Rewarding the Team

California's compensation system undermines efforts to recognize and reward employees dedicated to public service. Management salaries are uncompetitive with the private sector and other governments. Senior managers have few options for recognizing excellence in individuals and fewer still are exercised. And the State fails to maintain adequate pay separations between managers and their subordinates, creating disincentives to enter management ranks and undermining morale.

To attract the best and the brightest, leverage their potential and promote ongoing improvement, compensation must be strategically designed to improve outcomes. The State's compensation strategy should target three goals:

1) Compensation should promote the recruitment and development of the most skilled managers to improve public outcomes.
2) Policies and procedures should encourage tailored compensation packages to best reward and motivate public employees while holding down costs.
3) Compensation should recognize performance that advances public goals and improves outcomes.

To achieve these goals, the State must address the policies and practices that impede progress.

Problem #10: Management compensation is not competitive, hindering efforts to hire and retain the best and brightest managers.

California lacks an effective compensation policy for managers. For many department directors and other senior officials, compensation is fixed by the position. For example, directors of major state departments generally earn $123,255 annually.[120] But for the majority of managers in state service, salary increases are determined each year, based on the strength of the economy and whether rank and file workers are granted increases. During good budget times, salaries go up, during lean times raises are put on hold or reductions imposed across the board.

The State's Competition

County governments often pay their department directors significantly more than is offered by the State, for far fewer responsibilities. And federal employees in the Senior Executive Service in the Sacramento area earn between $107,550 and $162,000. In comparison, state employees serving as CEAs, a comparable class, earn between $69,216 and $117,960.

Sources: U.S. Office of Personnel Management. Department of Personnel Administration.

Determining pay levels. Each year, the Department of Personnel Administration reviews the compensation provided to managers and proposes changes based on the concerns raised by managers and agreements reached at the collective bargaining table with non-management workers. In simplest terms, the State seeks to pay managers 10 percent more than their subordinates, but only if the money is in the public coffer.

State law directs that "like salaries will be paid for comparable duties and responsibilities. In establishing or changing these ranges, consideration shall be given to the prevailing rates for comparable service in other public employment and in private business."[121] But the State does not have a grasp of comparable work or comparable pay.

Despite access to detailed employment and salary information, the State does not use these data to track compensation trends, develop pay policies or adjust earnings. In late 2004 DPA sought the assistance of personnel officials in other departments to call local agencies to determine the competitiveness of state compensation packages, a strategy that at best would provide a snapshot of compensation levels.

In contrast, the federal Office of Personnel Management taps national compensation surveys performed by the Bureau of Labor Statistics to develop local pay scales for federal managers in all regions of the country. Federal sampling procedures are under constant review to provide the best analysis to guide federal compensation decisions. Federal pay scales are tuned to 95 percent of the pay offered for comparable work in the same geographic region and the federal government issues an annual report on efforts to meet that goal.[122]

Entry-level positions. California's personnel system was designed to bring in potential managers as analysts who can graduate into management roles. The Staff Services Analyst position is the entry-level position for prospective managers in state service. Beginning pay for a Staff Services Analyst is $31,584 per year. A comparable position at the county level pays $43,584 in Placer County, $48,586 in Alameda County and $56,184 in Sacramento County.[123] The City of Sacramento, the home of California state government, pays $48,612 per year for a comparable position.[124]

The federal government generally recognizes federal grade scale 5 as the entry level for recent college graduates, offering $28,751 as a starting salary in the Sacramento area. But pressure to attract employees with multiple offers has pushed federal agencies to pay new hires at grade scale 7, or $35,614 annually. Nationally, the average starting salary for recent college graduates entering management trainee or other entry-

Salary Scales

The State has 4,462 separate job classifications which define the duties and pay scale for each state position. Many of these positions are grouped in classes that reflect similar skill sets but with specific areas of focus, such as Associate Governmental Program Analyst and Associate Personnel Analyst. Positions that perform comparable work receive comparable pay. The diagram reflects the organizational hierarchy of a sampling of positions and their respective salaries. Technical positions, including attorneys, medical professionals and other classifications, are not represented.

