Current Issues in Executive Level Public Compensation

An Honors Thesis (HONRS 499)

by

Dawn M. Huffman

Dr. Raymond Scheele

Ball State University

Muncie, Indiana

May 2001

Graduation Date: May 5, 2001
Abstract

The purpose of this thesis study is to reveal the fundamental problems of the current compensation structures used to determine executive level pay in public personnel. The first chapter will begin by discussing the history of the current structures in place for evaluating public compensation. The second chapter will delve into an example of a structure used to evaluate compensation at the executive level in order to better describe the structures in place. The third and fourth chapters will discuss the positive and negative aspects of the current compensation programs frequently used for the public sector, and the fifth chapter will then discuss compensation programs in the private sector. Chapter six will compare private sector initiatives with what could be used in the public sector. Finally, this thesis will make suggestions for possible avenues public sector compensation plans can strive towards to eliminate the present issues that are hurting their structures.

Acknowledgments

I would like to extend my deepest thanks to Dr. Raymond Scheele, my thesis advisor, for his guidance through the long process that has been my thesis. He has provided me with support through tons of literature to examine, his constructive comments, and his patience as I was getting closer and closer to graduation without having completed this. I would also like to thank Doc and his partner, R. Kent Irwin, for employing me at their consulting firm, otherwise I would not had this opportunity, nor would I have had any interest in this topic. Finally, I would like to thank my loved ones for their encouragement and computer usage as I worked to complete this thesis.
Table of Contents

Abstract .......................................................................................................................... 1
Acknowledgments........................................................................................................... 1
Table of Contents ........................................................................................................... 2
I. History of Public Compensation .................................................................................. 3
   General Schedule....................................................................................................... 3
   Federal Factor Evaluation System .......................................................................... 5
II. Oliver System for Job Evaluation ........................................................................... 6
   History of Oliver System........................................................................................... 6
   Differences between FES and the Oliver System ....................................................... 7
   Executive Level Measurement.................................................................................... 8
III. Advantages of the Current Executive Evaluation Systems ..................................... 10
IV. Problems with the Current Executive Evaluation Systems ..................................... 12
V. Private Sector Compensation Programs for Executives .......................................... 16
   Johnson & Johnson’s Example ............................................................................... 16
   Statistical Figures.................................................................................................... 18
VI. Could Private Sector Initiatives Work? ................................................................... 21
   Skill-Based Pay........................................................................................................ 22
   Competency-based pay........................................................................................... 22
   Gainsharing............................................................................................................. 23
   Cash incentives........................................................................................................ 24
VII. Other Suggestions .................................................................................................. 25
VIII. Conclusions ......................................................................................................... 26
Bibliography ................................................................................................................. 29
I. History of Public Compensation

Evaluation systems have existed throughout the world for ages, which can be found by looking at the long-standing military and religious hierarchies that have existed with their ranking structures for centuries (Oliver 3). More recently, however, job evaluation as it exists today in the United States can be traced back to Frederick Taylor and his revolutionary ideas for efficient production in manufacturing facilities near the end of the 19th century. Taylor’s ongoing mission was to find the most efficient method to perform a working task, which led to job evaluations to determine that method. Therefore, the earliest job evaluations existed as virtual “how-to” manuals, and developed into a way to determine who was performing more complicated duties. Differing compensation among these employees thus began a comparative compensation structure (Risher and Fay 3).

General Schedule

The General Schedule is the most widely used model of government job classification, and it was conceived back in 1923, following a time of federal reinvention at the conclusion of the First World War (Risher and Fay 86). Since that time, slight modifications have occurred, but the basic structure has remained static. This federal classification system was altered slightly in 1949 as part of the Classification Act, with the creation of fifteen grades into which all jobs of the federal government are placed (Risher and Fay 27). This system was developed in order to rank peoples’ jobs and pay them equally for similar jobs, as well as to ensure there was a systematic way to evaluate how much an individual should be compensated for their work responsibilities.
Steps have been taken to alter the General Schedule and bring it up-to-date as time has passed, and one of the largest steps regarding the federal executive pay occurred during President Carter's administration in the late 1970's. This established the Senior Executive Service (SES), which is for levels above GS 15 and represents six pay levels above that. According to Risher and Fay, the SES has no grades and does not base pay on job content, but on the individual. A person at the higher executive levels can opt into this system of merit pay, instead of staying in the typical GS schedule. This system serves as an example for the state and local levels of government, and the goals of the system are listed below (166-167):

- Provide greater authority to agencies to manage executive personnel.
- Enhance recruitment and retention of competent executives.
- Have the flexibility to assign executives where they can contribute to an agency's performance.
- Hold executives accountable for individual and executive performance.
- Provide for a flexible, merit-based system.
- Provide for the development of executives, reward outstanding performers, and provide the discretion to remove poor performers.

