especially evident in government, where staff may serve many masters: chief executives, legislators, political appointees, judges, and senior career executives.

The university researchers do not claim that incentives are not effective under the right conditions, but only that "ideal conditions are rarely met in empirical reality" (Bohnet & Eaton, 2003, p. 251). They endorse the belief that "the rising and falling tides of interest in the various incentive plans have more to do with changing social, political, and economic fashions than with accumulating scientific evidence on how well the plans work" (Blinder, as cited in Bohnet & Eaton, 2003, p. 241). Nonetheless, most managers, for motivation and cost-control reasons, believe that performance should be an important part of the compensation system. More than 80 percent of nearly 1,000 private firms surveyed in 2003 said that they "pay for performance," although often for small parts of their workforces (Hewitt Associates, 2003).

A meta-analysis of 39 empirical research projects in the private sector found that financial incentives were not related to performance quality (Jenkins, Mitra, Gupta, & Shaw, 1998). Indeed, in 2004 Harvard University Press published a book on business executive compensation titled *Pay Without Performance* (Bebchuk & Fried, 2004; also see Baker & Schieder, 2018). Lane, Wolf, and Woodard (2003) assert that "there is an utter lack of empirical evidence in the private and public sectors that pay for performance has any positive effect on either morale or productivity" (p. 138). Careful investigation—not intuitive reasoning, common sense, and misguided confidence—is needed to understand how performance pay operates, as managers often have little in-depth understanding of compensation complexities (Ariely, 2010, p. 37).

Pay-for-performance programs, in short, are deceptively difficult to achieve, both technically and politically. The idea of paying for performance may be good in principle but difficult to enact, as indicated by past experience with the federal general pay schedule as well as reform attempts in the 1970s, 1980s, 1990s, and into this this century. First, as Gage and Kelly (2003) point out, the federal GS is, in fact, a performance-based system that has never been correctly implemented. Supervisors do not take advantage of available incentives—cash awards, within-grade increases, quality step increases—because there are insufficient funds for them to do so. When this traditional approach was nonetheless modified to emphasize incentive pay, it had to be repealed as unworkable.

Second, as Risher (2002) notes, performance compensation was tried "first for managers under the Civil Service Reform Act of 1978 and then under the Performance Management and Recognition Act starting in 1984. [The] experience was so bad. . . . that [the laws] were allowed to sunset. . . . and the idea of pay for performance was all but forgotten" (p. 318). These attempts led to consternation and delay, paperwork, and appeals, and they cost more money while still not rewarding the best employees. Third, in 1996, the Federal Aviation Administration implemented pay for performance. By 2004, it was dubbed *a failure* that led to inequity and poor morale (Kauffman, 2004).

Fourth, following the implementation of a *best practices* reform program at the U.S. Government Accountability Office, it was reported that 81 percent of employees believed that morale was worse than before pay restructuring (Ballenstedt, 2008b). Another program once viewed as a model for the rest of government, that of the Senior Executive Service, was found after four years to have little effect on performance while hastening retirements and discouraging midlevel managers from applying to the SES. The U.S. Department of Homeland Security's MaxHR program as well as the Department of Defense's national security personnel system produced so many productivity problems, court defeats, and widespread dissatisfaction that both abandoned pay for performance (Haga,

(Countined)

(Countined)

Richman, & Leavitt, 2010; Tiefer, 2008). To date, no one has developed lessons from these failures.

In a triumph of hope over experience, pay for performance nonetheless remains as popular in management circles as ever. Thus, the 16 agencies constituting the intelligence community began implementing pay for performance in 2008, building on a little-known effort by the National Geospatial Intelligence Agency—a program that, according to the National Academy of Public Administration, had no influence on productivity or performance (Losey, 2010). In addition, an OPM report claimed success for the federal government's pay incentive plans, lauded more than 25 years of successful experiments with all existing alternative pay systems, and later announced performance pay pilot projects at five agencies (Walker, 2008).

A union official, however, noted, "The patchwork of pay programs across government cannot be collectively or individually characterized as a success; the reality is that each is terribly flawed," leading to increases in grievances, litigation, attrition rates, and low morale (quoted in Walker, 2008). At the Federal Deposit Insurance Corporation, for example, just 12 percent of employees believed that pay for performance reflected actual performance. Indeed, an arbitrator ruled that the Securities and Exchange Commission performance pay plan discriminated on the basis of sex and race (Ballenstedt, 2008a). An influential congressman, nonetheless, declared his intent to establish a pay-for-performance program for all federal employees based on a U.S. Postal Service program, an initiative that is under investigation for its problematic nature (Losey, 2011a).