Position	Salary Range
Cabinet Member	$127,560 to $137,976
Major Department Director	$119,664 to $129,432
CEA V	$107,016 to $117,960
CEA IV	$101,112 to $111,444
CEA III	$96,360 to $106,248
CEA II	$87,624 to $96,612
CEA I	$69,216 to $87,888
Staff Services Manager III	$76,008 to $83,808
Staff Services Manager II (managerial)	$69,216 to $76,332
Staff Services Manager II (supervisory)	$62,532 to $75,432
Staff Services Manager I	$56,952 to $68,712
Associate Governmental Program Analyst	$49,332 to $59,964
Staff Services Analyst	$31,584 to $49,860
Management Services Technician	$27,972 to $38,412
Office Assistant	$23,256 to $31,056

Source: Department of Personnel Administration. 2005. "Section 8: Variable Compensation." *Universal Salary Schedule*. Department of Personnel Administration. 2005. "Exempt Roster." *Civil Service Classification Database: Personnel Information Exchange*. Accessed May 10, 2005. Department of Personnel Administration. 2003. "Exempt Salary Chart." On file.

level management positions, in both the public and private sectors, was $34,447, or 10 percent higher than the State's entry-level pay.[125]

Setting aside differences in benefits and other forms of compensation, which require analysis that the State has not performed, for entry-level professionals, the State pays toward the lower end of salaries for comparable work in the public sector.

Senior managers. The State of California and the federal government each use a classification system to bridge the civil service system and the highest level of political appointees. In California, this service is referred to as Career Executive Assignments and is reserved for senior managers and executives who are tapped by political leaders. The Senior Executive Service is the comparable federal employment system.

State Salaries are Largely Noncompetitive[129]					
	State of California[130]	County of			
		Alameda[131]	Placer[132]	Sacramento[133]	Yolo[134]
Population of Region	36 million	1.5 million	292,100	1.3 million	184,500
Department	**Department of Finance**	**County Administrator's Office**	**Auditor-Controller's Office**	**Office of the Chief Financial/ Operations Officer**	**Auditor-Controller's Office**
Budget	$117.5 billion	$1.96 billion	$501 million	$4.2 billion	$252 million
Number of Employees	212,000	8,695	2,683	14,839	1,608
Director's Salary	$131,412	$218,982	$102,990	$163,728	$100,352
Department	**Department of General Services**	**General Services Agency**	**Department of Facility Services**	**Department of General Services**	**Central Services Division**
Budget	$931 million	$129 million	$145 million	$147 million	$7.1 million
Number of Employees	3,651	448	207	570	31
Director's Salary	$123,255	$155,969	$127,511	$120,874	$77,106
Department	**Department of Social Services**	**Social Services Agency**	**Department of Health and Human Services**	**Department of Human Assistance**	**Department of Employment and Social Services**
Budget	$17.7 billion	$581 million	$121 million	$665 million	$64 million
Number of Employees	3,982	2,277	840	2,188	361
Director's Salary	$123,255	$156,052	$122,016	$161,773	$103,716
Department	**Department of Personnel Administration**	**Human Resource Services**	**Personnel Department**	**Employment Services and Risk Management**	**Human Resources Division**
Budget	$105.6 million	$12.8 million	$7.7 million	$26 million	$923,000
Number of Employees	225	76	30	113	11
Director's Salary	$123,255	$145,662	$102,990	$105,966	$75,150

In California, CEA salaries range from $69,216 to $117,960 based on experience, the size of the agency and level of responsibilities.[126] The federal Senior Executive Service pays between $107,550 and $162,100. Salaries for these federal positions are not adjusted by location. CEAs in state service earn approximately one-third less than their federal peers in California. Local governments do not consistently have a comparable classification.