The Leadership Effectiveness Framework provides a set of competencies that are required for a given position, along with other specific professional experience that is dependent upon the position at hand. Salaries are decided after negotiation between the applicant and the agency, and can be placed at any of the six levels within the upper structure. Hiring bonuses and retention bonuses are possible for these executives, and performance appraisals at a minimum frequency of a year are required. While these salaries often depend on the funds allotted to an agency, the 1994 statistics for the super structure placed ES 1 at $95,771 and ES 6 at $119,275 (Risher and Fay 166-67).
Federal Factor Evaluation System

Job evaluation in a classification system, such as the General Schedule, involves constructing a job description of the duties performed and knowledge, skills and abilities required to effectively perform those duties. The job is then placed into a rank of GS 1-15 to determine pay received. The federal Factor Evaluation System (FES), the most commonly used system in the public sector, evaluates jobs from the job description on weighted compensable factors that have explicit definitions as to the degree of each factor a position requires (Risher and Fay 109). This system was developed during the beginning of the 1970’s to find a more thorough way to ensure accurate placement of positions with pay for duties performed.

For example, one compensable factor for FES is “Work Environment”, and if a person works fighting fires, he/she is going to receive more points for this factor than a person who sits at a desk in a climate-controlled office environment. The point value levels within each compensable factor lead to a sum total of points for a job, which can then be compared to the General Schedule for a ranking of GS 1 through GS 15, if an organization wishes to do so.

In all point-factor systems of job evaluation, the same generic factors exist for determining a job’s relative worth. Those factors are skill, effort, responsibility, and working conditions, and many formats of job evaluation structures exist that utilize these, stemming from the federal Factor Evaluation System. FES may be the most widely used point factor system in the public sector, but many variations of point-factor classification systems exist that are used on the local levels (Risher and Fay 109). One specific example of a point-factor system that eventually leads to a wage structure for an
organization is called the Oliver System, which will now be discussed in depth to lead to better understanding of this type of job evaluation and compensation structure.

II. Oliver System for Job Evaluation

History of Oliver System

The Oliver System, named after founder Philip M. Oliver, was developed during the beginning of the 1970's. It began as a Task Force Study, proposed by President Nixon and approved by Congress, to study the current systems in place for evaluating jobs and pay structures within the Federal Government (Oliver XI). This system is the result of the study, which examined the problems in the Federal Government job evaluation program and attempted to develop a system to eradicate these problems.

Although not the standard system used for the Federal Government, the Oliver System is also a point factor ranking system for job evaluation that contains many of the similar characteristics of the Factor Evaluation System. The Oliver System, since its inception in the 1970's, has been used in many different levels of government as a job evaluation system, from the city level to the state level and in foreign countries (Oliver XI). It is used as a basis for developing job evaluations and pay structures throughout many counties and cities in the State of Indiana, for example, when they contract with the consulting firm with which I am interning.

The Oliver System strives to provide a way for employee jobs to be placed into an internal ranking that coincides with equitable pay. This system is similar to the Factor Evaluation System by taking benchmark job descriptions and evaluating them on the major components considered essential to performing job functions. These evaluations
are given numerical point representations, depending on the degree of involvement within each factor, and the numbers are totaled. After all of the benchmark jobs are completed, a regression analysis is performed between the number of points assigned and the wage received.

The resulting graph can then be used to generate an equation that represents the midpoint of the placement of the individual benchmark jobs. This equation enables compensation specialists within an organization to determine where a person’s salary should lie relative to the difficulty of their job, based on the number of factor points received. Of course, it takes time and effort to construct this graph, but once the benchmarks have been accurately placed, the other jobs can “fall into place” as to where they should be for their point totals. In addition, it is generally recommended to conduct surveys of similar local jobs to assess their salary and ensure the salary being paid within the organization is externally aligned.