At best, it remains to be seen if these initiatives will overcome inherent problems typically found in these incentive plans. Even Howard Risher (2004), in an enthusiastic endorsement of performance pay, admits that the technique "may well prove to be the most difficult change any organization has ever attempted" (p. 46). As if to make the point, he offers no fewer than 29 recommendations.

Not to be overlooked, the National Institute of Standards and Technology reported that its long-standing pay-for-performance project has enabled the institute to "compete more effectively for top talent, retain more of its high performers, and expand managers' authority over hiring and pay decisions" (Kirkner, 2008, p. 23). The National Geospatial Intelligence Agency has a two-decade old, award-winning initiative (Risher, 2018c; Tobenkin, 2018). Hays (2004), in addition, has written about two cases in state and local jurisdictions where the approach apparently works. The state of Tennessee has a performance pay program (Risher, 2017b) as well as the City of Charlotte, NC. To be workable, the plans must be well designed, meet expectations for pay gains, and be implemented in an atmosphere of high trust and employee morale. Such success stories tend to be isolated, temporary, and/or constrained; if confirmed by independent research, they must nonetheless contend with a substantial body of evidence on performance pay failure. As the U.S. Merit Systems Protection Board (2006) stipulates, these systems can be effective only if the following factors are present:

- A supportive organizational culture
- Fair-minded, well-trained supervisors
- A rigorous performance appraisal system
- A system of checks and balances
- An ongoing system of program evaluation

One expert recommends that pay for performance be introduced first for managers. Among the criteria that should drive their salary increases is their mastery of the skills needed to manage employee performance.

While an organization's compensation system reinforces good performance, the focus on pay for performance, paradoxically, should not emphasize only money. Incentive compensation is neither quick nor easy. Other factors—public service motivation, good management, importance of work—affect job satisfaction; many professionals do not work for profits, stock values, or commissions. Jauhar (2008) provides an account, and a devastating critique, of the unintended consequences that can happen when physicians are paid for performance (also refer to Bolotnikova, 2016).

As Perry (2003) observes, "The reality is that pay for performance is likely to be of little benefit to organizations with serious performance problems and may actually be harmful" (p. 150). If not well implemented, a demoralized, embittered, unmotivated workforce can result. Brown and Heywood (2002, p. 10) cite an official who identified two common attributes of these plans—they involve huge amounts of management time and make everyone unhappy. Indeed, pay-for-performance programs—since they are often required to be *budget neutral*—can become an excuse to resist fair pay in the first place. Money can get people to work, but it cannot get people to want to work. The evidence suggests that incentives are seen as bribes and thereby reduce employees' self-respect. According to a federal incentive pay consultant, reform-minded officials should look at the culture of the agency, the kind of work it does, and the resources needed to deploy a new program. "Instead of saying, 'we want [it] because everyone else has it,' agencies should ask themselves, 'What are we trying to accomplish?'" (Hewitt Associates, 2003, p. 6).

Sources: Ariely (2010); Ballenstadt (2008a); Bohnet & Eaton (2003); Brown & Heywood (2002); Gage & Kelly (2003); Hays (2004); Hewitt Associates (2003); Jauhar (2008); Jenkins et al. (1998); Kauffman (2004, 2005); Kellough & Selden (1997); Kirkner (2008); Losey (2010, 2011a); Perry (2003); Risher (2002, 2004); Tiefer (2008); Walker (2008); Zeller (2004).

Merit Pay

Like longevity pay, **merit pay** involves annual incremental increases to base salary, an annuity that compounds for as long as the employee remains with the department. In *true* merit systems, managers have flexibility about who gets how much (not just when there are grade or classification promotions). Typically, organizations opt for either a longevity or a merit category, although raises may use both criteria simultaneously. One common practice, noted earlier, is to divide the pool of funds for raises into COLAs and merit. However, sometimes merit is designated as the sole determinant; in such cases, the portion going to performance is in lieu of the cost-of-living portion and longevity is implicitly eliminated. Those who are underperforming receive no merit, but generally, those individuals would be deprived of their step increases in most step systems as well. Merit systems jurisdictions may use pay ranges rather than steps for job classifications and their related grades, with minimums, midpoints, and maximums. The important feature is that the amount paid out is at the administrator's discretion. New employees are expected to start at the minimum pay in the range, but line managers may have more discretion than in step systems. In addition, most merit systems have fewer grades and move to broader pay bands with more than a 40 percent span rather than the 20 percent to 35 percent range more typical in step systems.

