Total Compensation Partnership Report

A Collaborative Effort of:

Colorado WINS
The Association of Colorado State Patrol Professionals (ACSPP)
The Colorado Department of Personnel and Administration, and
The Governor's Designee for Employee Partnerships

This project was undertaken by the above organizations as a system-wide effort under the auspices of Governor Ritter's Executive Order D 028 07. This report reflects agreements reached by the parties on November 6, 2009. It is intended to serve as an addendum to the State Personnel Director's December letter updating the Annual Compensation Recommendations for 2010-11 fiscal year.

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I. Introduction

On November 2, 2007, Governor Bill Ritter signed *Executive Order D 028 07* entitled *Authorizing Partnership Agreements with State Employees*. Below are some key passages reflecting the intent of the order.

> *"In today's twenty-first century marketplace, chief executive officers must constantly seek out new and better ways of leading their organizations. The same is true with state government. Examples in both the private and public sectors demonstrate that employee-management cooperation that engages and empowers employees in decision-making around service planning and implementation is likely to produce better service, more cost-effective provision of services, and a healthier work environment. Employee partnerships will foster collaboration and cross-fertilization of ideas between those in management and those whose daily jobs give them concrete knowledge of what can be done better, and how; what need not be done, and why; and what else should be done, and by whom."*

> *"The purpose of this Executive Order is to establish the framework for employee partnerships in service of a smarter, more effective, more efficient and more accountable state government for the citizens of this State."*

Each year, the State Personnel Director (Executive Director of the Department of Personnel and Administration) is required by law to issue a letter by August 1 of each year regarding recommendations and estimated costs for changes in pay and/or benefits for the upcoming fiscal year.

> Colorado Revised Statutes, Sec. 24-50-104 (1) (a) (I), states in part, *"It is the policy of the state to provide prevailing total compensation to officers and employees in the state personnel system to ensure the recruitment, motivation, and retention of a qualified and competent work force."*

> Colorado Revised Statutes Sec. 24-50-104 (4) (c) states, *"…by August 1 of each year … the state personnel director shall submit the annual compensation report and recommendations and estimated costs for state employee compensation for the next fiscal year, covering salaries, state contribution for group benefit plans, and performance awards, to the governor and the joint budget committee of the general assembly."*

In addition to the annual August 1 letter addressed above, the Executive Director of the Department of Personnel and Administration (the state personnel director) has for several years issued a December update to the August 1 letter.

1. Total Compensation Partnership Team

The Executive Order anticipates that some partnership undertakings will span across all departments. In ordinary usage, these are called "system-wide partnership" engagements. The Executive Order provides:

> *"Partnership Agreements that govern discussions of matters impacting all Covered Employees as a whole or that necessitate statewide uniformity (whether Constitutionally, by statute or rule, or as a practical matter) shall be negotiated on a collaborative basis*

with all Certified Employee Organizations. The negotiation of such a Partnership Agreement shall be conducted by the Governor's Designee in concert with the executive officials charged with administering the issues subject to the Agreement (such as the Director of the Department of Personnel and Administration), on the one hand, and a designee or negotiating team selected by a coalition of the Certified Employee Organizations, on the other hand. Such a Partnership Agreement is subject to the approval of the Governor and other officials charged with administering the issues subject to the Agreement."

Commencing March 3, 2009, the team members began working through the "interest-based problem solving" approach to bring the parties to consensus on the needed improvements in the State's total compensation system as well as ensure that all the parties were fully informed regarding the history and statutory framework of the total compensation process. As will be seen below, the Partners addressed the pay process from wage survey through pay administration. The Partners also discussed the implications of the key insurance benefits (health, life and dental) as well as the Public Employee Retirement Plan (PERA) retirement benefits.