Executives. At the top end of public management, department directors in state government generally earn $123,255 per year.[127] A few individuals earn more, including the Chancellor of the California Community Colleges, who earns $185,484 annually.[128] Department directors responsible for multibillion dollar budgets, thousands of employees and statewide responsibilities can earn considerably less than their local government peers who generally handle fewer responsibilities.

Department directors in Sacramento County generally earn between $100,000 and $150,000 annually.[135] In Alameda County, department directors earn between $100,000 and $200,000.[136] Department directors in Sutter, El Dorado and Yolo counties, smaller counties adjacent to the capital, earn between $84,000 and $120,000 per year.[137]

For senior administrators in the public sector, county or federal employment offers the potential for far greater earnings or comparable pay for considerably less responsibilities than is available through the State. For instance, in its review of the corrections system, the Independent Review Panel documented that state pay for senior correctional administrators falls short of comparable federal positions.[138]

The U.S. Bureau of Labor Statistics compiles data on public and private sector salaries in the Sacramento region. Data collected between December 2002 and January 2004 indicate that private executives and managers, on average, earn 21 percent more than their public sector counterparts.[139] At the bottom 10 percent of the management pay scale, government offers more comparable pay. On average, based on hourly pay rates, the lowest paid public sector managers earn 7 percent more than the lowest paid private sector managers. But for top earners, those earning at the highest 10 percent in the Sacramento region, private sector managers take home 42 percent more than their government peers.[140]

To attract and retain the best and the brightest, the State must offer comparable pay for comparable responsibilities. Doing so will require the State to better assess pay scales in comparable positions in the private sector, federal agencies, other states and local governments. And the State must recognize that managers assume additional duties in comparison to their rank-and-file peers, and compensation should reflect the added responsibilities. For California to attract managers and senior executives of national caliber, it must make salaries an attractive component of public sector employment.

Solution #10: The Governor and Legislature should ensure the State provides competitive compensation that attracts, retains and rewards managers and executives of national caliber.

- ***Develop competitive pay packages.*** Tapping federal efforts, the State should ensure that total management compensation, including retirement benefits, is comparable with the private sector, the federal government and local governments for each rung of the State's management ladder.
- ***Enhance compensation for senior executives.*** Pending the development and implementation of compensation reforms, the Department of Personnel Administration should explore alternative strategies to increase executive compensation, including tapping foundations or other sources of funding to ensure the State can attract national caliber executives.

Problem #11: Compensation rules are rigid and options limited, preventing the State from tailoring compensation packages to motivate improvement.

In addition to salary, California's three-tiered personnel system – rank-and-file workers, managers and supervisors and exempt appointments – offers different benefits to each segment of its workforce. Rank-and-file workers receive benefits defined in statute along with those negotiated at the bargaining table. Managers and supervisors do not have collective bargaining rights, but they are covered by civil service rules and thus enjoy the benefits of job security. And exempt employees are neither part of the civil service system nor granted collective bargaining rights, but the benefits of a political appointment include significant authority, opportunity for accomplishment and high public profile.

The majority of state employees receive health, dental and vision coverage, access to life insurance, legal service insurance, an employee assistance program, and disability insurance. The costs and coverage of these benefits may vary by employee group. Other benefits include holiday and leave pay, and access to limited merit award programs. Some employee groups can receive performance bonuses, reimbursement for the costs of required professional licenses, even assistance with relocation costs.

Despite the range of these benefits, many are insignificant. Employees who are recognized for "sustained superior job performance over a two-year period" can be granted a superior accomplishment award, which can be as small as $25 and cannot total more than $250. Supervisory bonuses can range from $250 to $750.[141] Access to group life insurance, health and dental benefits and other services is consistent with federal and private sector benefits for managers and executives and many benefits are required under federal law, such as access to continued health insurance when leaving state employment.[142]

The most recognized benefits of state employment include job security associated with the civil service system and guaranteed level of retirement benefits, including lifetime employer-paid health insurance for employees who qualify. But not all managers – particularly mid-career or second-career professionals – are willing to trade top salaries for job security and a robust retirement package. Thus the State's compensation strategy can actually thwart efforts to bring in the most qualified managers given how these benefits are structured.

