

**NOTES ON
PAY IN THE CIVIL SERVICE IN INDUSTRIALISED COUNTRIES**

28-29 June 2005

Francois EYRAUD, ILO

Causes and objectives of the reforms of civil service pay systems

The first wave of reform appeared in the 1980s, mainly in Denmark, Italy the Netherlands, New Zealand, Spain, Sweden, the United Kingdom and the United States.

The second wave followed in the 1990s till the beginning of 2005 with Germany, France, Switzerland and a few Eastern European countries (Czech, Hungary, Poland).

The causes of reform are diverse; however, they are more or less the same among countries:

- Recruiting and retaining staff particularly amongst the highly qualified (the main characteristic of the public sector wage structure is that salaries of the least/middle skilled occupations are frequently higher in the public sector than in the private sector. This is reversed for the senior occupations and in the 90s, pay level of civil service managers had slipped to between 30-50% below those of the private sector.),
- End of wage indexation with the decrease of inflation,
- Motivating staff while the seniority system came under attack, change in the role and attitude of civil servants and no more bureaucracy but entrepreneurial and service oriented.

The main characteristics of the reform were:

- Decentralisation of pay determination,
- Change in pay and grading structures,
- More contingent forms of remuneration related to skill, responsibility and performance.

The core objective was (and still is) to make seniority increments (main traditional pay determination factor together with educational level) less automatic and to relate increases to performance.

It should be stressed (and we will come back to this) that these reforms have been very difficult to implement and in most countries it is a permanent process that is still going on.

Types of civil service pay systems

The classification of civil service pay systems is usually based on the degree of decentralisation in wage determination, i.e. the degree of autonomy of the sectors/departments/agencies of the public sector in terms of elaborating or adapting their wage scale (to the requirement of their labour market for instance) and distributing wage increases. But in all countries the Ministry of finance closely controls the total wage bill, in one way or the other (see below). In a sense, the need to recruit and retain staff may face an even bigger need of controlling the civil services' pay bill.

- Centralised systems are found in Germany, France, Spain and Portugal.
- Decentralised system is found in the United Kingdom.
- In most countries (Italy, the Netherlands, Denmark, Ireland, Finland, Sweden, Canada and the United States) a mixed system exists.

Let's consider some examples in each of these categories.

Centralised systems

In France, there is one wage scale (with sub-scales) where each grade or wage level is defined by an equivalent educational level and responsibilities whatever the occupation or the sector of activities. In France sub-scale A is for managers and other high level civil servants, sub-scale B is for technicians and C for low skill/level of responsibilities. In Germany, scale A governs the remuneration of civil servants and soldiers except senior positions (scale B). Scale C applies to university professors and R for magistrates.

Decentralised systems

The United Kingdom shows the more decentralised system. When the reform was introduced in the early 80s, the idea was to adapt remunerations to the characteristics of the occupation or the sectors (army, education, nurses etc). In a sense it is in continuity with the traditional systems where 22 occupational/sectoral agreements existed. The main difference however is that, at that time, 1) the negotiations took place at the national level and 2) the government was directly involved. This is no longer the case and one can find, for example, in the health sector, salary scales for doctors, nurses and lab technicians and wage determination is the responsibility of the departments/agencies concerned. Decentralisation makes a very big difference in the sense that the managers concerned should deal within a budget without any possible help and salaries for a same occupation could display a huge difference.

In the United States and Italy, the degree of decentralisation is less developed. In the United States at the federal level (2.8 millions federal civil servants) there are 5 wage scales:

- The general schedule (46% of the federal civil servants)
- The collective bargaining system (post office workers)
- The Federal Wage System (mainly manual workers in transport and army)
- The Senior Executive system (high level officers and political appointees)
- Executive schedule (agency directors, minister cabinet members etc)

In Italy, the law of 1983 has defined 8 sub-sectors (ministries, universities, army, etc). Each one can adapt its scale depending on labour market constraints.

Pay increase decision making process

Who decides?

There are two main systems: unilateral decision from the state or collective bargaining. At a first glance, the first method applies to centralised system and the second to decentralised systems. In reality it is more common to have a combination of the two systems. For example, in France and Germany the decision is taken by the State. However, there is always a consultation whether it is a formal or an informal one.

In the United States, pay increases are decided by the government and the Congress, except for post office workers (collective bargaining). It is important to note that the decision is not only based on the cost of employment but also on the principle of parity with pay in the private sector for a similar job.

This principle of parity between public and private is also found in the United Kingdom for the “pay review boards”. Two systems of pay fixing exist: collective bargaining for most departments and agencies and the “pay review boards” for a significant group of civil servants. PRB members are independent but appointed by the government and make recommendations that the government is free to apply or not. They concern categories like: armed forces, top salary group, nurses, doctors, teachers in England and Wales (mainly health and education).