**Differences between FES and the Oliver System**

One major difference between the federal Factor Evaluation System and the Oliver System exists in the separate evaluations depending on the type of job that is used by the Oliver System. FES assesses all jobs on the same nine factors (work environment, purpose of contacts, etc), regardless of whether the position is managerial, clerical, or labor-intensive. The Oliver System, on the other hand, operates under the concept that like jobs should be paired with like jobs, and that dissimilar jobs, when paired together, can destroy the internal and external alignment attempted with an evaluation structure (Oliver 4). Jobs are also evaluated within substructures by job type due to the differences in what is considered to be the “local labor market”. Executive and managerial jobs tend
to have a wider labor market than clerical jobs, as executive local labor markets may extend to the national level.

The seven job categories of the Oliver System operate independently of one another and only are related by being a part of the same organization (Oliver 9). These categories are for Labor, Trades, and Crafts (LTC), Clerical, Office Machine Operation, Technician (COMOT), Protective Occupations and Law Enforcement (POLE), Professional, Administrative, Technological (PAT), Supervisors and Managers (SAM), Special Occupations (SO), and Executives (E). The majority of these categories are self-explanatory, with LTC being labor-intensive, janitorial, and physically involved, COMOT being more office-oriented, POLE involving police and sheriffs positions, and PAT involves higher level education and/or experience than the others mentioned. SAM positions supervise other employees and usually involve more job experience, SO occupations typically are a mixture of two or more previously mentioned categories, and E jobs represent the highest few percent of the total workforce and are discussed more in depth below.

**Executive Level Measurement**

For the majority of categories within the Oliver System, the same general factors of job requirements, difficulty of work, responsibility, personal relationships, and work environment are used. This is almost identical to skill, effort, responsibility, and working conditions, which are the factors used in the Factor Evaluation System. However, the Executive job category has four factors that are all significant aspects of an executive position, although they vary from the typical factors. The Oliver System varies these
factors because this system recognizes that different positions in an organization need to have focus in different areas.

The first factor used is entitled "Knowledge and Skill", and measures the range of information, accounting for amount, breadth and depth, and the application of this knowledge to the duties of the position. The second factor is entitled "Impact", and measures the result of the incumbent's actions, considering all applicable factors. The third factor used in the Oliver System for Executive positions is "Complexity and Difficulty", and measures these with respect to the duties involved with the position. The final factor is "Relationships", and this examines the communication with others at all levels of the organizations, as well as outside the organization (Oliver 15-16). All of these still remain similar to the main factors involved in every current job evaluation system, but have been varied to coincide with the differences involved in a position that usually oversees the entire operations of an area of an organization.

Looking more specifically into each factor, the Knowledge and Skills factor looks more into what is needed to manage the programs, rather than what specific subject material is being managed. The skills evaluated are, "analytical, creativity, initiative, judgment, leadership, persuasiveness, planning, and implementation" (Oliver 23). The second factor of Impact examines how much impact, how direct it is, freedom to allocate resources, and the effect on the general public. The third factor of Complexity and Difficulty looks at the number of issues, the variety, the intensity, and the responsibilities involved with the issues. The final factor of Relationships measures frequency of contacts, the level, internal or external, and importance of contacts (Oliver 23-24).
In order to calculate the total points allotted to an individual’s job evaluation, the weighted components of each factor must be calculated. For the Executive level of compensation evaluation, the factor of Knowledge and Skills was given 35% of the weight, Impact and Complexity and Difficulty both received 25% of the weight, and Relationships assumed the final 15% of this weight. This was devised by Oliver as a way to properly assess the importance of each factor with respect to the entire performance of an Executive’s job. From these points, a graphical analysis can be conducted with other Executive benchmarks in order to create a wage structure for all Executives in the public sector for the organization.

III. Advantages of the Current Executive Evaluation Systems

One of the major benefits to an evaluation system with factor points, regression, and benchmarks is the consistency that is created within an organization, not just at the executive level. A hierarchy is created that is legally defensible with respect to pay, if an equation has been developed into which a job’s evaluated factor points fit. Each employee can know that his or her job, according to this structure, is being given an amount of money equal to his or her coworker who performs at the same level. Both FES and the Oliver System represent structures people can look examine and assess where they belong.

Also, it is a widely accepted structure that can be easily challenged. People frequently request reclassification of their positions due to a change in duties, or a feeling that they are not equitably compensated for their duties performed. At that point, a person, usually a human resources representative, reviews the changes requested and either approves or denies the request. This system creates a checks and balances that
ensures employees cannot be paid whatever they demand on a whim, while still establishing a way to reevaluate when needed.