The use of merit has an intuitive attractiveness supported by conventional wisdom as well as leading motivation theories (economic, need, expectancy): Incentives lead to improved performance. Increases are based on managers' decisions relating to the quantitative and qualitative factors of employment (e.g., amount of results, accuracy of results). The explicit values of merit pay are competition and promotion of individual striving. The implicit values are that significant pay inequality is fair and that individual contributions are more important than teamwork.

It is not surprising that public and private organizations claim to give great deference to merit; the civil service is even named for it. A substantial discontinuity exists, nevertheless, between rhetoric and reality, as merit pay (outside of sales and commissions jobs) "may not be as desirable, as easy to implement, or as widely used as commonly believed" (Fisher, Schoenfeldt, & Shaw, 2006, p. 512).[9] In the national government, the results are at best disappointing (Kellough & Lu, 1993; Perry, Engbers, & Jun, 2009). The cardinal paradox is that performance pay is offered as a replacement for traditional pay systems that themselves are supposed to be merit based. That is, there is nothing under those approaches that obligates managers to give time-in-grade raises. Thus, while merit pay is a powerful cultural symbol and a source of control for managers over employees, they are reluctant to use it (Bowman, 2010).

For merit pay systems to be successful, certain conditions must be present: trust in management, a valid job evaluation system, clear performance factors, meaningful and consistent funding, and accurate personnel appraisal (Chapter 10). Even if these exist, merit compensation may perversely focus on the short term at the expense of the long term, encourage mediocrity by setting limits on expectations, reduce creativity and risk taking, promote self-interest above other interests, destroy teamwork by increasing dependence on individual accomplishment, generate counterproductive win–lose competition among employees for merit monies, encourage sycophancy ("do as I say performance pay"), and generally politicize the compensation system. Employees may "eventually come to see merit pay as a kind of punishment" (Gabris & Ihrke, 2004, p. 504), as rewards ultimately penalize employees when they are not received.

Merit pay, in theory, has the potential to produce high performance, but in practice it is difficult to administer in a way that personnel perceive as fair, as the example below illustrates:

> When a municipal government received political pressure to implement a pay plan, the city manager and professional staff contracted a consultant to develop a first-rate, by-the-book, technically sophisticated design. This new system should have worked.
>
> Originally, the total money available from the compensation pool was to be divided, with about 60 percent going for cost-of-living adjustments and automatic pay increases and 40 percent reserved for merit pay. When the elected officials heard this, they reversed the formula to 75 percent reserved for merit pay and 25 percent for cost-of-living increases. These political officials clearly wanted a strong merit message sent to employees.
>
> The city's employees resisted such intense merit pay strategies, and the police department, to avoid the merit program, unionized that same year. After the efforts of cooler heads and the making of various compromises, the merit

> distribution went back more or less to the original 60–40 split. Why was this so important to the rank-and-file employees? Why did they not want more resources put into the merit pool on the premise that if they performed well, they stood to receive considerable pay increases?
>
> By and large, these employees, like others in the public sector, were more concerned with external and internal equity than with individual equity. Merit raises, although helping, usually do not bring public agency base salaries up to market. What happens instead is that employees find their base salaries compressed in relation to what the market would currently pay someone with their level of skills and experience. This **pay compression** happens when people stay in the same jobs for long durations, receiving generally small base salary increases and only periodic merit raises. Ineluctably, these workers find new hires starting with base salaries not much below, and even in some cases above (pay inversion), their salaries. (Gabris, 1998, p. 649; emphasis added)

Even business admirers like Risher and Fay (1997) have concluded:

> Despite policy statements that make individual merit important, salaries have been managed in a lock step manner. [. . .] The most aggressive corporate programs rarely give meaningful recognition to outstanding employees. The underlying merit philosophy is solidly entrenched. [. . .] but the typical private sector employee can expect an annual salary increase with almost as much certainty as the typical public sector employee. (pp. 3, 43)

In order for a merit pay system to operate as advocated, the differences in pay must be substantial. For example, given a pool of dollars for distribution, the top 10 percent of employees get a 10 percent raise, 60 percent of employees get 5 percent, and 30 percent of employees do not get any raise. Such a system is motivating for those who are in the top group, there will be mixed reactions in the middle group (some will be satisfied, but since most people think they are above average, there may be resentment), and there will most likely be dejection and anger in the lowest group.

