an individual workers output (ORG 5 Pg 1). That is, factors that are out of the control of the individual worker may affect performance, and fairness dictates considerations be made. The fourth principle, performance appraisal is a shared responsibility, is novel. Here the organization states that while the evaluation process is management driven, the individual employee must complete self evaluations to be considered in the evaluation process (ORG5 Pg2). This is a new concept, but I believe the literature would agree, a functional one. The use of self evaluation lends legitimacy to the system. Additionally, it enhances the concepts of system equity, open communication, and overall system validity. The last principle, related to the final overall rating as a composite of individual ratings and level of importance, states that certain skills are more or less important depending on the diversity of duties (ORG5 Pg 2). As

such, the final evaluation weights certain measurements based on those differences in importance. This is a bit convoluted, but the importance lies in the fact that the weighting is used to ensure equity, and that the exact system is clearly communicated to the employees. In these guiding principles there are some obvious similarities with those in the literature. The concepts of insuring equity in the system, the belief that issues outside the control of the employees must be allowed for, and the belief in a system free from ambiguity are all present. Additionally, the concept of self evaluation inherently contains all the positive features examined in this study.

The performance-base pay system uses a type of pay banding system. PUBORG2 uses a four tier system, from Teir I, entry level with little experience, to Teir IV, top tier with many years of experience. Entrance into a tier, or band, is predicated on the employee's years of service and some factor of experience (ORG5 Pg 4), that is, upon hire, with regards to experience, an employee could be placed in an higher band with budget considerations being the paramount determining factor. Once an employee is hired and placed in a band, they must spend a requisite time within that band before they can be promoted (ORG5 Pg 4). In this, there is a performance element in that you must perform to receive pay increases within the band, but there is also a longevity element, in that no matter your performance, you may not be promoted to the next band without requisite time spent in the present band. This is a type of hybrid band system. The use of performance and longevity seem to be counteractive, but controlled movement of employees, as seen in the literature, is a important in the financial management, and overall success, of a merit based pay system. This type of band system was not explored in the literature. In fact, the systems in this study, and the literature, focussed on the elimination of longevity as a measure of competency, and touted its replacement with pure performance measures.

The evaluation element of the system incorporates a rating matrix in which five levels are defined. PUBORG2's system ranges from Greatly Exceeds Standards, at the high end, to Does Not Meet Standards, at the low end (ORG5 Pg 2). The employees are evaluated on three distinct types of skills; fundamental skills, those that all employees should possess to complete the work type, developmental skills, those skills that are expected to improve with experience and responsibility, and Personal/Motivational factors, or those factors that are determined by the employees interest in the work, initiative and creativity, and willingness to take on responsibility (ORG5 Pg 4). These three concepts, easily understandable, are the basis for the evaluation process. The final evaluation is based on a number system, derived from the measures of the two skill sets, with additional narrative support from the motivational section. Additionally, there is consideration of the self evaluation, and the assignment of the appropriate weight to each measure (ORG5 Pg 4). In the end, the employee is rated on a number system from 1-5, anyone employee scoring under a "3" rating is not eligible for an increase. The results are then given to the top supervisor and his assistance to ensure uniformity in the evaluation from manager to manager. This evaluation process takes into account some very important tenets expressed in the literature. First, the process is easy to understand and is managed with transparency in mind, secondly, it incorporates the concept of clear measures, and finally it ensures that the system is equitable from manager to manager, insuring system legitimacy.

In relation to rewards, PUBORG2 states that the usual increase as a result of performance is predicated on an amount of funding agreed upon yearly in collective bargaining, and that employees are awarded a percentage of the midpoint of the salary range within their particular band (ORG5 Pg 5). The system makes no mention of intrinsic rewards, but instead focusses on the monetary increases. In PUBORG2's reward system, there is no prescribe number of

employees who can be awarded increases. All the employees are eligible to receive performance increases. However, there is the inherent problem represented by the term “funding agreed upon”. It seems that in all rewards system, all performance pay systems in the public sector, funding is a caveat of contempt. This system, while it purports to give all employees a opportunity at increases, is actually limited by the amounts it has available. If 90% of the employees earn an increase, the funds must be spread across all. In this, we find the problem of substantial rewards. As stated in the literature, for a reward to have motivational value, it must be effective and substantial in that light.

PUBORG2 did not mention the issue of funding the system. As was stated before, many organizations find the inclusion of budget concerns inherent in the proposal of the new pay system. Yet, as you examine the budget issue closely, it becomes apparent that all organizations, especially those in the public sector, must explore and examine exactly how the new system will deal with funding issues. It is a shortsighted on the part of PUBORG2 to accept that the new system will experience no budgetary problems, even if the old system did not.

After completing a review of the system schematic, I interviewed an individual involved in human resources for the organization, the individual will be referred to as SPUBORG2. After I asked her who initiated the implementation of the performed-based pay scheme and why, she stated that the county had initiated the discussions on the subject of moving to a merit pay system. She also stated that their motivation was to make the agency, and county government, more responsive to the community (ORG6 Pg 1). I then asked SPUBORG2 if the organization had suffered any culture shock as a response to the system change, and she responded that during the planning stages the employees, chief administrator, and consultants worked together to devise a system that was fair and transparent. She also stated that the inclusive nature of the