Next, the factors that a system such as the Oliver System evaluates are still relevant to what is needed for public executives to effectively perform their functions in their positions. The factors of Knowledge and Skills, Impact, Complexity and Difficulty, and Relationships can be argued to be the most inclusive of job factors upon which an executive level position in the public sector should be evaluated. Furthermore, these factors examine the wide array of items encountered in the executive level positions, instead of being an exact replica of what is used to examine the other positions within the job hierarchy. For example, the Oliver System evaluation for an Executive (E) position measures similar, although not identical, items as the Labor, Trades and Crafts (LTC) evaluation.

The largest benefit to the current evaluation systems for positions in the public sector is the many auxiliary uses to this ranking system for human resource professionals, including assisting recruitment by listing minimum qualifications and training of current employees for succession/promotion, as well as to train new employees to effectively perform their own positions. Performance rating can also be assisted by evaluation because it specifies the standards to which an individual should perform the position. Another auxiliary use for a ranking point factor system is in grievances, because an evaluation system sets the standards for work to be performed with respect to content and level of performance (Oliver 103-104).

The final advantage to the current Executive evaluation systems is that they have been in place for years. The General Schedule has been the system people have known
for almost eighty years in federal government. And the past has shown that when changes are needed, for example in 1949, it is a malleable system that can adapt to the times. The capabilities of the FES and Oliver System to fit point-factor analyses within the General Schedule structure shows further adaptability. Finally, the development of the Senior Executive System in the late 1970's shows the strides that the government is willing to take with respect to Executive positions to attract and retain individuals worthy of existing within the highest levels of public sector organizations without being elected officials, if people choose to opt into the SES.

**IV. Problems with the Current Executive Evaluation Systems**

First of all, for the evaluation of executive positions on a local level, these positions are typically not held under the same stringent structure as the other positions. Usually, these positions are excluded from a pay study performed, and their salaries are allocated from a local council. These are the same people to whom they report. Therefore, at least locally, it is difficult to align executive salaries in the area of wages because they tend not to be handled in the same way as other positions within a local job hierarchical structure.

In addition, while the Senior Executive System creates an example of a structure for executive positions that has vital points of merit pay, performance appraisals, and financial incentives to attract and retain the individuals needed in the public sector, this high level of pay is almost always impossible in more local public structures. Many executive level employee salaries are determined by the previously mentioned public councils, and one of the largest issues that exists with council salary determination is pay compression. Pay compression occurs when there is a very small difference between the
wage received by the highest level position and the positions below that. In local public arenas, most items are controlled by public opinion.

For this reason, executive salaries are not given the same annual increases as other positions in local government. After a few years, the higher-level administrative positions have begun to "catch up" with the executive salaries, and pay levels need to be adjusted. Because executive compensation is treated separately and specially, it is more difficult to justify the needed increases until the discrepancy in salaries is substantial. Also, if there is a shift to merit pay for executives, like with the SES system, the funds have to be there to allocate to executives upon achievement of objectives. Oftentimes these extra funds do not exist.

Local governments are currently having increasing difficulty in attracting and retaining higher-level professional jobs that are not at the executive level. Examples of these jobs include nurses, information systems personnel, and planning positions. Many of these agencies have had to resort to using parts of their financial budgets that were previously allocated to other items for the local government in order to attract people to these positions through hiring bonuses. This "tightening of the purse strings" has put further pressure on the wages given to executives in these structures, since they should be the highest paid in their particular department.

While it makes no sense to pay subordinates more than their supervisors, this occurs in government with, for example, a State Governor or the President. The very hierarchy of positions that a job classification system strives to produce is not supported by the funds allocated to pay the people in those positions. The same occurs in local government with the various department heads, for example, a County Auditor and a
County Treasurer. Numerous examples exist to demonstrate people who are paid the exact same pay because of their title as a department head, regardless of the duties performed, the difficulty of those duties, etc. Many times the executive level positions are treated as “special” because of the differentiated circumstances behind their pay, and that does not mean they are treated “special” in a good way (Risher and Fay 165).

In theory, the executive level positions should be treated the same as other positions, with benchmarked comparative positions that can be used to determine equivalent pay externally. Also, the positions within an agency at the Executive level should be internally compared with their factors and their salaries. Too often, however, this does not occur, as there are neither enough positions within an agency to create a valid regression analysis, nor is there enough external market data to compare to the agency salaries.

