



## Testimony

Before the Subcommittee on Civil Service and  
Agency Organization, Committee on Government  
Reform, House of Representatives

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# DEFENSE TRANSFORMATION

## Preliminary Observations on DOD's Proposed Civilian Personnel Reforms

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Comptroller General of the United States





Highlights of GAO-03-717T, testimony before the Subcommittee on Civil Service and Agency Organization, Committee on Government Reform, House of Representatives

## Why GAO Did This Study

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

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

This testimony provides GAO's preliminary observations on aspects of DOD's legislative proposal to make changes to its civilian personnel system and poses critical questions that need to be considered.

[www.gao.gov/cgi-bin/getrpt?GAO-03-717T](http://www.gao.gov/cgi-bin/getrpt?GAO-03-717T).

To view the full report, including the scope and methodology, click on the link above. For more information, contact Derek Stewart at (202) 512-5559 or [stewartd@gao.gov](mailto:stewartd@gao.gov).

# DEFENSE TRANSFORMATION

## Preliminary Observations on DOD's Proposed Civilian Personnel Reforms

### What GAO Found

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

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

The critical questions to consider are: should DOD and/or other agencies be granted broad-based exemptions from existing law, and if so, on what basis; and whether they have the institutional infrastructure in place to make effective use of the new authorities. This institutional infrastructure includes, at a minimum, a human capital planning process that integrates the agency's human capital policies, strategies, and programs with its program goals and mission, and desired outcomes; the capabilities to effectively develop and implement a new human capital system; and, importantly, a set of adequate safeguards, including reasonable transparency and appropriate accountability mechanisms to ensure the fair, effective, and credible implementation of a new system.

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

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Chairwoman Davis, Mr. Davis, and Members of the Subcommittee:

It is a pleasure to appear before you today to provide our preliminary observations on the Department of Defense's (DOD) proposed National Security Personnel System (NSPS) included as part of the Defense Transformation for the 21st Century Act of 2003. As you know, DOD is in the midst of a major transformation and it has undertaken a number of related initiatives to transform its forces and fundamentally improve its business operations. As part of DOD's transformation process, the Secretary of Defense and senior civilian and military leaders have committed to adopt a capabilities-based approach to acquisition planning and to improve the linkage between overall strategy and individual investments. At the same time, DOD has embarked on a series of efforts to achieve strategic savings and improve its business processes, including financial management, support infrastructure reforms to include base closures, information technology modernization, logistics reengineering, and strategic human capital management. In that regard, I am pleased to serve as an observer to the Defense Business Practice Implementation Board. Notwithstanding these ongoing efforts, GAO has reported a range of DOD challenges for many years. In addition, DOD also is covered by several of GAO's governmentwide high-risk areas, including the area of strategic human capital management.

The proposed Defense Transformation for the 21st Century Act of 2003 represents a substantive legislative proposal that has both significant precedent-setting implications for the government and far-reaching implications on the way DOD is managed. Specifically, the critical questions are whether DOD and/or other agencies should be granted broad-based exemptions from existing law, and if so, on what basis; and do agencies have the institutional infrastructure in place to make effective use of the new authorities they are seeking. DOD's legislative initiative would, among other things, provide for major changes in civilian and military human capital management, make important adjustments to the DOD acquisition process, affect DOD's organization structure, and change DOD's reporting requirements to Congress.

As a starting point, and as agreed with the Subcommittee, today I will provide our preliminary observations on DOD's legislative proposal to make changes to its civilian personnel system. The proposed NSPS would provide for wide-ranging changes in DOD's civilian personnel pay and performance management, collective bargaining, rightsizing, and a variety of other human capital areas. The NSPS would enable DOD to develop and implement a consistent, DOD-wide civilian personnel system bringing

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together the many disparate systems that exist today. The proposal, while providing a section-by-section analysis, does not provide an adequate justification given the significance of the proposed changes. In addition, it is my understanding that a document containing a fully developed justification for the proposed changes is not available. At the same time, it is our understanding that DOD's current thinking is that NSPS will be based on the work done by DOD's Human Resources Best Practices Task Force. The Task Force reviewed federal personnel demonstration projects and selected alternative personnel systems to identify practices that it considered promising for a DOD civilian human resources strategy. These practices were outlined in a April 2, 2003, *Federal Register* notice asking for comment on DOD's plan to integrate all of its current science and technology reinvention laboratory demonstration projects under a single human capital framework consistent with the best practices DOD identified.<sup>1</sup>

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

Human capital reforms at DOD obviously have important implications for national security. However, given the massive size of DOD and the nature and scope of the changes that are being considered, DOD's proposal also has important precedent-setting implications for federal human capital management generally and should also be considered in that context. The critical questions raised are should DOD and/or other agencies be granted broad-based exemptions from existing law, and if so, on what basis; and whether they have the institutional infrastructure in place to make effective use of the new authorities. This institutional infrastructure includes, at a minimum, a human capital planning process that integrates the agency's human capital policies, strategies, and programs with its program goals and mission, and desired outcomes; the capabilities to effectively develop and implement a new human capital system; and

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<sup>1</sup>68 *Fed. Reg.* 16,119-16,142 (2003).