Overall, merit plans seldom provide enough funds to reward exceptional employees without unfairly penalizing valued satisfactory ones. It is a major administrative challenge for an organization to continuously reevaluate motivation and productivity, to identify the additional level of performance that warrants special recognition, and to provide those incentives on an equitable and timely basis. Bob Behn (n.d.; also see Behn, 2004) identifies more than 20 key design and perceptual issues found in these programs: who gets rewarded (e.g., eight design questions based on rewarding individuals and/or teams), the nature of the reward (four questions on whether the reward is intrinsic or extrinsic; if the latter, what is its size, is it a one-time bonus or added to base pay, and what is the source of funds?), what is rewarded (eight questions on how rewards are determined), and how the plan is perceived (three questions on advocates' motivation, whether the plan appears to reward or punish, and whether the plan is regarded as fair).

Merit pay, in short, should never be oversold as a panacea for organizational problems; if used, it should be merely one part of the compensation system (Gabris & Ihrke, 2004, p. 506). So long as government salaries are inconsistent with the expectations of job candidates, those motivated by money will find better alignment of individual and organizational needs in the for-profit sector. Performance pay, even well implemented, cannot address such inconsistencies. It is easy to understand why simpler, *set-it-and-forget-it* compensation systems are so widespread. Indeed, it is telling that performance pay promoters have not sought to apply the technique to presidents, members of Congress, agency secretaries, or the uniformed services. Further, it is not surprising that among the many techniques employed by Sloan workplace award winners, performance pay is not one of them (Galinsky & Eby, 2008). As well, two important books on civil service reform reject pay for performance (Bilmes & Gould, 2009; Donahue, 2008).

In spite of—or perhaps because of—these problems, there is no indication that decision makers are ready to abandon merit pay, an idea that has become a kind of management's *fool's gold*.[10] Indeed, OPM, the second National Commission on Public Service (Volcker II), and the National Academy of Public Administration have recommended a new federal governmentwide compensation system.[11] Widespread and consistently discouraging results inevitably raise questions about the efficacy of performance pay itself. Undaunted, compensation reformers, as a result, sometimes resort to tactics like (Don't Abandon Performance-Based Pay, 2007; National Academy of Public Administration, 2004; Partnership for Public Service, 2005; Risher, 2008; Schuster & Zingheim, 2007):

- Suggesting that technical concerns deflect attention from performance;
- Conceding that the evidence does not confirm that pay enhances performance;
- Claiming that alternatives are worse;
- Blaming critics for not creating better compensation systems;
- Arguing that pay for performance is not actually that important since it is not an end in itself; and
- Declaring that the real problem is not pay at all, but rather personnel appraisal, performance management, *communication*, or something else.

However ingenious (or disingenuous) and wishful (or desperate) these arguments might be, they are certainly effective in the realpolitik of public pay plans. There is a deeply ingrained belief in pay for performance, one encouraged by vendors promising that however difficult the technique may be it nevertheless can be done with their guidance. A pretense of assumed future benefits seems better than the prospect of exposing actual past and present failures.

Officials are generally reluctant to admit mistakes, and administrators tend to use merit monies to reward things other than performance (see below and Chapter 10). Performance pay can become a substitute for good management: Manipulating compensation packages is far easier than designing meaningful jobs and paying everyone fairly. Merit is simply too oceanic a social myth to reject outright; to do so would suggest that individuals do not make a difference. Instead, as Gabris (1998) suggests, because merit plans fixate on individual equity, every effort should be made to ensure that the total compensation system strives to align individual, internal, and external equities. This balance must include attention both to how much people receive (distributive justice) and to the processes used to decide how much (procedural justice). Failure to address these issues exacerbates the vicious, visible, and vital aspects of pay, a topic about which few hold neutral feelings.

Skill-Based Pay

Criticisms of merit schemes have triggered a high level of interest in **skill-based pay** (also known as knowledge or competency pay). Such plans analyze the job knowledge a competent employee needs to possess. As new skills are learned, used, and demonstrated by results, employees qualify for salary increments.