process limited any surprises and facilitated acceptance by the organization. I then asked if the union was involved in the initial planning. SPUBORG2 stated that the unions did not have much disagreement with the issue, and stated that their evaluation of the county's motivation for the change was positive (ORG6 Pg 1). I then asked what was the biggest factor in the success of the system. SPUBORG2 stated that she believed that the ability of the system to trace employee outputs and competencies was key. Continuing by stating that the ability to marry the outputs, clearly, to a measure, was paramount in the system's success (ORG6 Pg 1). In relation to the evaluation process, I asked if the process was administered fairly and as prescribed. SPUBORG2 explained that the evaluation process is managed as it was planned. She stated that the process is fair, and that supervisors are trained to evaluate employees equitably. She continued by stating that although the system is driven by the first line supervisors, once evaluations are completed, assistants and the chief administrator review them for continuity. Additionally, SPUBORG2 stated that the use of self evaluations promotes the transparency of the system, and that it is a big factor in giving the employees a sense of control in the process. She points to the self evaluation element as integral to the evaluation process (ORG6 Pg 1). I then asked if there had been any modifications to the system since its inception. SPUBORG2 stated that there had been some modifications to the system including a change to a four tier system, the inclusion of a classification system to accompany the number evaluation, and use of computer software to automate the process. SPUBORG2 then expounded on each. She stated that the three tier system was found to be too restrictive and there was a need for a higher band, thus it was implemented for those employees with great experience and particular expertise (ORG6 Pg 1-2). Continuing, SPUBORG2 stated that the classification was incorporated as a byproduct of the

automation, and was used to identify employees from a high level, Achiever, to a low level, Learner/Corrective (ORG6 Pg 1-2).

Finally, she explained the automated system. She stated that the first line supervisor makes subjective determinations on performance, those results are then enter into the computer program as objective responses, the computer assigns the correct weights to each category, and an evaluation rating is determined (ORG6 Pg 2). She stated that the automation had been successful in her determination. I then asked about the concept of proportionate rewards and if she felt the rewards in the system were sufficient. SPUBORG2 stated that the increases have been acceptable to the employees since the implementation of the program, she did however understand the limitations placed on the system by funding issues, and the possibility that budget concerns could become an issue in the future (ORG6 Pg 2). I continued by asking if the orgaization recognized team work. SPUBORG stated that while the organizational culture dictates that employees assist one another regularly, there is no specific program to recognize teamwork, with the only possible exception being as a part of the motivational factor evaluation (ORG6 Pg 2). Finally, I asked it there was one issue that she thought was imporant to the system functionality, and SPUBORG2 stated that the system ensures that outside influences, issues that the employees have no control over, are considered in the evaluaion process. She stated that this factor lends credence to the systems equity (ORG6 Pg 2).

I then interviewed an employee of PUBORG2, who will be refered to as WPUBORG2. The individual has been employed by the organization under the old and new pay systems and was involved in the last bargining agreement with the county. I first asked WPUBORG2 what was his assessment of the old pay plan. He stated that the plan incorporated grade/step increases, was based on longevity and seniority, and that it worked fine. He continued by explaining that the



there was no need for the change, and that the county was a driving force behind it (ORG7 Pg1). I then asked if there had been any culture shock as result of the new system. WPUBORG2 stated that the county offered enhancements in order to ensure the new system was implemented, and that the organization accepted the change with no problems. He went on to state that the employees at the organization all try to do a good job, and that the implementation of the system had little effect on that (ORG7 Pg 1). I then asked if he felt the system was fair. WPUBORG2 stated that the system was unfair in that it does not recognize meritorious efforts. He continued by explaining that system's inability to recognize performance was due to the nature of the work it was measuring, the work is done the same by most employees, and the measurement instrument being ineffective (ORG7 Pg1). I followed by asking if the evaluation system was fairly managed. WPUBORG2 stated that the evaluations were done fairly and the measures were clear, with no favoritism, however, he stated that process was time consuming and that even the self evaluation process was too labor intensive for the increases offered. I then asked what the best and worst attributes of the system were. WPUBORG2 advised that the best attribute was that the system had a distinct and understandable structure, and that it represented a system that was easy to understand (ORG7 Pg 1). Continuing, he stated that the worst attribute was that the system is dysfunctional, explaining that it does not produce increased performance in any way. I followed by asking if others in the organization felt the same way. WPUBORG2 stated that most people in the organization feel that the new system is dysfunctional, and believe that there was no need for it at all. Also, he stated that while he had not suffered adverse actions as a result of the new system, he believed it was a waste of time (ORG7 Pg 2). I then asked if the pay band system was functional. WPUBORG2 stated that the band system does not recognize contributions of individuals within the bands. He stated that the fact that the bands, and

promotion out of the bands is contingent on time, makes the system dysfunctional. He also stated that employees in the lowest band can complete tasks better than those in higher bands, but must wait to be promoted (ORG7 Pg 2). I continued by asking WPUBORG2 what he would change in the system. He stated that he would increase the compensation flexibility within the pay bands and increase the reward amounts, explaining that the current rewards and marginal increases in compensation are not motivating factors (ORG7 Pg 1). I then asked specifically about funding levels and their effect on the system. WPUBORG2 stated that the funding issue has always been a problem. He advised that it affects all members of the organization, and that it forces the system to be funded at very low levels. He continued by stating that the low funding levels result in low increases and rewards, and makes the whole system suspect (ORG7 Pg 2). WPUBORG2 closed by stating that the system, in practice, operates as designed, but in actual outcomes, it does not promote nor recognize employee performance (ORG7 Pg 2).

In the study of PUBORG2, the initial examination of the system gives a positive indication. From the planning, implementation, and general tenets, the organization seems to have implemented a performance pay system free from the award limitations, that promotes clear performance, that incorporates progressive ideas, and that has an inclusive manner. The organization seems to give a clear representation of the need for the change, has been able to win union support, and is making modifications as the system evolves. In looking at the system from all points represented by the literature, it should function well. The only contentious issue in the entire system is that of restricted funds. I point it out due to the fact that I recognized it in the analysis.