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importantly a set of adequate safeguards, including reasonable transparency and appropriate accountability mechanisms, to ensure the fair, effective, and credible implementation and application of a new system.

Consistent with this view, we have long held that the first step toward meeting the government's human capital challenges is for agency leaders to identify and make use of all the appropriate administrative authorities available to them to manage their people for results, undertaken as part of and consistent with proven change management practices. Much of the authority agency leaders need to manage human capital strategically is already available under current laws and regulations. This includes the ability to develop modern, effective, and credible performance management systems that would support more performance-based pay decisions. The second step is for policymakers to pursue incremental legislative reforms to give agencies additional tools and flexibilities to hire, manage, and retain the human capital they need, particularly in critical occupations. The third step is for all interested parties to work together to identify, based in part on the experiences of the incremental reforms and demonstration projects, the kinds of comprehensive legislative reforms in the human capital area that should be enacted over time, taking into account the extent to which existing approaches make sense in the current and future operating environment.<sup>2</sup>

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## Observations on Selected Provisions of the Proposed NSPS

With almost 700,000 civilian employees on its payroll, DOD is the second largest federal employer of civilians in the nation, after the Postal Service. Defense civilian personnel, among other things, develop policy, provide intelligence, manage finances, and acquire and maintain weapon systems. Given the current global war on terrorism, the role of DOD's civilian workforce is expanding, such as participation in combat support functions that free military personnel to focus on warfighting duties for which they are uniquely qualified. Civilian personnel are also key to maintaining DOD's institutional knowledge because of frequent rotations of military personnel. However, since the end of the Cold War, the civilian workforce has undergone substantial change, due primarily to downsizing, base realignments and closures, competitive sourcing initiatives, and DOD's changing missions. For example, between fiscal years 1989 and 2002, DOD

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<sup>2</sup>U.S. General Accounting Office, *Human Capital: Building on the Current Momentum to Address High-Risk Issues*, [GAO-03-637T](#) (Washington, D.C.: April 8, 2003).

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reduced its civilian workforce by about 38 percent, with an additional reduction of about 55,000 personnel proposed through fiscal year 2007. Some DOD officials have expressed concern about a possible shortfall of critical skills because downsizing has resulted in a significant imbalance in the shape, skills, and experience of its civilian workforce while more than 50 percent of the civilian workforce will become eligible to retire in the next 5 years. As a result, the orderly transfer of DOD's institutional knowledge is at risk.

These factors, coupled with the Secretary of Defense's significant transformation initiatives, make it imperative for DOD to strategically manage its civilian workforce based on a total force perspective which includes civilian personnel as well as active duty and reserve military personnel and contractor personnel. This strategic management approach will enable DOD to accomplish its mission by putting the right people in the right place at the right time and at a reasonable cost.

NSPS is intended to be a major component of DOD's efforts to more strategically manage its workforce and respond to current and emerging challenges. This morning I will highlight several of the key provisions of NSPS that in our view are most in need of close scrutiny as Congress considers the DOD proposal.

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## Providing the Wide-Ranging Authority to Design a New Civilian Personnel System

The DOD proposal would allow the Secretary of Defense to jointly prescribe regulations with the Director of the Office of Personnel Management (OPM) to establish a flexible and contemporary human resources management system for DOD—NSPS. The joint issuance of regulations is similar to that set forth in the Homeland Security Act of 2002<sup>3</sup> between the Secretary of Homeland Security and the Director of OPM for the development of the Department of Homeland Security (DHS) human resources management system. However, unlike the legislation creating DHS, the Defense Transformation for the 21st Century Act would allow the Secretary of Defense to waive the requirement for joint issuance of regulations if, in his or her judgment, it is “essential to the national security”—which is not defined in the act. While the act specifies a number of key provisions of Title 5 that shall not be altered or waived, including those concerning veterans' preference, merit protections, and safeguards against discrimination and prohibited personnel practices, the

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<sup>3</sup>Pub. L. No. 107-296, Nov. 25, 2002.

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act nonetheless would, in substance, provide the Secretary of Defense with significant independent authority to develop a separate and largely autonomous human capital system for DOD.

The DOD proposal also has significant potential implications for governmentwide human capital policies and procedures and for OPM as the President's agent and advisor for human capital matters and overseer of federal human capital management activities.<sup>4</sup> In essence, the act would allow for the development of a personnel system for the second largest segment of the federal workforce that is not necessarily within the control or even direct influence of OPM. To strike a better balance between reasonable management flexibility and the need for a reasonable degree of consistency and adequate safeguards to prevent abuse throughout the government, Congress should consider making these provisions of the Defense Transformation for the 21st Century Act consistent with the Homeland Security Act of 2002, or at a minimum, providing some statutory guidance on what would constitute a situation "essential to the national security" that would warrant the Secretary of Defense to act independently of the Director of OPM.