Many arguments also exist surrounding the age of the current job evaluation and classification systems. Both the Factor Evaluation System and the Oliver System were developed during the early 1970’s, and although the government has shown willingness to update their systems as needed, what these systems measure is still outdated. A specific example of this exists in the Oliver System tables for Executive (E) factor evaluation in the factor of Relationships. The number of points given for this factor depends upon the frequency of contacts, the level of contacts, whether they are internal or external to the organization, and importance of contacts (Oliver 23-24). In the last thirty years, organizations as a whole have turned to a theme of downsizing, and the number of contacts, their level, position, and frequency for a given Executive level position may have decreased over the last three decades. However, this structure still counts the...
numbers, thereby supporting what used to be considered most important, but no longer is as important as it used to be.

Other major factors were mentioned by Risher and Fay that criticize the current systems used in general, and not just at the executive level. The largest one of these focuses on the subjectivity of the evaluation of factors, depending upon a rater’s opinion of duties performed from a written job description. Furthermore, once managers know which “buzzwords” lead to greater factor points, and therefore more pay, they oftentimes doctor their subordinate’s job descriptions to inflate the position’s factor points. The current evaluation systems overemphasize achieving a rewrite of duties to get a wage increase.

Another similar argument is that the current systems consist of too rigid of a structure, and are often used as a control mechanism. Composing a questionnaire from which a job description is written, changes are sent back and forth using more paper, and finally factor points are assigned and a wage is determined, glorifies the paper-pushing, bureaucratic nature for which the public sector is so often criticized. Finally, Risher and Fay emphasize that the current evaluation systems, “…were designed not to accommodate and support rapid organizational change but rather to reinforce the stability of work and organizational relationships characteristic of the traditional scientifically managed organization.” (4). Today’s organizations, whether in the private or public sectors, must be more adaptable to change and able to conform. Team projects and multifaceted positions performed by one individual in an organization are two examples of frequent occurrences in today’s workforce that are difficult to align with current compensation structures.
V. Private Sector Compensation Programs for Executives

Many private sector compensation programs are in existence for executives in the workplace. Some, such as the Hay system, are point-factor comparison compensation systems utilized by many organizations in the private sector. In fact, the Hay system is the most widely used point-factor compensation structure in the private sector (Risher and Fay 109). Many smaller organizations do not have set structures with which to equitably compensate the employees at various levels of the organization; however, larger private organizations have published systems outlining their wage structures.

One such organization is Johnson & Johnson, and the specific information regarding the details of its Executive Compensation is discussed below. There are also significant statistics derived from polls determining the public’s opinion of their executives’ pay levels and whether or not they believe they are equitable. The public’s perception of their highest level supervisors’ pay is important because their perception is directly linked to their own perception of equity in their workplace. These survey results are also discussed after the Johnson & Johnson’s example of a private sector’s compensation structure.

Johnson & Johnson’s Example

The following information regarding the compensation of Johnson & Johnson’s executive level positions within the company is derived from the Notice of Annual Meeting and Proxy Statement on March 14, 2001. The compensation committee, consisting of nonemployee members of the Board of Directors, reviews, recommends and approves any changes to Johnson & Johnson’s compensation policies and procedures. As stated in their “Compensation Policy and Objectives”, Johnson & Johnson executive
compensation programs are designed to enable the Company to attract, retain and motivate the high caliber of executives required for the success of the business. These systems strive to support the current, as well as the long-term performance of the business.

The Chief Executive Officer’s compensation is determined entirely by the aforementioned Compensation Committee after they have examined the financial and nonfinancial performance of the organization. The primary consideration in assessing performance is corporate results over a long-term period, even though performance in many areas is assessed on an annual basis. For financial comparison externally, as well as comparison to Johnson & Johnson’s own yearly results, measures used include sales growth, earnings per share growth, increase in cash flow, new product flow, and growth in shareowner value. The nonfinancial performance measures are evaluated by the committee as a result of the “Credo” of Johnson & Johnson, outlining their direction and targets, looking at what is primarily considered to be mission and vision statements.