As the interview with SPUBORG2 begins, it seems that she to is positive concerning the entire system. She begins by stating that the organization made great efforts to include

employees in the planning process, she states that the evaluation system is fairly administered, and that self evaluation, a progressive concept, is considered a central part. SPUBORG2 also states that there is no forced distribution in the system, which makes everyone eligible for increases. She also states that the organization recognizes that there are factors beyond the control of employees, and considers those factors in the evaluation process. In the end, SPUBORG2 gives a positive appraisal of the system, and even when pressed on the issue of funding, states that funding has not been an problem. If the analysis stopped here, we would have a blueprint for the functional performance-based pay plan, but it does not.

Next I interviewed WPUBORG2, an employee under the old and new systems. WPUBORG2 gave a much different appraisal from those presented in the schematic and by SPUBORG2. A cynic would say that WPUBORG2 probably has an agenda, and is thus giving answers to further that agenda. While I understand that possibility, the answers given by WPUBORG2 seem to follow the same threads that are present in the discussion in PUBORG1. In giving his opinions on the pay system, WPUBORG2 states that funding is the most compelling problem. He states that due to the lack of funding, the system has become dysfunctional. He qualifies that in saying that the system offers little, if no, rewards, and that budget amounts for performance increases are not motivational. He also says that the use of the pay band system, including the use longevity as the requisite for promotion, and the current problem of employee performance in lower pay band exceeding the performance of employees in higher pay bands, brings the entire system into question. I find some intuitive truths in these statements.

First, the possible funding problems were apparent when analyzing the system schematic. If a certain amount of funding is agreed upon before the evaluations are completed, there is room

for these types of problems. Additionally, I also alluded to the possible incongruity of using longevity and performance based evaluation within the pay band system. It seems that the WPUBORG2's comments lend merit to my observations. In addition, it is not very often that a schematic and operational system fit so perfectly, as SPUBORG2 would represent. There is always some element, some part of a system, that simply does not function as planned. Once again, as in the other organizations, the contentious issue of funding represents this element..

After having examined the Department of Defense, PUBORG1, and PUBORG2, I will now begin an analysis of the Department of Homeland Security (DHS), and their proposed Max HR system. This analysis will take the same form as the examination of the DOD system, as it is in the process of implementation and has no basis for study in the functional respect. However, one change in the approach is to include data from the interview of a supervisor who is currently trained and being evaluated under the system.

The new performance-based pay system is proposed to positively influence the human resource function in the Department of Homeland Security. The change to the performance-based, Max HR system, was precipitated by a number of factors: the continued drive by the Bush administration to incorporate a merit based pay system into the government, the creation of the new Department of Homeland Security following the September 11<sup>th</sup> attacks, with its amalgam of agencies, the need for a management system to address the diversity, and the preceived failure of the General Schedule system. These are all factors that have fueled the performance-based pay issue at DHS.

In order to address these issues and to facilitate implementation of the new system, the department engaged in a number of initiatives. During the Max HR design process, DHS utilized inclusive measures. The organization incorporated employee committees, workgroups,

and input from stakeholders, including management and employees from all levels, to arrive at a what they believe is a functional system ( USDHS Pg 5274). Additionally, once the main tenets of the system were constructed, DHS engaged in a series of “Meet and Confer” sessions, in which the system was presented to additional stakeholders, including union representatives from the four largest labor groups, in an effort to illuminate any problems in the system (USDHS Pg 5275). In the end, DHS took the information provided by the employees and other stakeholders and made adjustments to the system before the final regulations were enacted. Here we see an example of the principle of system legitimacy. The literature espoused the need for a system to be acceptable to the employees and culture. In that light, DHS used inclusion to ensure that their new system was influenced by a large number of stakeholders leading to the system’s validity.

In relation to the reasons for implementing Max HR in replacement of the General Schedule, DHS states that the new system was needed to change the culture of entitlement, represented by the the General Schedule, to an environment where employees can be recognized and rewarded for their contributions, and where the employees understand what is expected of them (Max HR Fact Pg 1). DHS also believes the performance-based system will facilitate higher performance by implementing skill based training and development opportunities, and will create a culture of performance driven progress (Max HR Fact Pg1). Additionally, DHS explains that the new system is needed to assure the agencies continued ability to attract, retain, and reward a workforce that is capable of meeting critical mission requirements (USDHS Pg 5273). This is based on the belief that for government to be competitive in recruiting high quality employees, they must have flexibility in hiring and setting salaries as in the private sector.

Here, DHS incorporates familiar concepts as seen in the literature and in other organizations. The idea that government agencies include a measure of performance in replacement of longevity has been discussed as an important element in improving organizational efficiency. In addition, the idea that government employees should receive pay on par with the private sector is a driving concept in merit pay. The inclusion of the training and development opportunities exemplifies the notion of intrinsic rewards being important motivational factors.

The DHS utilized general tenets that they believe are integral to the success of the system. These tenets, which encompass both organizational objectives and concepts on which the new system will be based, communicate principles that will determine how Max HR will be implemented and managed. In the Max HR Employee Fact Sheet, the first tenet, “Setting Clear Expectations,” refers to management’s ability to communicate, clearly, the expectations and performance standards (Pg 1). In this tenet, the concept of clearly stated and understood expectations and measures of evaluation are apparent. The literature acknowledges transparency as having a significant effect on employee acceptance and trust of a new system.