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## Implementing Pay Reform and Performance Management

DOD states that it needs a human capital management system that provides new and increased flexibility in the way it assesses and compensates its employees, and toward that end, we understand that in implementing NSPS DOD plans to strengthen its performance appraisal systems and implement pay banding approaches as core components of any new DOD human capital system. We have a long and successful experience in using pay banding with our analyst staff as a result of the GAO Personnel Act of 1980. Certain DOD components have had a number of years of experience with pay banding through OPM's personnel demonstration projects, authorized by the Civil Service Reform Act of 1978, to test and introduce beneficial change in governmentwide human resources management systems. For example, in 1980, the Navy personnel demonstration project, commonly referred to as the China Lake demonstration project, implemented a number of reforms including pay banding and a pay for performance system. More recently, the Civilian Acquisition Workforce personnel demonstration project (AcqDemo) was

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<sup>4</sup>We discuss OPM's human capital leadership role in our report: *Major Management Challenges and Program Risks: Office of Personnel Management*, [GAO-03-115](#) (Washington, D.C.: January 2003).

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implemented in 1999 and created a pay banding system that covers part of its civilian acquisition, technology, and logistics workforce.<sup>5</sup> The expected results of AcqDemo's pay banding system include increased flexibility to assign employees as well as increased pay potential and satisfaction with advancement for employees. According to agency officials, an evaluation to OPM on AcqDemo's progress is scheduled to be available this June. Lastly, DOD's science and technology reinvention laboratory demonstration projects all implemented some form of pay banding and pay for performance. OPM reports that these reinvention laboratory demonstration projects have been able to offer more competitive starting salaries. Additionally some labs' turnover experience was significantly lower among highly-rated employees and higher among employees with lower ratings.<sup>6</sup> DOD's demonstration projects clearly provide helpful insights and valuable lessons learned in connection with broad banding and pay for performance efforts. At the same time these projects and related DOD efforts involve less than 10 percent of DOD's civilian workforce and expanding these concepts to the entire department will require significant effort and likely need to be implemented in phases over several years.

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

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<sup>5</sup>U.S. General Accounting Office, *Acquisition Workforce: Status of Agency Efforts to Address Future Needs*, [GAO-03-55](#) (Washington, D.C.: Dec. 18, 2002).

<sup>6</sup>U.S. Office of Personnel Management, *2002 Summative Evaluation: DOD S&T Reinvention Laboratory Demonstration Program* (Washington, D.C.: August 2002).



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performance-based pay and other personnel decisions. Unfortunately, based on GAO's past work, most existing federal performance appraisal systems, including a vast majority of DOD's systems, are not designed to support a meaningful performance-based pay system.

The bottom line is that in order to receive any additional performance-based pay flexibility for broad based employee groups, agencies should have to demonstrate that they have modern, effective, credible, and, as appropriate, validated performance management systems in place with adequate safeguards, including reasonable transparency and appropriate accountability mechanisms, to ensure fairness and prevent politicalization and abuse.

At your request Madam Chairwoman, and that of Senator Voinovich, we identified key practices leading public sector organizations both here in the United States and abroad have used in their performance management systems to link organizational goals to individual performance and create a "line of sight" between an individual's activities and organizational results.<sup>7</sup> These practices can help agencies develop and implement performance management systems with the attributes necessary to effectively support pay for performance.

More specifically, Congress should consider establishing statutory standards that an agency must have in place before it can implement broad banding or a more performance-based pay program. As the request of Congressman Danny Davis, we developed an initial list of possible safeguards to help ensure that any additional flexibility Congress may grant for expanding pay for performance management systems in the government are fair, effective, and credible. We provided an initial list to Congressman Davis late last week. This initial list of safeguards was developed based on our extensive body of work looking at the performance management practices used by leading public sector organizations both in the United States and in other countries as well as our own experiences at GAO in implementing a modern performance management system for our own staff. We believe that the following could provide a starting point for developing a set of statutory safeguards in

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<sup>7</sup>U.S. General Accounting Office, *Results-Oriented Cultures: Creating a Clear Linkage between Individual Performance and Organizational Success*, [GAO-03-488](#) (Washington, D.C.: Mar. 14, 2003).

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connection with any additional efforts to expand pay for performance systems.

- Assure that the agency's performance management systems (1) link to the agency's strategic plan, related goals, and desired outcomes, and (2) result in meaningful distinctions in individual employee performance. This should include consideration of critical competencies and achievement of concrete results.
- Involve employees, their representatives, and other stakeholders in the design of the system, including having employees directly involved in validating any related competencies, as appropriate.
- Assure that certain predecisional internal safeguards exist to help achieve the consistency, equity, nondiscrimination, and nonpoliticization of the performance management process (e.g., independent reasonableness reviews by Human Capital Offices and/or Offices of Opportunity and Inclusiveness or their equivalent in connection with the establishment and implementation of a performance appraisal system, as well as reviews of performance rating decisions, pay determinations, and promotion actions before they are finalized to ensure that they are merit-based; internal grievance processes to address employee complaints; and pay panels whose membership is predominately made up of career officials who would consider the results of the performance appraisal process and other information in connection with final pay decisions).
- Assure reasonable transparency and appropriate accountability mechanisms in connection with the results of the performance management process (e.g., publish overall results of performance management and pay decisions while protecting individual confidentiality, and report periodically on internal assessments and employee survey results).