2. The Partners' Shared Interests

Early in the interest-based process, the parties identified what interests they shared – i.e. interests that transcended the concerns of the respective organizations and represented some core agreements that governed the succeeding work. The result of that work was the following list of shared interests:

- Partnership success
- Recruit / retain an engaged, productive workforce
- Retain seasoned officers
- Compete for best applicants
- Long term focus – sustainable
- Understandable
- Efficient administration
- Defensible – legally and politically
- Competitive with market
- Flexible – 1 size does not fit all
- Integrated total rewards components – includes distribution of new dollars
- Mutually agreed upon pay distribution method
- Technically and professionally sound survey
- Pay system that:
    - Addresses retention
    - Addresses internal equity
    - Acknowledges skill development (meets expectations)
- When motivating employees beyond "meets expectations":
    - Performance measurement tied to larger (unit, dept) goals (link personal and larger goals; specific quality improvements)
    - Fosters collaboration, not competition (team focus)
- System is truly fair and equitable (performance evaluations):
    - Consistency in evaluations
    - Accountability (up the chain)
    - Objective criteria

- System must be flexible to address variations in occupations and work environments
- Accuracy:
    - Reflects state of labor market, independent of ability to pay
    - Measures wages and changes in wages
    - Measures employee compensation, not just cost
- Verification / transparency
- Simplified and credible
    - Understandable (easily) to average state employee

[The parties recognize that there is some degree of overlap among these items but that, collectively, this list represents the consensus of the parties.]

3. Additional Considerations of the Partners

The Partners recognize the current fiscal circumstances have created unprecedented pressures on the State budget. The work elements identified in this report are intended to develop recommendations to improve the pay system. The Partners recognize that until the current fiscal pressures abate, implementation of pay system changes requiring significant appropriations may not be possible.

Wherever this report refers to work to be completed in the future, the intent is for the Partners to negotiate in good faith, using an interest-based process. The mutual expectation is that the Partners will be able to bring each matter to a successful conclusion through consensus. However, if the Partners are unable to reach accord on a particular matter, each can determine what recourse it wishes to take to address the impasse.

While the Partners will be collaborating on improved methods for establishing compensation and benefits, nothing in this report is intended to diminish the responsibility and authority of the Executive Director of the Colorado Department of Personnel and Administration to conduct the work necessary to satisfy constitutional or statutory requirements, including any work elements agreed to in accordance with this work plan.

II. Market Survey and Related for the August 2010 Letter

Many of the work elements to which the Partners have agreed relate to the design of the market survey and the manner in which survey results are analyzed. Below are the major topics to be addressed between now and the issuance of the Executive Director's August 2010 total compensation letter and report relating to the State's 2011-12 fiscal year. The Partners will engage in good-faith negotiations on each of these matters with the aim of reaching consensus during that time frame.

1. What is "Prevailing" Practice?

The parties will establish a definition of "prevailing" that will be consistently applied in the total compensation process.

2. Benchmarking

The benchmarking process will be evaluated by the Partners to ensure that it provides the most useful information to compare state salaries and pay plans with prevailing practices. The Partners will review the information and jointly develop, via consensus, a protocol to establish benchmarks that best reflect salaries in the occupational groups (i.e. best practices). The benchmarking work will also ascertain best practices regarding weighting or not weighting benchmark classifications in determining occupational group pay movement.

3. Survey Selection Criteria

The Partners will develop criteria for survey selection to reflect best practices, and which the Partners can support via consensus. The Partners will apply these criteria to available surveys to arrive at a set of surveys to be used in the total compensation survey process (all subject to the good faith and consensus processes described above. Internal milestones have been established in order to best ensure that the survey process meets the timing requirements for the August 1, 2010, total compensation letter and report. This could result in DPA adding surveys or adapting those currently used. The surveys should measure compensation in a manner that meets the Partners' definition of "prevailing."

4. Weighting In-State and Out-of-State Data

Currently, DPA uses in-state and out-of-state data without weighting to favor one category over the other. The Partners will evaluate alternative practices in weighting in-state data differently than out-of-state data and will develop a protocol reflecting best practices to be used by DPA (all subject to the good faith and consensus processes described above).