The second tenet, that the system will accurately reflect individual contributions (Pg 1), incorporates the idea that the individual will be measured on his or her performance and role in accomplishing organizational goals. Inherent in this tenet is that the employee will also be accountable for failing to perform properly. Again, the concepts mesh with those in the literature. Any performance-based pay system must identify the employees who perform at a high level. This is the identifying precept of the system. But equally, if not more important, the system must also identify the poor performers and ensure their deficiencies are addressed.

The third tenet, which is to promote a continuous learning environment and create new opportunities and leadership (Pg 1), exhibits the concept of intrinsic rewards as discussed in the

literature. Intrinsic rewards are reported as a much more far reaching motivational factor than monetary compensation. That idea is understood by DHS, and its inclusion as a general tenet shows its importance. The fourth and fifth tenets address the organizational culture of DHS, and include building a culture of organizational trust, facilitating communication and feedback, and utilizing coaching to enhance performance.

As discussed in case studies and literature, the actual and perceived equity of a merit pay system is important. That equity, perpetuated by trust between managers, employees, and ultimately the organization, is the foundation for a performance-pay system's acceptance and ultimate success. In addition, the ideas of communication, top down and bottom up, are important as they relate to communication, but are also important as the system evolves and modifications need to be implemented. Communication is the key to an open and transparent system, and in the inclusion of this concept, DHS is insuring that the organization continues to incorporate open communication during implementation and as the system changes.

Finally, the concept of coaching (Pg 1), which was not addressed in the literature, is, I feel, a valuable addition. As discussed in the literature, and in case studies, the correction of poor performing employees is an important function of any human resource system, DHS accepts that idea and incorporates it into Max HR.

DHS also includes the use of pay bands within Max HR. The use of pay bands allows the organization the ability to hire new employees and compensate them at levels that more closely mirror the rates in the private sector (USDHS Pg 5278). This flexibility is seen as a central reason for the implementation of the new system. Max HR is set up with four broad-pay bands, which are actually four levels (Recommendations Pg.1). Within each level or band, there is a maximum and minimum compensation rate, which can represent a difference of twenty thousand

dollars or more. In this pay band system, DHS incorporates the ideas of a flexible pay scheme, involving the ability of the agency to hire personnel at competitive salaries, and retain those employees who are attracted to the private sector. Additionally, the system functions to place employees in the proper band, contingent on market demand and experience, and ensure they are compensated at the correct level. DHS represents the use of pay bands as completely functional, with no negative attributes. In examining the literature, this is a simplistic view of the system, and pay bands do come with inherent risks, both for the organization and the employees. Pay bands must be intensely managed for the financial viability of the organization and continued validity of the system, and the possibility that the band system will inhibit employee progression, through by extraneous causes, is always a possibility.

The evaluation process within Max HR is centered on the concept that there will be a direct line of sight between an employee's goals and the department's objectives, and that employee goals may be adjusted depending on organizational needs (Max HR Tutorial). Here, as in the DOD's system, we find the idea that mission is the most important issue. This issue is only discussed in the NSPS and Max HR systems. While it seems intuitive that the concept of "mission first" would be functional in a military setting, at DHS it seems out of place and counter to building a system that works to improve and evaluate employee performance.

At the beginning of an evaluation period, the employee is responsible for the completion of self appointed goals. This is completed as an element of the structured system, and gives the employee input into the process. After completing the personal goals, the employee meets with a supervisor to discuss those goals and arrives at measurement goals for the evaluation. These ultimate goals are designed with the current ability and capabilities of the particular employee in mind (Max Hr Tutorial). Once the goals for the employee are set, the employee then works to



meet all the performance standards. At the midpoint of the evaluation period, a second meeting is held where the employee's progress is discussed. Finally, at the completion of the evaluation period, a final meeting, in which the employee completes a self evaluation, is held (Max HR Tutorial). In that meeting, the supervisor, using information from the employee's self evaluation and their own appraisal of the employee, determines if the employee was successful in completing the assigned goals (Max HR tutorial). This evaluation system contains the general ideas presented in the literature, but also adds a progressive element. The use of the initial meeting to discuss the evaluation goals and the evaluation process lends credence to the entire system.

Likewise, the midpoint meeting allows for clarification and measurement of the employees progression. This is important to the legitimacy of the system, and also works to make the evaluation process clear and transparent. DHS makes it clear that the system will be fair, and that all information as to performance will be available to the employee, yet the organizations also includes the concept of self appointed goals and self evaluation. In the examination of PUBPRG2, I discussed the issue of self evaluation, stating that it gave the employee a sense of control within the evaluation system. In this case that is true also, but the inclusion of self appointed goals is another valuable addition. By allowing the employee to have some self determination, the organization accomplishes two things; First it allows the supervisor to understand what the employee believes is important, and secondly it gives the supervisor a starting point from which to formulate proper goals and measurements for each employee.

Aside from the "mission first" issue, there is another, more problematic issue, within the system. The fact that the supervisor sets a subjective set of goals for each employee intuitively means that the employees are not being judged in a uniform manner. That is, the possibility of a

high performer having to meet higher requirement than a low performer is inherent in the system. While I understand that an organization has a diverse workforce, with different strengths and weaknesses, the performance-based pay system must pay the performers. The measure is unfair to the employees the system is purported to reward, and as we have seen in the literature, the measurement instrument must be fair to everyone.

In regards to rewards and funding, Max HR puts no forced distribution in the system. As discussed earlier, this means that all employees are eligible to receive a performance increase or reward, but a major problem with the system is that it does not address what the awards payments or increases will be. The organization touts the idea that it will reward high performing individuals, stating the higher the performance, the higher the pay (USDHS Pg 5277), but then fails to give any indication of what the increases or awards might be.