Skill compensation can be consistent with longevity and/or merit principles and is compatible with broad pay banding because employees are recognized for gaining additional competencies in a wide array of job practices. It is person centered rather than job centered because, unlike job evaluation, it focuses on how well the individual is doing the job, not on how well the job is defined. For example, the Riverside, California, police department provides pay increases for becoming bilingual, qualifying for the sniper team, and learning hostage negotiation skills. Skill-based pay is common in education (e.g., substantial increases in pay for a master's, master's + 30 credits, various certifications), public safety (e.g., courses and certifications for firefighters in emergency medical training, aerial operations, trench rescue, associate's, bachelor's, and master's degrees), health, and other areas where constant skill upgrading is important. The state of California has five pay ranges for psychologists depending on whether incumbents have a master's degree only, two years of doctoral work, three years of doctoral work, three years of doctoral work plus the completion of comprehensive exams (indicating work on a dissertation), or the completion of a doctoral degree.

The technique of basing pay on skill promises to improve productivity: Instead of focusing on minimal qualifications, it emphasizes competencies that a fully performing, multiskilled employee is expected to demonstrate. In so doing, it specifies what the organization needs (a capable, flexible workforce) and what people want (control over compensation and job success). As an added benefit, it also helps resolve a nettlesome problem for both employers and employees—that of traditional performance appraisal (Chapter 10), as the individual either does or does not progress in skill level. It should be noted that this form of pay may add to labor costs, at least in the short run, until increased productivity manifests itself.

Although few studies have validated skill-based pay systems, they are growing in popularity, especially in organizations that focus on participatory management and teamwork. Englewood, Colorado, for example, has developed a skill-based pay system that updated all job descriptions, verified each job position's current salary, and formulated career development plans. Implementation of the strategy involved developing a new pay line (determining the skill bases for jobs and assigning a monetary value to each skill category), establishing an individualized career development program for employees, and giving employees a choice as to whether or not they would participate in the plan. The program resulted in higher individual satisfaction, better-defined personal and professional goals, increased employee empowerment, and cost-effectiveness (Leonard, 1995).

The Virginia Department of Transportation's skill-based program failed, however, because it lacked supervisory or union support, compelled all employees to participate (many of whom then complained to legislators), and neglected to redesign human resource systems needed to support the change (e.g., classification and appraisal). A significant factor was the use of business consultants who did not understand the sensitive political milieu in which the agency operated (Shareef, 2002). Between the experiences of the Englewood and Virginia programs are those of the Veterans Benefits Administration, the Federal Aviation Administration, and the North Carolina State Transportation Department, each of which had to undertake major changes in their skill-based initiatives to make them work (Thompson & LeHew, 2002).

These plans are not, then, a panacea for two reasons. First, intrinsic concerns include the frustration that occurs when newly achieved skills go unused or when employees *top out* of the program with no further opportunity to earn raises, as well as the complex bureaucratic processes that are likely to develop to monitor and certify employee progress. Second, extrinsic impacts include effects on complementary personnel functions (short-term training and long-term payroll costs increase) and the dynamic political atmosphere (electoral cycles, employees as voters, unions, rank-and-file versus managerial pay).[12] Note also that it is far more difficult to determine external equity in this approach to pay.

Bonus Programs

As noted earlier, when employees receive a temporary pay increase, a type of bonus program is in effect (Exhibit 7.9). Payouts can be awarded based on high levels of individual productivity (performance awards) or can result from the distribution of savings to the organization (gainsharing, where the benefits are disbursed to groups or even whole organizations).

Exhibit 7.9 Employee Bonuses: Compensatory, Contemptible, or Comical?

Money costs too much.

—Ralph Waldo Emerson

A growing compensation trend is the use of bonuses, one-time payments sometimes made instead of awarding more costly permanent pay increases. To encourage high performance, the payouts must be noticeable—at least 10 percent of salary is common in Europe—because smaller amounts may be demoralizing and counterproductive. For the organization, this technique provides an economical, flexible method to control salary expenditures but nonetheless still reward employees. For the individual, one lump sum may seem like more money than a comparably sized raise spread over an entire year. At least in the short run, then, bonuses appear to resolve the paradox of needs.

Unfortunately, such plans are subject to political processes that frequently undermine them because the politicization of compensation often results in program underfunding. Administrators, then, are faced with two unattractive options: giving a few employees relatively large amounts and other deserving staff nothing, or providing virtually everyone with trivial rewards. At the federal level, the average award in 2007 was $577; most personnel believe that their agencies' programs do not provide incentives to encourage performance (Method, 2008). A similar result can be found at the state level, as the case below illustrates:

Some politicians are fond of blustering about making government run *like a business* and they often stereotype public employees as do-nothing bureaucrats. So when the government does run *like a business*, that, one might think, would make them happy.

The Florida Department of Revenue took state lawmakers up on a challenge issued when the legislature passed a law allowing monetary rewards—bonuses—to state employees who go above and beyond the call of duty and save the state money. The department saved state taxpayers $9 million. Not bad.