5. Additional Work Plan Elements

Wherever the research indicates to the satisfaction of the Partners that a change is appropriate, the Partners will work in good faith to design consensus changes to be used by DPA in time for the survey work for the 2011-12 fiscal year. In this regard, the Partners will continue to meet regularly to complete their work.

In addition to the above, the Partners agree to evaluate a redesign of the pay structure to ensure that the internal structures of job classes are appropriate. Further, to the extent that higher paid and supervisory job classifications within the State were more likely to reflect pay levels at above "market" during the 2009 survey process the Partners will examine the causes to determine whether system changes are appropriate. Based on such studies, the Partners will develop appropriate actions to be taken by DPA (subject to the good faith and consensus processes described above.

III. Pay Progression

There are two essential components of base pay adjustment: (i) adjustments based on changes in prevailing pay in order to assure employees are paid competitively with the market and in accordance with statute; and (ii) adjustments to recognize increased skills and knowledge which advance employees within their assigned pay ranges. Progression refers to the salary movement of an employee through the respective pay range. Currently, the only way an employee moves through the range is by receiving the base-building pay increment (achievement pay) for that budget year.

The Partners agree, and the general rule in compensation is, that a new hire, if entering at the bottom of the range, and otherwise competent, should regularly progress through the pay range reflecting the increased skills and knowledge of the employee. Employees should be expected to progress to the midpoint of the range upon achieving full competency. However, given the recent rates of base increases, state employees would not reach midpoint of the range until 20 or more years from the date of hire, substantially beyond the point where state employees would be expected to have reached full competency. This is largely due to underfunding in the current achievement pay system.

The Partners agree that the current patterns of pay progression, especially for those hired since 2002, are not consistent with the objectives of motivation and retention of qualified and competent employees as provided in the above statute.

(a) Those hired before approximately 1994 have, in many cases, reached or approached the maximum for the respective pay range.

(b) Those hired between 1994 and 2002 may have progressed up the pay range for a while under previous plans, but are now in a relatively immovable position due to lack of funding for achievement pay. Those hired above entry level in recent years are in a similar position.

(c) Those hired since 2002, unless hired above the minimum of the range, are all congregated within about 2 percent of the minimum (entry level) irrespective of time in grade or quality of performance evaluations.

Thus, the base-building objectives of achievement pay are not being achieved, in large part because of insufficient funding. These conditions arise not only because of the infrequent funding for achievement pay but also because achievement pay, when available, has been in very small increments that have not materially moved the employees' base pay through the respective ranges.

The Partners agree to collaborate on the redesign of the pay progression process to ensure a reasonable degree of progression in the respective ranges (subject to adequate performance and available funding). The Partners anticipate that this would result in employees reaching the midpoint of the respective pay range once they are fully competent with the ability to progress toward the maximum during the course of their careers.

In May of 2009, in the course of partnership discussions, both ACSPP and COWINS have proposed specific types of pay progression. The Partners agree that these alternatives will be more closely evaluated in the coming months as part of this partnership engagement.

IV. Benefits as Part of Total Compensation

The Partners agree that comparing pay to the market, without regard to other major compensation elements, is not in accord with industry practice. Some form of total compensation is the norm in the profession. Specifically, the Partners will evaluate the current practice of relying upon benefit survey data from employers that have not been surveyed for salary purposes.

1. Health, Dental and Life Insurance

Ordinarily a principal element in total compensation comparisons with the market is the employer contribution for health, dental and life insurance.

For the fiscal year 2009-10, the State contribution for health insurance premiums is currently at 90 percent of what the surveyed employer market pays, and the State contribution for dental insurance premiums is at 85 percent of that market, using DPA's current methods for measurement.