In addition, there is only a cursory discussion concerning the initial cost of the system, and how it will be funded in the future. DHS states that the initial cost of implementation will be met by the training budget, and if it is needed, a shift in funds from other programs (USDHS Pg 5317). The organization continues by using an elaborate series of regulations, most of which are indecipherable, to explain what the payments will be, and where the funds will come from (USDHS Pg 5318-5336). This is the most troubling element of the system. A viable system must explain how funding will be completed, both for implementation and continued management, and as stated throughout the literature, must communicate that to the stakeholders. Max HR fails to provide that information.

The DHS manager I interviewed has been employed by a component of DHS for the past two decades, and has operated under the General Schedule for the majority of his employment. Recently he and other managers attended training on the management of Max HR and were

placed, as an initial group, on the Max HR program. He will be referred to SDHS. I first asked SDHS if he felt that there were any problems with the General Schedule. He stated that the General Schedule was functional, but that in practice the managers had failed to implement the needed sections of the adverse job actions. He continued by stating that group supervisors, as a whole, were poor at implementing the General Schedule, and that given supervisors who were not “frightened” of their subordinates, the system could operate properly. I then asked what SDHS thought of the organization’s preparation for the implementation of Max HR. He stated that the organization had done little to prepare the workers for the change. He stated that there was no thought of organizational culture, and that on the contrary, the organization not only implemented the change in pay plans, but at the same time, significantly changed the job responsibilities within the department. He stated it was too much change for many to handle and resulted in mass retirements and resignations.

When asked if the Max HR system was fair, SDHS stated that the system was unfair because after the meetings, goals, and evaluations, the first line supervisors had too much input and no one to answer to. He continued by explaining that the issue of personal feelings, the buddy system, would hinder the equity of the system. In terms of the fairness in the evaluation process within Max HR, SDHS stated that the evaluation process is unclear, and remains unclear even after the training he had just attended. He stated that the fact that managers must lower goals for less capable employees brings the system’s fairness into question. He also explained that as a manager, he must set subjective goals based on the employee’s ability. He then stated that it was not fair to judge individuals with different abilities the same, but in the end stated that judging on performance should indicate the use of a single measure of that performance.

In relation to his recent training, I asked SDHS if it prepared him to effectively manage the system. He stated that he had not been trained properly, but felt that he would work it out as he began to implement the system. I then asked if the evaluation system, as designed, tied rewards to performance. SDHS stated that he felt the system was good at tying the two together, and that the system was also very open to communication and information transfer. He also stated the major problem lies in that the system fails to recognize high performers due to the differential measurements already discussed. In relation to his position as a new employee under the system, I asked SDHS if he had his initial meeting with his supervisor. He stated that he had received an email from his supervisor requesting his self initiated goals, but that he had no meeting to discuss his performance measures. He then stated he did not know when his evaluation period had started. I then asked SDHS about the role of managers in the Max HR system. He stated that there is nothing in Max HR that will make the managers implement it any more successfully than the General Schedule. He continued by explaining that the supervisors were so afraid of adverse work actions that the majority would find a way to give all the employees the highest rating possible. Finally, I asked SDHS about the funding of Max HR. He stated that at his recent training, the group had asked the trainer, a contractor, about the possibility of the system going unfunded, he stated the contractor explained that was an absurd notion. SDHS continued by stating that he believes that the funding issue will ultimately make the system undesirable for the employees. He concluded by stating that in his opinion, all changes in compensation plans benefit the organization more than the employees.

The data from the documents were used to determine the organizational perspective on performance-based pay systems. Through my analysis, it became clear that certain patterns, containing the concepts of organizational change, system function, and system dysfunction were

present in all the study's merit pay systems. These concepts gave a clear indication of how successful the pay plan had been and the prospect for its continued viability.

### **Organizational Change**

Organizational change represents an amalgamation of motivations, expressed by all study organizations, for the change to performance-based pay. In addition, it contains the concepts and practices that the organizations believe to be central to a functional transition.

The organizations espouse that the change from the grade/step system, represented by the General Schedule, is necessary for the advent of performance-based pay. The two systems are incongruent, and for performance to be recognized appropriately, the organizations believe that a new system of pay and management must be implemented. The organizations also believe that the measure of an employee's success should not be his or her ability to remain at a job, but should instead be based on their performance of the job. They state that the use of longevity as a performance measure is antiquated, and further explain that the use of performance measures and incentives are needed to change work environments to reflect the organizational values of performance.

The organizations also express that accountability is a major factor for the change, forwarding the idea that public organizations, and public workers, should be accountable to the public in some measurable way. In addition, they state that with that accountability, the worker should have the ability to have his or her individual contributions recognized and awarded by the people, through the organization. The use of performance pay increases, and awarding one time bonuses, is seen as a functional way to reward the inputs of employees, while also providing a way to show that the individual is valued for their contributions to the organization's success.

The organizations feel that the concept of organizational culture is important when considering impending change. They state that at the onset of a new pay system, during the implementation stage, it is paramount that the system is clearly communicated to the stakeholders, including employees and managers. They state that the communication must be reciprocal in nature, and that it must be opened to reflect the ideals that the organization and the employees hold as important. They also state that organizational culture must remain a consideration as the work environment evolves, and the system implements changes. Here the organizations feel that it is equally important to ensure that any changes are congruent with the culture.