Having accomplished this, the agency's executive director, Larry Fuchs, asked the legislature to appropriate enough to give half of his deserving staff $100 bonuses. Save $9 million. Spend $250,000. But, that's when another stereotype came into play: the stereotype of the conniving, forked-tongue, hypocritical politician. The Senate refused to give Fuchs the bonus money.

Some lawmakers say the state should not pay its employees extra for simply doing their jobs. Others have questioned whether the agency met performance standards, but Fuchs says he was never told why the Senate refused to pay the bonuses. If the Senate does not want to offer financial incentives for meeting higher work standards in state government, it should say so. But, government leaders have an obligation to keep their promises. Pay the $100 bonuses. (Cotterell, 2004)

In the same state, many departments paid identical amounts to eligible staff (e.g., $371, although some payouts ranged from $76 to $2,000 for a small number of employees; Cotterell, 2004). For different reasons, most personnel—those receiving and those not receiving the monies—found the payouts to be depressing. In Wyoming, $400 annual performance bonuses were allotted to state agencies for distribution in 12 monthly installments. In some departments, awards were given to a few people who then gave the money to others, threw a party, or refused to accept it. In other offices, employees drew straws for the money (Behn, 2000, p. 4). Thus, while these programs are a tool in the pay raise quiver, they are much less suited to widespread use than in the private sector, especially in areas like sales, executive pay, and Wall Street, where they predominate.

Another concern is that performance awards incentivize inappropriate behavior. In 2014, an outcome-driven performance management system at the Veterans Administration (VA) created unrealistic goals that ultimately put the health of veterans at risk. The program led managers to falsify wait-time records to make it appear that veterans were being seen by medical personnel sooner than they actually were. At the height of the scandal, an agency official testified before Congress that annual bonuses were a vital tool in recruiting and retaining top employees (nevertheless, the reward program was canceled). The episode was ironic since the VA had been seen as a success story; in the 1990s, reformers cut back middle-management ranks and began using performance data. The overall result was that patients received high-quality, low-cost care and did not appear to wait longer than nonveterans in private hospitals (the satisfaction rate among patients was over 80 percent; Fahrenthold, 2014).

Incentive payout schemes like bonus programs, even if adequately funded, should not be used to cover up more fundamental problems in the workplace. There are settings in which bonuses make sense if the work offers employees no opportunity to find satisfaction and fulfill intrinsic needs. And, yes, there should be public acknowledgment of extra

(Countined)

(Countined)

performance. The offer of bonuses, however, implies that employees are not working hard, cannot be trusted to do their work, and need extra incentive to do their jobs well. It is for these reasons such plans are often counterproductive. Promoting the idea that no one will do anything right unless it is required is no way to run an organization.

Sources: Behn (2000); Cotterell (2004), p. 1B; Lee & Strauss (2004); State should keep promise (1996 December 13), *Tallahassee Democrat*, p. 10A.

Performance awards are akin to merit increases in that they are competitive and unequally distributed; the difference is that they must be earned each year and they do not contribute to base salary. They are used extensively at the federal level and for executive pay in state and local governments. In the federal government case, discretionary bonuses are capped at "no more than 1 percent of an agency's aggregate salaries of rank-and-file employees, and no more than 5 percent of the aggregate salaries for its senior executives" (Mullen, 2014). This category topped out in 2011, when the payout was $439 million, but has declined dramatically since then (due to strong political criticism), with a payout of only $177 million in 2013. In addition, the Presidential Rank Awards were suspended in 2013. Ironically, the use of this type of raise has increased in the private sector, where it is called variable pay.

In a **gainsharing** pay plan, similar to profit-sharing in companies, the organization and its employees divide greater-than-expected gains realized through productivity and/or cost reductions. Typically, half of the savings revert to the agency general fund and the balance is allotted equally among the people involved. Several interesting variations of gainsharing have been used by city governments. For example, under a popular program in Loveland, Colorado, the provision of funds to city personnel depended on the results of citizen satisfaction surveys and the amount of funds left over in the budget; this program was terminated, however, because managers found it to be problematic. In Denver, city employees share in savings gained through changes accomplished by work teams (Risher, 201bc). Charlotte, North Carolina, has a *competition-based program* that distributes monies either to employees when they competitively bid and win projects or to city departments when they exceed benchmark performance standards (Jurkiewicz & Bowman, 2002).