In all cases the civil service wage bill is controlled in one way or the other:

- Germany: Responsibility of the Ministry of Interior under strict control from the Ministry of Finance.
- France: the Ministry of Finance fixes the range of the increases.
- United Kingdom: Treasury fixes the range of increases for local collective bargaining based on a strict control of the evolution of the global wage bill.
- Italy: the Industrial relations Agency (1993, members appointed by the government and follow directive fixed by the government) fixes the target of local bargaining
- Post office in the US: the Congress fixes the range of the increases.

Advantages and disadvantages of centralisation and decentralisation

Advantages of decentralisation:

- Adaptability of wage increases to occupations and sectors,
- Make managers responsible of HR management

Advantages of centralisation:

- Solidarity among civil servants and mobility among sectors,
- Allows coherence in pay policy among occupations and sectors of the civil service and reduce inequalities,
- Avoid overbidding.

From this point of view, note that in the United States, after a period where adapting and adding wage grades locally were allowed to fit local labour market conditions, they are now back to common wage scales to limit the inequalities which were then created.

Performance pay in the public sector

Why introducing Performance-related Pay PRP?

Together with decentralisation, linking pay to performance rather than to seniority is the other big challenge of the public sector pay reform. The main issue of the pay reform is to transform in a more or less radical way the traditional seniority-based system into a pay system where individual qualities are rewarded rather than the grade of the job.

PRP has been introduced by law in most OECD countries except Denmark and Finland where this was done by collective bargaining.

However, only a handful industrialized countries can be considered to have a Performance related pay (PRP) system: Denmark, Finland, Korea, New Zealand, Switzerland and the United Kingdom.

One reason is that it has been found that job content and career development prospect are stronger incentives for public employees than PRP. This is why many countries tend to focus primarily on promotion to motivate staff.

The question is then: why PRP continues to be developed? The reason is that it appears to be very helpful in facilitating change. In effect, introduction of PRP allows developing:

- Effective appraisal and goal setting process,
- Clarification of tasks,
- Skill development,
- Improved employees/managers dialogue,
- Team work,
- Flexibility in work performance,
- Act as recruitment incentive.

How does PRP work?

There is no best PRP device. It should be adapted to the local conditions.

At the beginning, quantitative appraisal measurements were introduced to avoid subjectivity. However, empirical research shows that it does not work well in the

public sector due to the difficulty to measure productivity. Today systems are less formalised than 10 years ago and based more on dialogue with line management. More precisely, performance appraisals rely more on the assessment of pre-identified objectives and dialogue with managers than on strictly identified quantified indicators

Obviously, PRP goes with decentralisation and pay delegation. But pay delegation is generally confined to issues such as measurement of performance and distribution of a prefixed amount of money due to the control of public service wage bill made at the central level.

Another evolution regards the categories concerned. In the 80/90s PRP applied only to senior management. Today all categories are concerned, nevertheless, to a lesser extent. Moreover, the systems remain different for senior management and for the other categories of staff, in particular, the bonus as a percentage of basic salary is far higher for the first category. On average, among non-managerial employees, PRP represent a fairly modest percentage of basic pay (less than 10%). Higher at managerial level: around 20%. In the United States for instance, bonuses have been abandoned for non-managerial staff.

Another noticeable change is the shift from individual bonus to a more collective approach, particularly for non-managers. Performance bonuses now are team based rather than individual based in many countries.

A clear anticipation of the budget needed and related cost should be made. Another decision to make is the type of increase, which is going to be granted. The 2 main techniques are either a lump sum bonus or a merit increment.

Merit increment is integrated into the base salary and is therefore a better incentive on a long-term basis. Lump sum bonuses better highlight the performance-related nature of the reward and could change from one month/year to the other. They do not add to fixed payroll costs (pension). They could be managed with greater flexibility.

PRP could be used as a tool to control pay bill under certain conditions:

- The increase should not be in addition to other traditional rewards, such as seniority bonus. From this point of view, PRP will replace the seniority bonus to be cost neutral. Alternatively, seniority payment may be made dependent on performance (i.e. no payment if unsatisfactory performance).

- In most countries, PRP must be funded from within agency budget (Australia, Denmark, United States, and Hungary). In some others, a special budget is provided (Canada, Finland, Korea, Ireland, and Spain).

Finally, it should be stressed that any PRP system should be reformed after some time.

Others aspects of the reforms

Finally, another less documented phenomena concerns the changes introduced in the number of grades. Several countries face the problem of the lowest coefficients, which are no more attractive to recruit even low skilled workers, due in particular to the higher level of education of the population. The solution has been to cut these coefficients and integrated them into the higher levels. That has happened in Germany where the grades from A1 to A5 have been suppressed (max is A16) and in France where the category D has been cut, staff having progressively integrated into the category C.

In Italy, in order to attract high-level staff, grades have been created at the top of the scale.