### **System Function**

System function incorporates the attributes that the organizations have identified as affecting the functionality of all the studied performance-based systems. The organizations provided that these concepts, when incorporated, determine the ultimate success of the system, and its overall sustainability.

The organizations state that primarily, a merit pay system needs to be inherently equitable. That is, that all facets of the system must be conceived in a manner that promotes openness and trust, and that facilitates the concept of trust throughout the organization. They explain that the concept of trust is a product of having open communication that flows from the top of the organization down and from the bottom up. They also explain that this communication is the foundation for the continued exchange of ideas that lead to feedback from diverse groups within the organization. With the input, employees and managers feel they have a stake in the system, and will continue to work at enhancing it.

The organizations also state that using clearly expressed goals, goals that are easily understood by management and employees and are communicated to the organization, via the system, are the key to tying performance to rewards. They explain that a functional performance-based pay system must facilitate employee understanding as to what he or she is expected to accomplish, and what the rewards will be upon reaching their goals. The organizations also point to the evaluation process as an important element in accurately matching achieved goals with rewards. They state that the evaluation process must maintain its transparency. To that end, the organizations feel that evaluation systems must be free from elaborate matrixes that force the managers to judge on criteria that is hard to define and difficult to measure. They suggest instead, a system that is open to all employees, that is explainable in a short description, and that in the end, works to promote the attainment of awards, and not be an impediment to them.

The utilization of pay bands, as an element of performance-based pay, was expressed by the organizations as integral to the operation of such systems. The organizations explained that pay banding allows them flexibility in relation to pay issues, and enables them to recruit employees from the private sector, resulting in the most experienced and knowledgeable employee pools. They explained that pay bands are the foundation of performance-based pay, and that for the system to operate effectively it must have the ability to reward employees, within preset limits, using a structure that incorporates the concept of rewards and incentives. The organizations believe that pay banding fits the function perfectly.

### **System Dysfunction**

System dysfunction includes the problematic areas found in the performance-based systems of the study. In my analysis two were discovered. While one of the issues is the result

of the systems themselves, the other is the result of an extraneous variable that affects the systems.

The organizations all state that they use first line supervisors to drive their performance-based systems. They state that the supervisors are responsible for meeting with the employees, in most cases assigning goals, and are the ultimate evaluator in determining if the employee's performance is acceptable. The organizations also stated that after their initial training, the supervisors are free to run the system as instructed, with the only caveat being that upon adverse job action, or bringing a complaint against an employee, a higher authority reviews the supervisor's decision. In this, the inherent problem of the human factor is apparent. The human factor refers to behavior of human beings as they interact with one another. The human factor is implicit in the function of all systems, but more so in performance-based pay systems. Performance-based pay is contingent on the belief that an employee will be judged fairly on the issue of his or her performance only. The organizations, by allowing the first line supervisors to operate with only marginal checks, increase the possibility that the managers will award increases on factors other than performance. Additionally, as seen in the management of the General Schedule, supervisors are not likely to initiate adverse job actions due to the necessity of their decisions being reviewed, and to that end, most managers are lenient in the way they evaluate employees due to the possibility that poor evaluations could result in a troublesome work environment.

The issue of funding was a major concern to all of the organizations. In examining the most problematic issues of funding, the organizations stated that the overall lack of funding caused the entire performance-based pay system to be questioned and resulted in employees losing faith in the system and becoming discontented. This lack of funding results from a



number of practices; projecting rewards, projecting the percentage of employees who will receive rewards, prescribing the amount of awards that will be given, and the inability of the organization to control its own funding. In relation to projected awards, the organizations often use an informed guess, based on the information they have available at the time, to decide the amount of funding they will need for incentive bonuses. The problem is that once the money is budgeted, the estimate may not, and often does not, cover the actual expense. The result is that the employees who have performed and met their goals go unrewarded. Relative to projecting awards based on a percentage, the organization determines, by estimate, what percentage of the employees will perform at levels that will result in payments, say 15%, and the organization then budgets for an amount that represents the percentage. The problem occurs if the estimate is low. In that event, again, those workers who were given goals to attain and performed well enough to reach them, are denied their due payments. Additionally, some organizations engage in placing limits on the number of employees that can receive incentive payments or awards. This is problematic, in that, if more than the prescribed numbers of employees qualify for payments, the organization will simply refuse to compensate them although they attained the goals that were set. In other systems, there are no limits placed on awarding incentives, but the organizations still express funding problems with those systems. The organizations state that systems which do not use forced distribution often suffer from having inadequate funds to pay all the high performers. That is, that in a system where all employees are capable of earning incentive payments based on their performance, the system is not prepared or able to make payments to everyone. In that event, the managers either pay individuals based on some other factor, possibly rotating payments from performer to performer over time, or spread the incentives payments across all the employees with the results of the incentives becoming a non-motivational factor.

The organizations also expressed that their inability to control their funding was of paramount importance. They stated that although their performance-based pay systems were fair, the lack of funding, or in some instances non-funding, of the system proved to render the system dysfunctional.

The data from the interviews was then used to determine the perspectives of the managers and workers as to their conclusions on the function of the system that they worked within.

### **Management Perspective**

Management perspective encompasses the opinions and beliefs of the human resource managers as to function of their particular merit pay system. It includes the manager's feelings on four general concepts; system equity, system function, system implementation, and also includes additional items that the managers felt were important.

The managers feel that the systems are fair in that they use evaluation elements that are clear and tie performance to rewards in a meaningful way. They also stated that the systems operated in an open manner, and that this ensured their ability to remain equitable.