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

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should consider adopting class exemption approaches and OPM should be required to act on any individual certifications within prescribed time frames (e.g., 30-60 days). This approach would allow for a broader-based yet more conceptually consistent approach in this critical area. It would also facilitate a phased-implementation approach throughout government. The list is not intended to cover all the attributes of a modern, results-oriented performance management system. Rather, the items on the list cover possible safeguards for performance management systems to help ensure those systems are fair, effective, and credible.

Congress should also consider establishing a governmentwide fund whereby agencies, based on a sound business case, could apply for funds to modernize their performance management systems and ensure those systems have adequate safeguards to prevent abuse. This approach would serve as a positive step to promote high-performing organizations throughout the federal government while avoiding fragmentation within the executive branch in the critical human capital area.

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## Establishing Senior Executive Service Pay and Performance Management

The Senior Executive Service (SES) needs to lead the way in the federal government's effort to better link pay to performance. We have reported that there are significant opportunities to strengthen efforts to hold senior executives accountable for results.<sup>8</sup> In particular, more progress is needed in explicitly linking senior executive expectations for performance to results-oriented organizational goals and desired outcomes, fostering the necessary collaboration both within and across organizational boundaries to achieve results, and demonstrating a commitment to lead and facilitate change. These expectations for senior executives will be critical to keep agencies focused on transforming their cultures to be more results-oriented, less hierarchical, more integrated, and externally focused and thereby be better positioned to respond to emerging internal and external challenges, improve their performance, and assure their accountability.

Given the state of agencies' performance management systems, Congress should consider starting federal results-oriented pay reform with the SES. In that regard and similar to the Homeland Security Act, the proposed NSPS would increase the current total allowable annual compensation limit for senior executives up to the Vice President's total annual

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<sup>8</sup>U.S. General Accounting Office, *Results-Oriented Cultures: Using Balanced Expectations to Manage Senior Executive Performance*, [GAO-02-966](#) (Washington, D.C.: Sept. 27, 2002).

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compensation. However, the Homeland Security Act provides that OPM, with the concurrence of the Office of Management and Budget, certify that agencies have performance appraisal systems that, as designed and applied, make meaningful distinctions based on relative performance. NSPS does not include such a certification provision. Congress should consider requiring OPM to certify that the DOD SES performance management system makes meaningful distinctions in performance and employs the other practices used by leading organizations to develop effective performance management systems that I mentioned earlier, before DOD could increase the annual compensation limit for senior executives.<sup>9</sup>

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## Employees and Employee Organizations Involvement in Creating NSPS

The proposed Defense Transformation for the 21st Century Act includes provisions intended to ensure collaboration with employee representatives in the planning, development, and implementation of a human resources management system. For example, employee representatives are to be given the opportunity to review and make recommendations on the proposed NSPS. The Secretary of Defense and the Director of OPM are to provide employee representatives with a written description of the proposed system, give these representatives at least 30 calendar days to review and make recommendations on the proposal, and fully and fairly consider each recommendation. DOD may immediately implement the parts of the proposed system that did not receive recommendations or those recommendations they chose to accept from the employee representatives. While these provisions are designed to help assure that employees and their authorized representatives play a meaningful role on the design and implementation of any new human capital system, DOD does not have a good track record in reaching out to key stakeholders. In fact, it is my understanding that neither DOD employees nor their authorized representatives played a meaningful role in connection with the design of the legislative proposal that is the subject of this hearing.

For the recommendations from the employee representatives that the Secretary and the Director do not accept, the Secretary and the Director are to notify Congress and meet and confer with employee representatives in an attempt to reach agreement on how to proceed with these recommendations. If an agreement has not been reached after 30 days, and the Secretary determines that further consultation with employee

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<sup>9</sup>[GAO-03-488](#).

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representatives will not produce agreement, the Secretary may implement any or all parts of the proposal, including any modifications made in response to the recommendations. The Secretary is to notify Congress of the implementation of any part of the proposal, any changes made to the proposal as a result of recommendations from the employee representatives, and the reasons why implementation is appropriate.

Although the procedures called for in the DOD proposal are similar to those enacted in the Homeland Security Act, the latter states explicitly the intent of Congress on the importance for employees to be allowed to participate in a meaningful way in the creation of any human resources management system affecting them. To underscore the importance that Congress places on employee involvement in the development and implementation of NSPS, Congress should consider including similar language as that found in the Homeland Security Act.

More generally, and aside from the specific statutory provisions on consultation, the active involvement of employees will be critical to the success of NSPS. We have reported that the involvement of employees both directly and indirectly is crucial to the success of new initiatives, including implementing a pay for performance system.<sup>10</sup> High-performing organizations have found that actively involving employees and stakeholders, such as unions or other employee associations when developing results-oriented performance management systems helps improve employees' confidence and belief in the fairness of the system and increases their understanding and ownership of organizational goals and objectives. This involvement must be early, active, and continuing if employees are to gain a sense of understanding and ownership for the changes that are being made.