There is considerable evidence that the value of State health plans is substantially less than those in the market. The following table compares the percentage of covered expenses borne by participants in the State's self-funded medical and prescription drug plan with the percentage of covered expenses borne by participants in Cigna's insured base within Colorado. Cigna currently manages the State's self-funded plan. The data shown for Cigna Medical and Cigna Pharmacy reflect their overall business state-wide. It should be noted that the State plan may cover fewer services (e.g. vision care) which requires additional expenditures by State health plan participants:

	State Medical	Cigna Medical	State Pharmacy	Cigna Pharmacy
Plan Share	76%	85%	68%	80%
Participant Share	24%	15%	32%	20%

While this data is limited to a comparison of the State's plans to that of one large carrier, it does strongly suggest that the value of the compensation employees receive in health benefits is substantially below prevailing levels. This illustrates that the State pays less for a benefit that is also worth less than what other Colorado employers provide. Further, the State workforce is considerably older than the non-state workforce, and therefore, will have higher health care utilization resulting in higher premiums.

The result is that the State's cost for health benefits, being below market, has a downward effect on the value of the State's total compensation package.

The Partners also agree to evaluate the surveys and survey methodology for health and dental benefits to ensure that the State, through DPA, takes advantage of best practices.

For the 2009-10 fiscal year, the basic life insurance coverage provided by the State is less than the employer provided life insurance in the market. The coverage in the market equates to 1.4 times the annual salary on average. Beginning July 2009, the State increased its life benefit to $50,000 for all employees, which approximates the average state salary. Thus, the coverage is estimated to be roughly 100 percent of salary, or 72 percent of prevailing market benefits.

The Partners agree to evaluate the appropriate administration and coverage for State-provided life insurance.

2. Retirement as a Factor in Total Compensation

The employer contributions to pension and social security are normally considered in total compensation comparisons.

The Partners agree that PERA benefits are of value to both the employer and employee. This discussion is not intended to be a commentary on the quality of the PERA plan design, or upon the current funding status, or upon the plan's unfunded liability. Rather, it is intended only as a discussion of the employer and employee share of the funding of the "normal cost" of the plan as currently designed, and the implications of these respective shares in the total compensation comparison. With these qualifications, consider that:

i. The State does not participate in the national Social Security (SS) system. As a result, the State does not incur the 6.2 percent employer share of FICA, nor does the employee incur the 6.2 percent employee share. (Here and elsewhere, the 6.2 percent of payroll is used because the 1.45 percent for Medicare tax applies across the board.)

ii. Therefore the employee does not accrue service credits for a social security benefit. Moreover, the State employee will likely incur a reduction ("offset") in any earned SS benefit from other employment because of the PERA defined benefit plan. Similarly, the spousal SS benefit may be offset.

iii. Currently, the "normal cost" for the PERA plan benefits is 13.45 percent of pay. *[Report of the Actuarial Valuation of the Public Employees' Retirement Association of Colorado, 12/31/08]* The "normal cost" represents "the portion of the cost of projected benefits allocated to the current plan year." [*Washington Office of the State Actuary*]

iv. Of 13.45 percent, 5.4 percent is paid by the State as the employer share and 8.05 percent is paid by the employee as a payroll deduction. [See PERA actuarial report above.]

v. The employee share of "normal cost" covers 60 percent of the total cost of accruing benefits.

vi. Consequently, the State contributes less for the employer share of the plan (5.4 percent) than it would if the employee were eligible for social security (6.2 percent employer contribution).

[These data were reviewed with PERA prior to publication.]

Most employers in the market pay for social security and contribute something – usually as a percent of pay – to either a defined benefit or a defined contribution plan. The Partners will select an appropriate data source to identify the "prevailing" practice for retirement benefits (subject to the good faith and consensus processes described above).

In conclusion, the State contributes significantly less to the future retirement of State employees than is contributed by employers in the market.

The Partners agree that the August 1, 2010 Executive Director’s total compensation letter will include comparative data for the employer share of retirement/pension costs.

3. Combined Effect of Benefit Package

When these factors are taken into account, the State contributions for insurance benefits and retirement are considerably less than the corresponding market contributions for these components of total compensation.

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In conclusion, the Partners will issue additional reports or memoranda from time to time to reflect the findings and conclusions of the collaborations identified above.