In relation to the function of the systems, the managers stated that the systems have sound theoretical rational, but that it was difficult, in some cases, to transfer that theory into functional practice. They also stated that the problem of funding is always a concern, and that in many cases funding issues; the lack of funding or no funding at all, has rendered the entire system dysfunctional. The managers stated that funding contributes to the problems of low motivation for employees when they understand that no matter their performance, they may not be paid what has been promised due to funding.

Relative to system implementation, the managers feel that the systems were implemented properly, with attention to organizational culture and sufficient communication. They explain

that the organizations could have engaged in better planning in some cases, but that the overall estimation of the process was positive.

The managers then discussed some issues that they felt were important. They stated that systems that utilize self-evaluations, where the employees rate their own performance, and which account for factors outside the control of employees, as in the involvement of other organizations in the completion of goals, allow for a more thorough and fair evaluation. The managers also stated that funding issues undermine the system's ability to function and that the inability to pay employees after they have performed is unfair and cause the entire system to be in question.

### **Employee Perspective**

Employee perspective incorporates the opinions and beliefs of the employees as to function of their particular merit pay system. It includes the employee's feelings on four general concepts; system equity, system function, system implementation, and also includes additional items that they felt were important.

The employees stated that the systems were not fair in that they provided additional payments for individuals that were not available to others. This was exemplified by the system offering large increases to new hires, but after those employees reached a level of compensation their pay was no longer increased due to budget issues. The employees did state that the evaluation systems were managed in a fair fashion, they were open and easy to understand, but that the system's one inequity made it unfair for all involved.

Relative to system's function, the employees stated that the systems did not affect the performance of employees due to the lack of funding. They stated that the systems provided incentives and clearly communicated goals, but failed to pay them meaningful rewards. This was due to the system being under funded or not funded at all. They stated that the issue of funding

contributed to the feeling of apathy in relation to the performance system and the possibility of rewards, and that in the end, the performance-based pay systems were seen as non-motivational issues. The employees also explained that once the payments were withheld, the system loss all credibility.

In relation to system implementation, the employees felt that the implementation process was handled well by management, but that in the future, more attention should be paid to the timing of that implementation. Finally, the employees stated that the systems are sound in what they propose to accomplish, but the problems occur when the systems are put into practice. They stated that the organization's lack of control in the funding issue undermines the foundation of the performance-based system.

### **Max HR Continuity Concerns**

Continuity concerns examines the differences in the organizational plan for Max HR and how the plan is being managed from the perspective of a manager, both covered by and managing, the new system.

In the initial study of the implementation of Max HR, it appeared that it was inclusive and effective, and that DHS had taken great strides to ensure the system was accepted by the employees. SDHS stated, to the contrary, that DHS had not included anyone he knew of in the process, and that even if he had been included, the system had been implemented at the worst time possible. He stated that along with the implementation of the new pay plan, the organization had changed the responsibilities of many organizations. He stated that the result was mass retirements and resignations.

In explaining the need for the change to Max HR, DHS cited the General Schedule and its outdated management structure, SDHS stated that the General Schedule was still functional,

and he felt that the managers, the same managers that were going to manage Max HR, had failed in enforcing the employee discipline procedures. SDHS also stated that the same managers, who are frightened to initiate negative work actions, would find a way to give the highest evaluations they could under Max HR. Max HR espouses to evaluate performance in a fair and equitable manner. When asked his opinion, SDHS stated that the system is unfair due to the fact that the first line supervisors have too much discretion without much oversight. He stated that this would lead to individuals receiving evaluations based on factors other than performance. SDHS also stated that the evaluation process was unclear even after he had been trained. While he stated that the system was effective at tying performance to rewards and offered open communication, he also advised that in the end, the use of different measures for employees with different capabilities was inequitable and did not properly measure performance.

DHS stated that the managers would be trained properly in order to manage the system effectively. SDHS stated that he had not been trained properly, in fact, he stated he had no idea how the system was going to function. He continued by explaining that the training was insufficient to prepare him to manage Max HR, but he felt he would work it out as he went. I then asked SDHS about his experience as new member of Max HR, he stated that he had not had his initial meeting with his supervisor, but they had exchanged e-mails on the subject. SDHS then stated that he did not know when his evaluation period had started. In relation to funding, SDHS stated that he felt that was the one issue that would render the system undesirable to employees. He stated that the system would eventually be unfunded, and no increases would be awarded.

The issues explored here illuminate some of the same concerns stated at the start of this project, but include additional issues. The belief that the system would be unfair, and that it would be ineffective in measuring the performance of employees in a proper manner is obvious.

The system's inherent inequity in using different measures and the funding concerns were not an issue I considered, and I could not have imagined that the training deficiencies and the functioning of the system could be so poor. Additionally, I would not have believed that the same problems that plagued the General Schedule may be present in Max HR.

I will now take the information learned from the results of the study and the issues explored in the continuity concerns and apply them to a discussion on the Max HR system, in terms of its positive and negative attributes.

### **Function in the System**

In examining Max HR, the system incorporates some very functional and progressive ideas. It is important to discuss the positive points contained in the system in an effort to remain impartial, but also for the purpose of producing a proper appraisal.

The use of self appointed goals within the evaluation element is a progressive concept incorporated in Max HR. The concept allows the employees to communicate the goals and issues that they feel are important. They communicate their goals to their supervisors at the onset of the evaluation process. With that, the supervisor can then customize measures, for better or worse, to meet the interests of the individual. This, as found in this study, allows the employees a feeling of control and adds to the legitimacy of the system. Max HR also incorporates the use of employee self evaluation. This concept allows the employee the opportunity to examine their performance over the evaluation period and grade themselves. As with self goals, this gives the employee a sense of control, but this concept also ensures the employee has some self determination. Max HR accomplishes two very important things through the utilization of these concepts: First it allows the supervisor to understand what the employee

believes they have accomplished, and secondly it gives the supervisor a starting point from which to formulate proper goals and measurements for each employee.