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## Attracting Key Talent

The legislation has a number of provisions designed to give DOD flexibility to help obtain key critical talent. Specifically, it allows DOD greater flexibility to (1) augment the use of temporary appointment authorities, (2) hire experts and consultants and pay them special rates, (3) define benefits for overseas employees, and (4) enter into personal services contracts for experts and consultants for national security missions,

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<sup>10</sup>U.S. General Accounting Office, *Insights for U.S. Agencies from Other Countries' Performance Management Initiatives*, [GAO-02-862](#) (Washington, D.C.: Aug. 2, 2002) and *Human Capital: Practices That Empowered and Involved Employees*, [GAO-01-1070](#) (Washington, D.C.: Sept. 14, 2001).

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including for service outside of the United States. Specifically, the Secretary would have the authority to establish a program to attract highly qualified experts in needed occupations with the flexibility to establish the rate of pay, eligibility for additional payments, and terms of the appointment. These authorities give DOD considerable flexibility to obtain and compensate individuals and exempt them from several provisions of current law. While we have strongly endorsed providing agencies with additional tools and flexibilities to attract and retain needed talent, the broad exemption from some existing ethics and other personnel authorities without prescribed limits on their use raises some concern. Accordingly, Congress should consider placing numerical or percentage limitations on the use of these provisions or otherwise specifically outline basic safeguards to ensure such provisions are used appropriately.

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## Rightsizing and Organizational Alignment

The proposed Defense Transformation for the 21st Century Act would provide the Secretary with a number of broad authorities related to rightsizing and organizational alignment. These include authorizing the Secretary to restructure or reduce the workforce by establishing programs using voluntary early retirement eligibility and separation payments, or both. In addition, the Secretary would be allowed to appoint U.S. citizens who are at least 55 years of age to the excepted service for a period of 2 years, with a possible 2-year extension, subject only to certain provisions preventing displacement of current employees. The proposal also provides that annuitants who receive an annuity from the Civil Service Retirement and Disability Fund and become employed in a position within the Department of Defense shall continue to receive their unreduced annuity. This and selected other NSPS provisions will clearly have incremental budget implications for which we have not seen any related cost estimate. Furthermore, this and other selected NSPS provisions would create an unlevel playing field for experienced talent within the civilian workforce.

Authorities such as voluntary early retirements have proven to be effective tools in strategically managing the shape of the workforce. I have exercised the authority that Congress granted me to offer voluntary early retirements in GAO in both fiscal years 2002 and 2003 as one element of our strategy to shape the GAO workforce. However, given DOD's past efforts in using existing rightsizing tools, there is reason to be concerned that DOD may struggle to effectively manage additional authorities that may be provided. While DOD has used existing authorities in the past to mitigate the adverse effects of force reductions, the approach to reductions was not oriented toward strategically shaping the makeup of the workforce. We have previously reported that the net effect of lack of

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attention to workforce shaping is a civilian workforce that is not balanced by age or experience, which risks the orderly transfer of institutional knowledge.<sup>11</sup> DOD thus may be challenged in using new authorities in a cohesive, integrated way that supports achieving mission results, absent a comprehensive and integrated human capital strategy and workforce plan.

In the past, OPM has managed its authority to reemploy an annuitant with no reduction in annuity on a case-by-case basis. The NSPS proposal, which broadly grants such treatment, raises basic questions about the intent and design of the federal benefits or total compensation of federal employees and obviates the importance of establishing an effective DOD partnership with OPM in prescribing the use of this authority. As noted previously, providing such authority only to DOD would provide DOD a competitive advantage in the market place that would place other agencies at a disadvantage. It would also involve incremental costs that have yet to be estimated. Flexible approaches to shaping the workforce, such as 2-year excepted service appointments, may be helpful in avoiding long-term commitments for short-term requirements, addressing transition gaps, and smoothing outsourcing strategies. At the same time, these authorities represent tools that are not effective on their own, rather they are elements that need to be developed into an effective strategy and aligned with program goals and missions.

The legislation could also allow DOD to revise Reduction-in-Force (RIF) rules to place greater emphasis on an employee's performance. DOD has indicated that it will be considering for application DOD-wide, personnel practices that were identified in the April 2, 2003, *Federal Register* notice. This notice describes revised RIF procedures that change the order in which employees would be retained under a RIF order. Specifically, employees could be placed on a retention list in the following order: type of employment (i.e., permanent, temporary), level of performance, and veterans' preference eligibility (disabled veterans will be given additional priority), which we note would reduce the order in which veterans' preference is currently provided. While we conceptually support revised RIF procedures that involve much greater consideration of an employee's performance, as I pointed out above, agencies must have modern, effective and credible performance management systems in place to properly implement such authorities.

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<sup>11</sup>U.S. General Accounting Office, *Strategic Approach Should Guide DOD Civilian Workforce Management*, [GAO/T-GGD/NSIAD-00-120](#) (Washington, D.C.: Mar. 9, 2000).

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## Establishing Employee Appeals Procedures

The proposed NSPS would allow the Secretary, after consultation with the Merit Systems Protection Board (MSPB), to prescribe regulations providing fair treatment in any appeals brought by DOD employees relating to their employment. The proposal states that the appeals procedures shall ensure due process protections and expeditious handling, to the maximum extent possible. In this regard, the proposal provides that presently applicable appeals procedures should only be modified insofar as such modifications are designed to further the fair, efficient, and expeditious resolution of matters involving DOD employees. This provision is substantially the same as a similar provision in the Homeland Security Act of 2002 allowing DHS to prescribe regulations for employee appeals related to their employment. As required of the Secretary of DHS, the Secretary of Defense would be required to consult with MSPB prior to issuing regulations. However, neither the Homeland Security Act nor the proposed legislation expressly requires that employee appeals be heard and decided by the MSPB. There is also no express provision for judicial review of decisions regarding employee appeals decisions.