Four main areas exist for executive compensation within Johnson & Johnson, and the first of these is base salary. The Johnson & Johnson Salary Administration Program exists for all exempt employees, and increases in base salary are contingent upon the factors of merit, market parity, and promotions. Merit increases are based on an individual’s performance within his/her position. Market parity is an external alignment based on analysis of similar positions in organizations similar to Johnson & Johnson. Promotions resulting in an increase of base salary are from increases in work responsibility.
The second area for executive compensation within Johnson & Johnson is their “Cash and Stock Incentive Compensation Programs”, and there is a set maximum award that can be distributed among the executive employees. The amount allocated to each executive is strictly up to the discretion of the Compensation Committee after they are presented with all figures and reports from the previous year. The third area of executive compensation is Stock Options, designed to link shareowner value with executive rewards. As with the “Cash and Stock Incentive Compensation Programs”, there is no set formula by which the Compensation Committee decides which executives are to receive Stock Options, nor how to allocate the total allotted.

Both of these compensation plans are decided by the Committee at its own discretion, and the same applies for the final area of executive compensation. The final compensation program consists of Certificates of Extra Compensation (CEC), and these Certificates provide deferred compensation offered upon the conclusion of an executive’s career with Johnson & Johnson. Specific award amounts are once again based on the Compensation Committee’s evaluation of individual performance and contribution to the company on a long-term basis. While programs such as these in the private sector provide many rewards to the executives involved, and assist in achieving the goals of internal and external motivation, issues may exist within the lower levels of employees within an organization, which is discussed next.

**Statistical Figures**

According to John Dantico, author of “The Executive Pay Package-What’s Different?” pay for executives in the private sector is different from pay for other employees in several key aspects of what is offered. Overall, the packages offered
beyond base salary and an annual cash incentive plan involve numerous, often complicated, accounting, tax, cost and documentation issues. This is further supported from the BNA Daily Labor Report, which used the annual *Worldwide Total Remuneration Report* to find that over 11 million employees are now covered by long-term incentive stock plans, and stock options are the most common type of long-term incentive used, especially for senior management and executive positions. “One of the reasons for this dramatic rise is that companies are increasingly seeking ways to tie pay to performance,” said Robert Freedman, who is a global executive pay specialist from the company that performed the study, Tower Perrin.

According to the same study, the use of long-term incentives for a typical chief executive officer is also occurring more frequently in other countries. Canada and Malaysia offer long-term incentives on average for a CEO equal to 90% of base salary, just behind the US average of 111%. Singapore offers 71% of base salary, and Brazil is next with 54%. The same report also shows significant growth in annual bonus and long-term incentive awards in countries around the world for executives. All of these statistics are interesting to show the trends occurring in the private sector, but they also poses a question involving what the other workers in an American business think of the compensation their executives are receiving.

A poll conducted by Business Week/Harris in the summer of 1997 showed the beginnings of deep resentment between employees and their executives because of the compensation these executives are receiving. The average compensation for top executives in large companies rose 54% in 1996, but the average American worker only received an increase of 3-5% in the same year. The ratio of CEO pay to average wages
was 143:1 in 1992, and increased to 185:1 in 1996. And it has continued to increase since then.

When polling the employees of the organization, 72% of executives surveyed felt they are paid the “just right”, but only 19% of the public feels executive compensation levels are “just right”. Some of this dissention can be related to the idea that the public feels top executives receive further rewards for positive results, but they are not penalized for negative results. Both groups had a majority who believed executives should have a cut in salary if the company does not perform up to standards, but there was one staggering statistic upon which the groups greatly differed. Almost 70% of the public believes the growth rate of executive compensation should not be greater than the growth rate of the lower level workers at a company, when only 21% of executives supported that notion.

While this idea makes sense, it would be impossible for any company to be able to attract and retain the best executives unless all companies initiate this policy, which will not happen any time soon. As mentioned before, executives in both the public and private sector have to be paid at levels high enough to receive interest from the best, which is all any company would want to work for them. For private companies, like Johnson & Johnson, that can afford to pay their executives large amounts of incentives through allocated budget excess, paying above and beyond may work for them. But they need to consider the affects this excess in pay may have on the morale of their general workers.
VI. Could Private Sector Initiatives Work?

The compensation plans that Johnson & Johnson have for their executives are innovative and work well for that organization; however, they are inapplicable to the public sector for a multitude of reasons. First of all, from a practical viewpoint, nothing in the public sector is comparable to stock options as offered in the private sector. Next, the Certificates of Extra Compensation and Cash Incentives must have the extra funds behind them that enable those awards to become a reality. In current governmental structures, as mentioned previously, funds are already too strapped. That leaves the ideas listed within “Base Salary” for Johnson & Johnson’s executive pay plan to be examined.