### **Dysfunction in the System**

The Max HR system incorporates elements that have been proven, both in the literature and in this study, to be detrimental to the function of a performance-based pay system. These issues must be discussed in an effort to facilitate an understanding of how they will negatively effect the success of the system.

The analysis of the documents, along with the information gained from the management and employee perspectives, has shown that for a system to be functional, it has to be inherently equitable. That is, it has to be fair to all the employees that work within it. Additionally, the system also must link performance to rewards in a significant way and provide an evaluation process that is understandable. The evaluation element of Max HR fails to incorporate any of these concepts. On the contrary, the system's use of different measures for different employees, based on their individual abilities, measures an abstract concept. For the system to truly measure performance, it is paramount that measures be constant across the organization, or at least within agencies or work groups. Max HR provides no such continuity. The practice of using different measures, while espousing to be fair to the diversity within the organization, actually becomes unfair as a result. It measures something other than performance, it measures a measure of performance. The system actually lowers the standard of performance by allowing the managers to lower their expectations to fit the levels of the diverse workers. For the system to measure and award incentives based on this basis is patently unfair, and will ultimately render the system dysfunctional.

Max HR also includes the problematic element of the supervisors having sole responsibility for managing the system. In this study, the document analysis showed that organizations are concerned with the issue of first line supervisors having a high level of evaluative discretion. The analysis showed that the factor of human interaction can effect the managers ability to remain detached and can result in the system being plagued by inaction. Max HR ignores this idea and gives its managers sole responsibility of assessing employee goals, evaluating the employees, and subjectively assigning them a performance rating. The managers have little oversight, and there is no grievance procedures in place.

Finally, the issue of funding is also problematic for Max HR. The document analysis showed that in relation to funding, the organizations in this study believed it was their biggest concern. Additionally, the managers and employees also pointed to funding issues as rendering their performance-based pay systems dysfunctional. Max HR makes no effort to explain where their funding will come from. While the General Schedule has its well documented problems, it never caused a high performing employee to go without a pay increase, on the contrary, it allowed the poor performers to be paid as well. The result of Max HR going unfunded, or under funded, will be that no employees, or very few, will receive pay increases. While it is not certain that the system will experience budget problems, this study has shown that to be the exception in government and not the rule. Max HR is being implemented with the promise that it will pay high performers for their contributions to the organizations, in reality the system is lowering the performance measures of some, while setting them higher for others, and in the end, will not pay either.



## **Conclusion**

The of utilization of performance-based pay within the government has been proven to be problematic at best. In examining the principles of performance-based pay and the attributes of functional systems, and after conducting my own study of public organizations that utilize performance-based pay, it is clear that there are central tenets that must be present for these systems to function and to remain viable. Max HR is currently being implemented by the Department of Homeland Security with inherent problems that violate three of these tenets. The system is patently unfair in its evaluation process by measuring worker performance on a variable scale related to individual ability. The system's management element provides an inordinate amount of discretion to the first line supervisors, which has been proven to result in evaluations based on factors other than performance, and the system's funding element is non-existent, which has led to catastrophic results when merit pay systems are unfunded or under funded. If Max HR is fully implemented with these fundamental problems, the organization, and the employees that work within it, may suffer yet another crisis comparable to the September 11th attacks, but it will be one that could have been avoided.

## **Recommendations**

At the beginning of this study, I felt that the most important factor inhibiting the implementation of performance-based pay would be the system's inability to fairly evaluate employees in the public sector. I believed that the objective, quantifiable measures, used in the private sector could not possibly translate into the public sector. As the study progressed, as I completed the research, I found that the measurement issue was not contentious, but that funding was the greatest concern.

Throughout the study, the issue that seemed to be in every discussion was the lack of funding, or the lack of funding control by the organizations. The funding problem is inherent in government. The problem is that organizations can implement new systems and initiatives, but they are only as functional as Congress makes them, through its control of funding. In the organizations and systems in this study, the managers and employees agree that the negative impact of funding is ubiquitous. This is an issue that must be explored in future research. It must be examined from the perspective of how the funding can be changed to more effectively contribute to the goals of pay-for performance systems and the values of elected officials in their funding decisions.

The unanimous agreement, both of the managers and organizations in this study that the General Schedule is patently ineffective must be explored as well. It is a system that has been effective for a long time, despite the fact that it has been mis-managed. The system must be studied to determine if its failures are a result of the system being antiquated, mis-managed, or in need of modifications. This type of study may lend credence to the need for performance-based pay, but it is necessary to determine if the system, already in place, can be made viable once again.

Additionally, throughout the literature, the use of pay bands is expressed in a positive light, although the reporting, as discussed, may be skewed. In this study, pay banding has proven to be problematic in that funding constraints tend to limit the increases within the bands, while vacancy shortages limit the number of individuals promoted from band to band. The further study of pay banding is essential to determine its overall function as the structure for performance-based pay systems. While it is clear that the systems needs some type of structure,

an empirical study of the effectiveness of the banding system would be valuable both to the management and function of performance-based schemes in the future.

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Jerry C. Templet Jr is a life long resident of New Orleans. He earned his B.A. from Loyola University, New Orleans, in 1998. He is a Special Agent with the U.S. Government, and is dedicated to the pursuit of knowledge.