Given the transparency of the federal system dispute resolution and its attendant case law, the rights and obligations of the various parties involved is well developed. It is critical that any due process changes that are implemented after consultation with MSPB result in dispute resolution processes that are not only fair and efficient but, as importantly, minimize any possible perception of unfairness.

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## Building the Institutional Infrastructure Needed to Support NSPS

The critical need for an institutional infrastructure to develop and support change has been a consistent theme raised throughout the observations I have been providing on some of the specific aspects of the proposed NSPS. This institutional infrastructure includes, at a minimum, a human capital planning process that integrates the department's human capital policies, strategies, and programs with DOD's mission, goals, and desired outcomes; the capabilities to effectively develop and implement a new human capital system; and a set of adequate safeguards, including reasonable transparency and appropriate accountability mechanisms to ensure the fair and merit-based implementation and application of a new system. Quite simply, in the absence of the right institutional infrastructure, granting additional human capital authorities will provide little advantage and could actually end up doing damage if the new flexibilities are not implemented properly. Our work looking at DOD's strategic human capital planning efforts and our work looking across the federal government at the use of human capital flexibilities and related



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human capital efforts underscores the critical steps that DOD needs to take to properly develop and effectively implement any new personnel authorities.

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## Strategic Human Capital Planning at DOD

Our work here and abroad has consistently demonstrated that leading organizations align their human capital approaches, policies, strategies, and programs with their mission and programmatic goals. Human capital plans that are aligned with mission and program goals integrate the achievement of human capital objectives with the agency's strategic and program goals. Careful and thoughtful human capital planning efforts are critical to making intelligent competitive sourcing decisions. The Commercial Activities Panel, which I was privileged to chair, called for federal sourcing policy to be "consistent with human capital practices designed to attract, motivate, retain, and reward a high performing workforce" and highlighted a number of human capital approaches to help achieve that objective.<sup>12</sup>

In April 2002, DOD published a strategic plan for civilian personnel.<sup>13</sup> However, as we reported in March 2003,<sup>14</sup> top-level leadership at the department and the component levels has not until recently been extensively involved in strategic planning for civilian personnel; however, civilian personnel issues appear to be a higher priority for top-level leaders today than in the past. Although DOD began downsizing its civilian workforce more than a decade ago, top-level leadership has not, until recently, developed and directed reforms to improve planning for civilian personnel. With the exception of the Army and the Air Force, neither the department nor the components in our March review had developed

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<sup>12</sup>Commercial Activities Panel, *Improving the Sourcing Decisions of the Government* (Washington, D.C.: April 2002).

<sup>13</sup>*Civilian Human Resources Strategic Plan 2002-2008*. At this time, DOD also published two strategic plans for military personnel (one addressing military personnel priorities and one addressing quality of life issues for service members and their families). In a December 2002 report (*Military Personnel: Oversight Process Needed to Help Maintain Momentum of DOD's Strategic Human Capital Planning*, [GAO-03-237](#)), we addressed aspects of the two plans concerning benefits for active duty military personnel, noting that the plans were incomplete and that DOD needed a process to oversee the plans' implementation.

<sup>14</sup>U.S. General Accounting Office, *DOD Personnel: DOD Actions Needed to Strengthen Civilian Human Capital Strategic Planning and Integration with Military Personnel and Sourcing Decisions*, [GAO-03-475](#) (Washington, D.C.: Mar. 28, 2003) and *DOD Personnel: DOD Comments on GAO's Report on DOD's Civilian Human Capital Strategic Planning*, [GAO-03-690R](#) (Washington, D.C.: Apr. 18, 2003).

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strategic plans to address challenges affecting the civilian workforce until 2001 or 2002, which is indicative of civilian personnel issues being an emerging priority.

In addition, we reported that top-level leaders in the Air Force, the Marine Corps, the Defense Contract Management Agency, and the Defense Finance and Accounting Service have been or are working in partnership with their civilian human capital professionals to develop and implement civilian strategic plans; such partnership is increasing in the Army and not as evident in the Navy. Moreover, DOD's issuance of its departmentwide civilian human capital plan begins to lay a foundation for strategically addressing civilian human capital issues; however, DOD has not provided guidance on aligning the component-level plans with the department-level plan to obtain a coordinated focus to carry out the Secretary of Defense's transformation initiatives in an effective manner. High-level leadership attention is critical to developing and directing reforms because, without the overarching perspective of such leaders as Chief Operating Officers and the Chief Human Capital Officers, reforms may not be sufficiently focused on mission accomplishment, and without their support, reforms may not receive the resources needed for successful implementation. We have previously reported that the concept of a Chief Operating Officer (COO) could offer the leadership to help elevate attention on key management issues and transformational change, integrate these various efforts, and institutionalize accountability for addressing management issues and leading transformational change both within and between administrations.<sup>15</sup> In our view, DOD is a prime candidate to adopt this COO concept. In addition, if Congress provides DOD with many of the flexibilities it is seeking under the NSPS, the basis for adding a COO position at DOD would be even stronger.