Gainsharing, in short, is designed to accomplish the same objective as individual incentives: the linking of rewards with performance. The difference is that in gainsharing performance is measured as a result of group effort, thereby reinforcing team cohesion, promoting a problem-solving culture, and reducing perceived internal inequities. Individual and group incentives are not mutually exclusive but can be blended through concentration on individual behavior consistent with gainsharing (i.e., contributions to teamwork). To succeed, the technique requires a high degree of organizational trust as well as widespread information distribution. Focusing on employee empowerment and quality improvement, a number of experiments in the U.S. Department of Defense since the 1980s have had varying degrees of success. One concern with gainsharing is that it may be quite successful in the program's first several years, when the potential for savings is high, but this potential can decline over time.

Although not widely used, gainsharing carries genuine potential to create a flexible, proactive, problem-solving workforce (Masternak, 2003). This is one of many areas, however, where rhetoric and reality collide. As Sanders (1998) has ruefully observed, lawmakers may argue that "bureaucrats are already paid (perhaps too much) to efficiently use public funds, and that they should not be offered more money to do what they should be doing anyway" (p. 239). The idea is that base salary and just having a job should be adequate incentive (a notion that progressive businesses rejected long ago). Accordingly, when an agency attempts an incentive plan like gainsharing or bonuses, its payroll may subsequently be reduced by the amount of savings generated.

For incentive programs to be successful, a cultural change is required to overcome the suspicion and cynicism with which these plans are currently viewed. Yet, should such a change occur, these approaches, when used as partial or complete substitutes for other plans, can mean less money for most employees than that provided under other approaches to individual equity.

Differential Pay

Differential pay is additional pay for special work conditions based on time, location, responsibilities, or deference to special needs or employee considerations. It is considered temporary and not a part of the base pay; however, employees may be eligible for differential pay for long periods or even their entire careers, and some compensation systems allow differentials to be used in calculating pensions (a practice curtailed by recent pension reforms). The implicit values of this type of pay are to motivate people to take on less desirable assignments, locations, or responsibilities, and to hold them harmless for job-incurred expenses.

Shift differentials, for example, are common where hours extend considerably beyond the normal 8:00-to-5:00 workday and the Monday-through-Friday workweek (e.g., the evening or swing shift, 4:00 p.m. to midnight; the late-night or graveyard shift, midnight to 8:00 a.m.). It is typical for agencies to give employees hourly shift differentials for working these shifts, as well as to provide a larger differential for the graveyard shift. The federal government customarily pays 7.5 percent and 10 percent differentials for the second and third shifts, respectively.

Location pay is typically provided to employees working in high-cost areas or unattractive regions and those with undesirable duties. The national government pays up to a 35 percent premium in the most expensive cities (e.g., for the San Jose–San Francisco area), but with a norm of 20 percent to 28 percent for most other urban sites, including, ironically, the minimum 14 percent location pay provided to all U.S.-based federal employees. Undesirable assignments, common in the armed forces and U.S. State Department, are also eligible for location differentials, such as hazardous duty pay, hostile-fire-and-imminent-danger pay, hardship pay, and assignment-incentive military pay (for extending tours in less desirable locations). The equivalent for civilian personnel is danger pay, which can be as high as 35 percent in war-ravaged areas.

Overtime pay is for time beyond the 40-hour workweek and is provided at one and a half times the worker's regular pay rate. Holiday pay is a special type of overtime, requiring work on a state or national holiday; it is usually double time in recognition of this work's onerous nature. Although overtime is rarely allowed in many agencies except in extraordinary conditions, it is common and desired in public safety and corrections, where staffing limitations and the need for trained personnel require agencies to use large amounts of overtime routinely. Such departments regularly have standing overtime allocations built into their budgets. Overtime among employees in fire and corrections can be so extensive that a few individuals nearly double their salaries. Since overtime is not a part of the base salary, it normally does not count toward pension benefits. Special variants of overtime are standby pay for availability to work in extreme circumstances and call-out pay for being on duty during non-normal hours for an emergency.

Allowances are monies to pay for costs imposed by employment or as part of the job. They can be relatively small (food, clothing, dislocation, moving, and family separation) or large (cars, housing). Allowances can be considered either reimbursements or income: Most travel and uniform allowances are considered reimbursements and not taxable, whereas automobile and housing allowances are regarded as a type of income and have tax ramifications. The military makes extensive use of allowances; they are also common in executive positions and public safety. A variant of an allowance is when an employee gets benefits from a job that reduce costs and may not be taxable (e.g., food eaten on the job or a *take-home* car for an employee who is on call).