The increase in base salary upon promotion makes sense, and already occurs most of the time in both the public and private sectors, so it will not be discussed further. The idea of market parity, which is oftentimes called external alignment, occurs in the public sector after surveys are conducted, and even then occurs infrequently. The final area of base salary increases occurs from merit increases, or increases based on performance, which would be an excellent idea in government executive pay, if the extra money required out of an agency’s budget exists. Also, in the Johnson & Johnson example, these funds are allocated at the sole discretion of the appointed Committee, which could lead to multiple potential legal battles for a government agency.

In addition, as mentioned above, creating a larger differential between pay levels for executive pay and the lower levels of pay will not help employee morale in public agencies. There are already enough issues with respect to the allocation of budgeted funds to public workers. Too often in public agencies, annual increases in salaries are given regardless of performance, to the point where an “entitlement” culture has
developed among employees, regardless of the actual pay structure in place. The major idea among proponents of change in public compensation point out the need to end the entitlement culture through changes in compensation structures, also in an attempt to link desired employee behaviors and performance to pay received.

**Skill-Based Pay**

One idea proposed by Risher and Fay for public compensation is a shift to a skill-based pay program, with a focus on individual performance within a given position. The premise of skill-based pay is every time an individual within a position learns a new skill, he/she receives a raise for the new skill he/she is capable of performing (127-8). Seniority tends to fall into place in this type of system, as it encourages constant self-improvement and creates its own hierarchy, because people who have been in a given position longer have had more opportunities for pay increases through more skill learning opportunities. This creates an external motivation for self-improvement. While a good idea in theory, skill-based pay programs have been proven to work most effectively in a labor-intensive environment, where additional skills can always be utilized. When assessing compensation programs for executive level pay, skill-based pay is not the most applicable solution.

**Competency-based pay**

Competency-based pay is similar in theory to skill-based pay with the idea of paying employees for what they are capable of performing in the context of their position. The ultimate intention of instituting competency-based pay in an organization is to define what successful workers are expected to be able to do at each level on their
career ladder (Risher and Fay 146). Also, the fundamental idea behind competency-based pay is that an employee's value depends on what that employee can do within an organization, and that the person with the most competencies will be at the highest level. Yet again, this compensation structure supports the move away from just performing responsibilities of a position into also taking responsibility and being evaluated on an individual basis.

If a public agency truly wishes to get away from the entitlement culture that exists so strongly within current organizations, a shift to competency-based pay would be a reasonable solution. The current requirements of a position listed in a job description could easily be rewritten to adapt to competency levels, and the most commonly used federal classification system already supports specific levels at which an individual has to perform duties, and outlines them in job descriptions. Finally, competency-based pay also focuses on subjective assessments, just as the current system does, so it has its flaws. But this system does have enough potential to be looked at more thoroughly if a public agency wishes to institute significant changes that may reap substantial rewards for the organization.

**Gainsharing**

A potential motivational compensation program could exist in addition to whatever current system is in place. This plan is known as gainsharing, and has a focus on rewarding employees based upon the productivity of the work group. This is not a guaranteed bonus; it is variable pay that is not the same as profitsharing, and it actually seems to be utilized less in the federal government. Trials were performed in the 1980's
within the Department of Defense and the IRS, as well as the Air Force, and the results versus those of a control group in trials were disappointing (Risher and Fay 235-7).

The results were disappointing due to a wide variety of reasons. And while there did not seem to be a particular flaw in design, many reasons were provided as to why the circumstances did not work. However, the trials did provide good grounds upon which to discover the best conditions under which gainsharing could work. The largest problem when considering practical application in a public agency is the lack of supplemental funds in a government sector. Very infrequently do government agencies have the capability to conclude operations with extra funds left in the budget that could be allocated among the employees. And if a public agency achieves its targets without full utilization of budget finances, chances are, the agency will not receive those finances in the next budgeted term because the agency proved they did not need all of the funds. This creates a vicious cycle that is counterproductive to a gainsharing plan, as well as employee morale.