Despite the progress that has been made recently, the DOD human capital strategic plans we reviewed, for the most part, were not fully aligned with the overall mission of the department or respective components, results oriented, or based on data about the future civilian workforce. For example, the goals and objectives contained in strategic plans for civilian personnel were not explicitly aligned with the overarching missions of the respective organizations. Consequently, it is difficult to determine whether

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<sup>15</sup>U.S. General Accounting Office, *Highlights of a GAO Roundtable: The Chief Operating Officer Concept: A Potential Strategy To Address Federal Governance Challenges*, [GAO-03-192SP](#) (Washington, D.C.: Oct. 4, 2002).

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DOD's and the components' strategic goals are properly focused on mission achievement. In addition, none of the plans contained results-oriented performance measures that could provide meaningful data critical to measuring the results of their civilian human capital initiatives (i.e., programs, policies, and processes). Thus, DOD and the components cannot gauge the extent to which their human capital initiatives contribute to achieving their organizations' mission. Also, for the most part, the civilian human capital plans in our review did not contain detailed information on the skills and competencies needed to successfully accomplish future missions. Without information about what is needed in the future workforce, it is unclear if DOD and its components are designing and funding initiatives that are efficient and effective in accomplishing the mission, and ultimately contributing to force readiness.

Lastly, the DOD civilian strategic plans we reviewed did not address how the civilian workforce will be integrated with their military counterparts or with sourcing initiatives. At the department level, the strategic plan for civilian personnel was prepared separately from corresponding plans for military personnel and not integrated to form a seamless and comprehensive strategy and did not address how DOD plans to link its human capital initiatives with its sourcing plans, such as efforts to outsource non-core responsibilities. For the most part, at the component level, the plans set goals to integrate planning for the total workforce, to include civilian, military, and contractor personnel. The Air Force and the Army, in particular, have begun to integrate their strategic planning efforts for civilian and military personnel, also taking contractor responsibilities into consideration. Without integrated planning, goals for shaping and deploying civilian, military, and contractor personnel may not be consistent with and support each other. Consequently, DOD and its components may not have the workforce with the skills and competencies needed to accomplish tasks critical to assuring readiness and achieving mission success.

In our March report we recommended, among other things, that DOD improve future revisions and updates to the departmentwide strategic human capital plan by more explicitly aligning its elements with DOD's overarching mission, including performance measures, and focusing on future workforce needs. DOD only partially concurred with our recommendation, and, as explanation, stated that the recommendation did not recognize the involvement in and impact of DOD's Quadrennial Defense Review on the development of the departmentwide plan. We also recommended that DOD develop a departmentwide human capital strategic plan that integrates both military and civilian workforces and

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takes into account contractor roles and sourcing initiatives. DOD did not concur with this recommendation stating that it has both a military and civilian plan, and the use of contractors is just another tool to accomplish the mission, not a separate workforce with separate needs to manage. The intent of our recommendation is not to say that DOD has a direct responsibility to manage contractor employees, but rather to recognize that strategic planning for the civilian workforce should be undertaken in the context of the total force—civilian, military, and contractors—since the three workforces need to perform their responsibilities in a seamless manner to accomplish DOD’s mission. In commenting on our recommendations, the Under Secretary of Defense for Personnel and Readiness stated that DOD is in the early stages of its strategic planning efforts. We recognize this and believe that our recommendations represent opportunities that exist to strengthen its developing planning efforts.

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## The Capabilities Needed to Effectively Develop and Implement Human Capital Flexibilities

Our work has identified a set of key practices that appear to be central to the effective use of human capital authorities. These practices, which are shown in figure 1, center on effective planning and targeted investments, involvement and training, and accountability and cultural change.<sup>16</sup>

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<sup>16</sup> U.S. General Accounting Office, *Human Capital: Effective Use of Flexibilities Can Assist Agencies in Managing Their Workforces*, [GAO-03-2](#) (Washington, D.C.: Dec. 6, 2002).

**Figure 1: Key Practices for Effective Use of Human Capital Flexibilities**

<b>Plan strategically and make targeted investments</b>	<ul style="list-style-type: none"> <li>• Obtain agency leadership commitment</li> <li>• Determine agency workforce needs using fact-based analysis</li> <li>• Develop strategies that employ appropriate flexibilities to meet workforce needs</li> <li>• Make appropriate funding available</li> </ul>
<b>Ensure stakeholder input in developing policies and procedures</b>	<ul style="list-style-type: none"> <li>• Engage the human capital office</li> <li>• Engage agency managers and supervisors</li> <li>• Involve employees and unions</li> <li>• Use input to establish clear, documented, and transparent policies and procedures</li> </ul>
<b>Educate managers and employees on the availability and use of flexibilities</b>	<ul style="list-style-type: none"> <li>• Train human capital staff</li> <li>• Educate agency managers and supervisors on existence and use of flexibilities</li> <li>• Inform employees of procedures and rights</li> </ul>
<b>Streamline and improve administrative processes</b>	<ul style="list-style-type: none"> <li>• Ascertain the source of existing requirements</li> <li>• Reevaluate administrative approval processes for greater efficiency</li> <li>• Replicate proven successes of others</li> </ul>
<b>Build transparency and accountability into the system</b>	<ul style="list-style-type: none"> <li>• Delegate authority to use flexibilities to appropriate levels within the agency</li> <li>• Hold managers and supervisors directly accountable</li> <li>• Apply policies and procedures consistently</li> </ul>
<b>Change the organizational culture</b>	<ul style="list-style-type: none"> <li>• Ensure involvement of senior human capital managers in key decision-making processes</li> <li>• Encourage greater acceptance of prudent risk taking and organizational change</li> <li>• Recognize differences in individual job performance and competencies</li> </ul>