Job security. The civil service system is intended to prevent political patronage. But civil service rules also shield poor performers and prevent the entry of experienced managers from other sectors. As discussed earlier, the selection process favors recruitment from within state service and discourages superior applicants from entering state service. And the costs and time involved with disciplinary proceedings undermine efforts to remove employees who fail to perform.[143] As much as the civil service system prevents nepotism and patronage, it also can undermine efforts to ensure employees have the needed skills to achieve public goals.

Assessing Needs

The State has not effectively explored with its management workforce how to better tailor compensation to needs. A 2000 survey of state employees on work and family balance needs found many seeking improved child care and dependent care services. That same year, the State established the Work and Family Fund and has provided $3.5 million to help employees balance work and family responsibilities.

Soliciting employee suggestion on other needs could improve the State's ability to recruit, retain and motivate its workers. Access to child care, tuition credits at state colleges and universities, access to new technologies at wholesale prices, sabbaticals and other innovative offerings could improve compensation at less cost than direct salary increases.

Sources: Work & Family Program. 2004. "Summary Report." Page 5. Syd Perry, Labor Relations Office, Department of Personnel Administration. March 15, 2005. Personal communication.

Retirement benefits. As the nation's workforce ages and the federal government debates reforms to social security, the State's investment in fixed, lifetime retirement benefits is a major benefit of state employment. State retirees can receive as much as 100 percent of their salary for the rest of their lives. Peace Officers can accrue these benefits with 33 years of work.[144] Fully funded lifetime health benefits come with 20 years of work. Recent scandals at the California Highway Patrol highlight the lure of disability pensions, which can shield retirement income from state and federal taxes. And recent press reports have highlighted the range of ailments defined as job-related for some public employees, including lower-back pain, heart disease and even syphilis, with no requirement to demonstrate any link between the job and the disability.[145] Although state salaries for some workers may be less than competitive, for those employees looking to remain with a single employer and retire early, state employment is overly competitive.

Compensation challenges. California's compensation system fails to recognize the diverse needs and preferences of potential employees. For many workers, the State is an attractive employer because it pairs stable if uncompetitive salaries with generous and guaranteed retirement benefits. These attributes draw an adequate number of candidates for most state jobs. But not all employees are looking for the particular compensation balance the State offers. And an inflexible compensation system may discourage skilled managers from entering public service. Several concerns undermine the State's efforts to leverage its compensation package to recruit, retain and recognize the best employees:

1. ***Individual employees have no say in compensation package.*** California's compensation system treats all employees equally. Single parents entering the job market for the first time receive the same mix of benefits – although potentially at different levels – as second-

career empty-nesters with different needs and interests. Departments are unable to offer a mix of salary and benefits that can be tailored to the needs and interests of individual employees.

2. ***State compensation assumes longevity of employment.*** The compensation system is designed for employees who join public service at the beginning of their career and remain through to retirement. Managers looking to spend a few years in state service toward the end of their careers cannot realize the value of the State's retirement package. And managers who may have lost interest in state service are prevented from transferring retirement benefits to another system and so may stay on despite a lack of motivation to perform. Job protections and a robust retirement package are of limited value to potential employees with established careers or short-term interest in state employment.

3. ***The State's compensation strategy is antiquated.*** The State offers traditional salary, benefit and retirement packages. Leading edge employers have found that employees can be better motivated by a mix of benefits that address their needs. The U.S. Government Accountability Office offers on-site child care at many of its offices. Universities commonly provide reduced tuition to employees and their families, recognizing that tuition rewards can boost the value of a compensation package at less than face value. And private sector employers may make available discounted technology and other purchases that have a mix of home and work-related uses. The State has multiple opportunities to diversify its compensation package, at less cost than traditional salary increases, including those mentioned above.