Cash incentives

The same major issue mentioned above exists for the idea of cash incentives. At this time in local government, cash incentives are being offered to new employees in order to attract them to the professional positions, as was previously mentioned. This puts even more pressure on the current budget local agencies have with which they pay employees. If an agency does not go over its budget it is a major accomplishment, not to mention performing at the budgeted limits. Having extra money with which to entice performance through cash incentives is a good idea for linking pay to performance; however, it is not a feasible option for the public sector for any level of employee.
VII. Other Suggestions

While it is impossible to address all of the issues within public compensation structures, including subjective position evaluations and entitlement culture, there is one suggestion for which executive level employees can be held more responsible for the outcomes of their departments or agencies. The Balanced Scorecard, by Robert S. Kaplan and David Norton, discusses linking an organization’s strategy to its actions to achieve long-term success. The ideas represented in this book can be related to public sector government agencies. Financial perspective of strategy accomplishment is not the only objective to consider, according to the book, there are also the customer perspective, the internal-business-process perspective and the learning and growth perspective that must be examined for a well-rounded organization to succeed.

The stringent focus on financial factors is no more obvious than in the public sector, where operating within budget is key. According to Risher and Fay, government executives are rarely held accountable for their performance, or for setting and working to achieve realistic but difficult goals (173). This needs to change if an agency is expected to be successful. An agency needs to derive goals from its mission statement, even backtracking to derive a mission statement if it does not already have one, then the same agency needs to construct goals which contain stretch, but are possible.

Kaplan and Norton acknowledge that for government agencies, the financial perspective composes a strong constraint. However, a government agency’s success should not be measured on its financial successes. “Success for government... organizations should be measured by how effectively and efficiently they meet the needs of their constituencies.” (Kaplan and Norton 180). The customer perspective of the
Balanced Scorecard must be seriously considered here, for without the public, governmental agencies would not be in existence.

While it is unfortunate that finances pose a constraint on objectives, instead of being an objective themselves, objectives of customer focus need to take precedence in the public sector workforce. Executive level employees need to be held responsible for financial budgets, as they already are, but they also need to be in charge of devising customer service objectives. Then they should be ultimately held responsible for their unit’s accomplishment of these objectives or not. Even though many of the Balanced Scorecard’s ideas exist primarily in theory, and it is difficult to estimate how accomplishment of objectives would be rewarded, the ideas themselves are important to consider.

VIII. Conclusions

The current job evaluation systems that are in place to evaluate public sector executive pay need to be updated if they are to remain in use. For overall public sector usage, point-factor analysis in order to construct a wage structure is a paper-pushing, bureaucratic system, but it has worked for years and will continue to work if updated to reflect the current items needed to be measured in compensation administration. Flatter organizational structures and a focus on teamwork are two evolving trends found in any workforce, public or private. At the same time, restricted budgets and difficulty in attracting and retaining qualified professionals are issues that must be addressed immediately in the public sector. These are just an example of the items that must be considered when deciding what, if any, changes need to be made to current systems such as FES or the Oliver System.
At the same time, competency-based compensation structures are worthy of more consideration to potentially alleviate some of the issues in public agencies involving compensation. While substantial work would be required of any human resource professional attempting to implement such a system, the feasibility of such a system is the most realistic of any proposed at this time. A competency-based structure would put an end to the entitlement theory in place currently in public sector workforce, but for these reasons, employee backlash would be considerable.

Finally, the ideas portrayed in the Balanced Scorecard are considerable ones to keep in mind when looking at public sector compensation. Agencies seem to have lost their focus and only operate to achieve their financial goals. Working toward achieving objectives such as quality customer service would help the public sector get a better name with the people they serve, which would lead to better public reception to higher wages, in theory. Having objectives upon which to focus helps any worker, in the public or private sector, to work more diligently. And focusing upon both financial and nonfinancial objectives and their accomplishment will enable executive level employees to be held more accountable for their quality of management on the job.

While I do not claim to have any concrete answers regarding executive level compensation in the public sector, I do believe there are arrows pointing to a better direction. If these avenues are pursued, including revamping the current evaluation systems and examining ideas such as competency-based pay structures, and the ideas outlined in the Balanced Scorecard, agencies may have a better idea as to where they are heading. Working with an updated system that reflects the current needs of an agency, while maintaining constant communication with employees at all levels of the agency,
will lead to understanding of any changes. This will eventually lead to acceptance, and
finally public compensation at the executive level will once again measure what it is vital
for employees to help the organization succeed.
Bibliography