Source: GAO.

Congress should consider the extent to which an agency is capable of employing these practices before additional human capital flexibilities are implemented. In the context of NSPS, Congress should consider whether and to what extent DOD is using those practices.

### **Adequate Safeguards, Reasonable Transparency, and Appropriate Accountability**

I have discussed throughout my statement today the importance of moving to a new human capital system which provides reasonable management flexibility along with adequate safeguards, reasonable transparency, and appropriate accountability mechanisms to prevent abuse of employees. In addition to the suggestions made above, Congress should consider requiring DOD to fully track and periodically report on its performance. This requirement would be fully consistent with those contained in our

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calendar year 2000 human capital legislation, which required us to comprehensively assess our use of the authorities granted to us under the act.<sup>17</sup> More generally, Congress should consider requiring DOD to undertake evaluations that are broadly modeled on the evaluation requirements of OPM's personnel demonstration program. Under the demonstration project authority, agencies must evaluate and periodically report on results, implementation of the demonstration project, cost and benefits, impacts on veterans and other EEO groups, adherence to merit principles, and extent to which the lessons from the project can be applied elsewhere, including governmentwide. This evaluation and reporting requirement would facilitate congressional oversight of NSPS, allow for any mid-course corrections in its implementation, and serve as a tool for documenting best practices and sharing lessons learned with employees, stakeholders, other federal agencies, and the public. DOD has stated that it would continue its evaluation of the science and technology reinvention laboratory demonstration projects when they are integrated under a single human capital framework.

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## Concluding Observations

In summary, DOD's civilian human capital proposals raise several critical questions. Should DOD and/or other federal agencies be granted broad-based exemptions from existing law, and if so, on what basis? Does DOD have the institutional infrastructure in place to make effective use of the new authorities? This institutional infrastructure includes, at a minimum, a human capital planning process that integrates the agency's human capital policies, strategies, and programs with its program goals and mission, and desired outcomes; the capabilities to effectively develop and implement a new human capital system; and a set of adequate safeguards, including reasonable transparency and appropriate accountability mechanisms to ensure the fair, effective, and credible implementation and application of a new system.

Many of the basic principles underlying DOD's civilian human capital proposals have merit and deserve the serious consideration they are receiving here today and will no doubt be received by others in the coming

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<sup>17</sup>Our October 2000 legislation gave us tools to realign our workforce in light of mission needs and overall budgetary constraints; correct skills imbalances; and reduce high-grade, managerial, or supervisory positions without reducing the overall number of GAO employees. This legislation allowed us to create a technical and scientific career track at a compensation level consistent to the SES. It also allowed us to give greater consideration to performance and employee skills and knowledge in any RIF actions.

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weeks and months. However, the same critical questions should be posed to the DOD proposal. Should DOD and/or other federal agencies be granted broad-based exemptions from existing law, and if so, on what basis? In addition, Congress and DOD should carefully assess the degree to which DOD has the institutional infrastructure in place to make effective use the new authorities it is seeking. Our work has shown that while progress has been and is being made, additional efforts are needed by DOD to integrate its human capital planning process with the department's program goals and mission. The practices that have been shown to be critical to the effective use of flexibilities provide a validated roadmap for DOD and Congress to consider. Finally, as I have pointed out in several key areas, Congress should consider, if the authorities are granted, establishing additional safeguards to ensure the fair, merit-based, transparent, and accountable implementation and application of NSPS.

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

This morning, I have offered some preliminary observations on some aspects of the proposal. However, these preliminary observations have not included some serious concerns I have with other sections of the proposed legislation that go beyond the civilian personnel proposal. My observations have included suggestions for how Congress can help DOD effectively address its human capital challenges and ensure that NSPS is designed and implemented in an effective, efficient, and fair manner that meets the current and future needs of DOD, its employees, and the American people. Human capital reforms at DOD obviously have important implications for national security and precedent-setting implications for governmentwide human capital management. Given the massive size of DOD and the magnitude of the nature and scope of the changes that are being considered, such reform at DOD also has important precedent-setting

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implications for federal human capital management generally and should be considered in that context.

We look forward to continuing to support Congress and work with DOD in addressing the vital transformation challenges it faces. Madam Chairwoman and Mr. Davis, this concludes my prepared statement. I would be pleased to respond to any questions that you may have.

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## Contacts and Acknowledgments

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