The private sector, the federal government and some states have pioneered strategic compensation systems that use non-traditional rewards to improve the value of compensation at less overall cost. The availability of on-site child care, access to training, sabbaticals, loan forgiveness programs, tuition credit at state colleges and universities, performance incentives and other rewards could form a richer compensation package at lower cost, produce a more motivated workforce and support improved outcomes.

Solution #11: To motivate improvements and attract a strong management team, the State's compensation system for managers and executives should be transformed into a flexible and innovative strategy that aids recruitment, retention and performance.

- ***Promote tailored compensation.*** The administration should periodically survey employees on their needs and interests and develop reforms leading to tailored compensation packages for individual managers.

Problem #12: The State's compensation system fails to recognize performance.

California's compensation system rewards longevity and ignores performance. First, pay raises are on autopilot. State law requires each employee to receive an annual pay raise, referred to as a "merit salary adjustment," up to the maximum pay for the position. Unless a department documents why each employee should not receive a raise, raises are automatically granted.[146] The California Performance Review reported that 99.2 percent of all eligible employees received a raise upon their last period of eligibility.[147]

Second, despite provisions for recognizing superior performance, few departments award performance bonuses. In 2003-04, the State recognized 1,024 employees, or less than 1 percent, for superior performance, granting an average award of just $250.[148] The infrequent and small size of performance bonuses undermines their effectiveness.

The combination of automatic pay increases and anemic bonus opportunities serves to level compensation at the top of the pay range. Failure to distinguish between superior performers and others can quickly demoralize the best employees. The Volcker Commission and the Brookings Institution have found that equal pay for unequal work undermines efforts to improve performance.[149]

Incentive-based compensation plans can align the State's workforce with public goals.[150] In essence, a portion of management pay is "at risk" if the public is not well served. Performance pay also motivates workers to speak up about what is working and what is not. The private sector has long utilized performance-based pay to improve outcomes. The public sector has been slow to respond, given a number of challenges associated with public sector budgeting, union resistance and other barriers.[151] Nearly 10 years ago, Governor Pete Wilson pursued merit-based pay for managers, but with little success.[152]

Reforms are underway. The federal government is linking compensation to performance for members of the Senior Executive Service (SES).[153] Federal departments with performance management provisions can increase the top range of SES salaries. For those employees, agencies can grant bonuses up to 20 percent of annual salary for outstanding performance.[154] Some expect up to half of the civilian federal workforce to be compensated under a system of performance-based pay in the near future.[155] In 2004, Congress allocated $1 million to a Human Capital Performance Fund to provide additional compensation to top performers throughout federal agencies. The President initially sought $500 million for that purpose.[156]

Some states also have performance compensation components in their performance management systems. Texas authorizes departments to award bonuses up to 6.8 percent of an employee's base pay for stellar contributions.[157] Florida has piloted a program to award departments additional funds for meeting prescribed goals, allowing funds to be used as performance bonuses for personnel.[158]

Reforms to California's compensation system should include rewards for individual performance. The State already requires departments to develop performance appraisal systems for managers.[159] But appraisals are not linked to compensation decisions.

The State has four award programs for management and senior staff. Three of these programs offer awards up to $750. The fourth, the Merit Award Program, authorizes cash awards up to $50,000 for suggestions that improve the operation and efficiency of state government. A total of 1,024 Merit Awards, averaging $250, were granted in fiscal year 2003-04. The smallest award was just $19.23, the largest, $4939.03.[160] The State's Merit Award Board, which must approve awards above $5,000 did not meet between 2001 and 2004.[161] The Department of Personnel Administration does not track awards or monitor their effectiveness.[162]

Research suggests that cash awards are the most persuasive, but the most difficult to manage.[163] Other strategies include public recognition of excellence. The President issues presidential awards for distinguished and meritorious service that include a signed certificate and distinctive

Performance Compensation

The federal government and a number of states have developed performance compensation strategies to attract, motivate and reward high-performing leaders who can consistently meet public expectations for service and efficiency. CalPERS is one example of a state entity that operates under performance contracts. In establishing its rationale for performance contracts, CalPERS states:

> *As the largest public pension fund in the nation, CalPERS' current assets are valued at over $180 billion, and a significant percentage are actively managed. Managing the portfolio requires a highly-skilled staff of investment professionals in a number of specialized areas. The primary recruitment source for these highly-qualified individuals is the private sector where they are compensated far above what is offered through the State's standard compensation strategy. Although other factors may influence qualified investment professionals to come to CalPERS, including the opportunity to work at the nation's largest public pension fund, the total compensation paid to these positions must be at a level sufficient to attract and retain the caliber of individuals needed to manage a fund of its size and complexity.*

California is home to the largest state educational system, prison system, Medicaid program, highway network and child welfare program in the country. With billions of dollars and millions of lives involved, which of these systems should not be led by the most qualified and experienced professionals in the country?

Source: CalPERS. "Suggested Response to Inquiry from Little Hoover Commission Regarding CalPERS 'Performance Bonuses.'"

pin, along with a cash award.[164] Michigan's governor periodically invites stellar employees to cabinet meetings where the cabinet stands and applauds in their honor.[165] Access to additional training, release time, partially funded sabbaticals, and other performance incentives also could form a richer compensation package, produce a more motivated workforce, reduce costs and result in improved outcomes.

As part of a strategic performance management system, the State can implement a performance compensation system that recognizes excellence, distinguishes stellar performance from minimum contributions and motivates improvement.

Solution #12: The State should craft and adopt a performance compensation strategy for managers and executives.

- ❑ ***Develop a performance compensation strategy.*** DPA, in consultation with state employees, other departments and the Legislature, should develop a compensation strategy that recognizes performance and supports improved public outcomes.
- ❑ ***Require performance contracts.*** All managers, including exempt appointees, should be hired under limited-term performance contracts that outline goals, establish performance metrics and include provisions for termination. Performance contracts should be phased in, beginning with the upper echelon of management ranks.

Rewarding the Team

Responsibility for compensation issues – from recruitment to retirement – is dispersed across several departments. And no one in state service is charged with ensuring that departments actually use available compensation tools to motivate performance, distinguish stellar from mediocre contributions, and meet the needs of individual managers. An inspired leader can transform compensation into a strategic performance initiative, guide the application of compensation policies and monitor their effectiveness. Those efforts should begin with the promotion of existing tools, the championing of additional strategies available under existing law and the identification of policy, regulatory and fiscal changes needed to better recognize and promote performance.

- ❑ **Tapping leadership.** The governor should direct the State's leader for personnel management to develop specific proposals for effectively using compensation tools to improve performance.

Compensation issues are highly political, constantly changing and require thoughtful analysis. At the federal level, the Office of Personnel Management, the Department of Labor and the Office of Management and Budget, working together as the President's Pay Agent, are charged with ensuring that federal agencies offer competitive compensation to its managers and executives. The President's Pay Agent is required to annually report on the competitiveness of federal pay and strategies to address deficiencies. A similar structure, including the director of the Department of Finance, the secretary of the Labor and Workforce Development Agency, and the director of the Department of Personnel Administration, could ensure that California's compensation strategy remains competitive.

- ❑ **Establishing a structure.** The governor and Legislature should establish a mechanism to ensure the State's compensation strategy is competitive and recognizes performance.

Compensation strategies can reinforce a performance management system. But compensation discussions almost universally focus on gaining an increment of salary increases or cutting personnel costs. A culture that focuses almost exclusively on the strength of job entitlements, reliability of pay raises and availability of cost-of-living adjustments must be replaced by a culture that focuses on public service and the opportunity to create a legacy for the people of California. Compensation should be part of a strategic effort to make that transition.

- ❑ **Recognizing the culture of public service.** The governor, agency secretaries and department directors should regularly recognize the contributions of state workers by granting and highlighting merit awards, publicizing the accomplishments of individuals and departments and celebrating state workers who personify the ethic of public service.

Source: The President's Pay Agent. 2004. "Report on Locality-Based Comparability Payments for the General Schedule."