Finally, differentials are also provided for assumption of special responsibilities (special duty or assignment pay). They may be awarded for assignments that are difficult, filled on a crisis basis, or hard to fill because unusual skills are needed. For example, the U.S. Navy has 23 standing special duty pay areas, ranging from being a recruiter to working on the *USS Constitution* to being a military attaché to being a brig officer.

IMPLICATIONS

The above discussion has examined the similarities and differences among pay systems awarding raises based on cost of living, longevity, merit, skill, bonuses, and differentials. These provide a set of compensation tools that can be precise and purposeful. In practice, they are often conflated, used too bluntly, ignored, and/or simply misrepresented, with the result that the similarities engulf the differences. Any reasonable increase becomes a symbolic lightning rod for criticism. Consequently, available resources are often so trivial that managers have little choice but to use the *peanut butter* approach: spread the funds more or less equally among employees to help keep everyone from losing ground to inflation.

This is perhaps most clear when cost-of-living allowances not only are used as a substitute for incentive pay but also are doled out below living costs. When there is little consistent attempt to keep employees "whole" against inflation, the real issue is not raises (seniority, merit, skill, or gainshare) but the size of the pay reductions. When the economy improves, many lawmakers paradoxically, if predictably, see even less reason to provide raises—to say nothing of furnishing *catch-up* monies.[13] Indeed, they often argue against raises as a way to keep inflation under control.

This strategy serves as an indicator of elected official toughness and responsiveness to taxpayers. Thus, equity—external, internal, individual—is simply replaced by the amount of lost purchasing power as the years go by. Nowhere is the dilemma between organizational and individual goals more evident: Employees wish to be treated fairly at the same time that public compensation systems often act to deny that need. The depth of the problem was illustrated in 1999. Rather than pay soldiers salaries sufficient to keep them off public assistance, the military again lowered recruiting standards, and some elected officials advocated reinstating the draft.[14] The value to the public of this conundrum is limited:

Employees in an inequitable situation, according to equity theory, seek to reduce the inequity by decreasing performance, increasing absenteeism and tardiness, or simply quitting.

Although it may be true that relative pay levels will not drive government out of business, it is also true that a noncompetitive salary structure has very real consequences for public service. It serves as an impetus to hire peripheral labor—low-paid, often poorly trained, part-time employees, temporary workers, and even volunteers, many of whom are likely to leave as soon as they find full-time positions.[15] It also acts as a stimulus to privatization—the functional equivalent of going out of business—sometimes at a higher cost to the taxpayer.

In this context, then, debates over pay reform plans, although intellectually interesting, are diversionary because they miss the fundamental point: inadequate pay for all employees. The actual problem is decidedly not the type of pay technique; rather, the real, substantively rational issue is the amount of pay. It is not unexpected, therefore, that incentive systems often do not produce expected gains. Rather than focusing on fundamental problems—insufficient funding, inaccurate evaluations, incomplete feedback, ineffective leadership—agencies introduce incentive pay, thought to be a quick way to increase effort, while not understanding that in reality it is a complex, expensive, questionable enterprise.

In developing a 21st-century pay program it will be important to:

1. Commission an independent market analysis to assess the public/private salary competitiveness
2. Learn from past experiences with pay programs
3. Create teams in each department to examine proposed reforms
4. Direct agencies to identify sill critical to achieving their missions
5. Study the ways leading companies improve managerial effectiveness in implementing changes
6. Develop appraisal procedures (Chapter 10) that link to compensation best practices and pilot new systems prior to agency-wide reform
7. Train a corps of generalists and specialists to administer the new compensation system (adapted from Risher, 2017a)

Pay in all sectors has been stagnant for several decades; gross compensation has increased slightly largely because of health care costs (Bureau of Labor Statistics, 2014). Productivity has grown 80 percent since 1973, but incomes have grown only 10 percent on average, and that was before 2000. Indeed, mean income (including market earnings) has continued to rise slightly, yet because 65 percent of that income went to the top 1 percent, overall median household income has actually slid by more than 10 percent since 2000 (Greenhouse, 2013). In the federal case, ideological factions see the gap differently and cite different studies to argue either for reducing pay and benefits (Congressional Budget Office, 2012; House Budget Committee, 2014) or attempting to keep federal workers' incomes from slipping due to inflation and reducing pay gaps (President's Pay Agent, 2011; U.S. GAO, 2013). Because government employees tend to be substantially better educated