

EXECUTIVE SUMMARY

The State of North Carolina General Assembly's Government Performance Audit Committee (GPAC) engaged Fox Lawson & Associates, LLC (FLA) to conduct an independent performance review of the personnel system and specifically, the career banding system with recommendations for legislative consideration.

Approach

FLA reviewed relevant statutes, laws and practices relative to North Carolina's career banding and personnel practices and procedures as well as research studies, manuals, and other material analyzing personnel practices in general and career banding specifically. Representatives of the GPAC, 18 agency/university HR directors, and Office of State Personnel (OSP) staff were interviewed. Focus groups totaling approximately 300 individuals from across the state representing a cross-section of agencies/universities were held with employees, managers, agency HR directors, agency directors, as well as university chancellors and HR directors. FLA also collected quantitative data, as available, to provide comparisons.

GPAC Questions Posed and Summary Responses

- 1. A review of organizational reporting relationships, delegation agreements, and degree of independence or centralization within the human resources system structure and the authority of the State Personnel Commission.**

Currently OSP has authority to provide policy development, rule making, training, maintaining personnel information and data, providing approval of personnel actions, negotiating the decentralized authority to agencies/universities and implementing corrective action for cases of noncompliance. For the most part, this has worked as well as might be expected in a large complex government operation. The decentralization of personnel actions requires three essential elements: trained human resources personnel in the agencies/universities, a system to audit and review the actions of the agency/university, and information for the PMIS system. The right to rescind the delegation of authority needs to be strengthened to allow the OSP to take back the authority if the agency/university is found to be out of compliance with the proper

administration of Chapter 126 and policies of the State Personnel Commission and/or their program has been found to be ineffective. We encourage decentralization of personnel practices if the audit function is strengthened. Further, we believe that there should be a dotted line relationship between the OSP Director and the HR director in the agencies/universities, to ensure consistency. However, we encourage the centralization of some training programs, statewide coordinated recruitment process and technology, and benefits administration. These are high cost areas where efficiencies can be achieved through centralization of resources, focus and process.

2. **A review of the Chapter 126 of the General Statutes (State Personnel System) as it exists and recommendation for potential changes that enable an effective human resources culture and high performance workforce.**

Changes to Chapter 126 to improve the operation of the state personnel system have been included in the Appendix. (See pages 141 through 146 that compare the current law to proposed changes). These changes have been reviewed and approved by OSP, SEANC, local government and agencies, but have not been acted upon by the General Assembly. We encourage adoption of these recommendations.

3. **Recommendation for improving cost forecasting for executive budgeting and appropriation of salary and benefits by the General Assembly.**

Cost forecasting is currently complicated by the restrictions on lapsed funds, in-range adjustments, range adjustments and across the board adjustments. These are symptoms of a process that has piecemealed compensation based on the problem that causes the most pain at the time. The process should not be so difficult, but it requires a realistic assessment of the labor market. The current classification system does not make that easy, since the classification system have been so altered and manipulated over the years, that it is not clear where the State's rate of pay is for every occupational group. Our best assessment is that the State is paying, on average, about 7% below the competitive market. The implementation of career banding clarified the relation of pay to the market and it has made it easier to assess the pay impact of the current forecasting process.

Cost forecasting should be straightforward and direct. We recommend that the General Assembly receive a recommendation of labor market movement and performance based increases from the Office of State Personnel. They may use several sources, including projections from private companies (whose projections are typically within 2 tenths of a percent of each other), or from an assessment of the market changes from year to year of their benchmark classes, or by making projections from the Employment Cost Index published by the U. S. Department of Labor. This will provide the State with an estimate of the amount that the market has or will move, depending on if the State wishes to lead or lag the market. This percent (or some other number that the General Assembly believes is appropriate given economic conditions of the State) should be applied to each agency/university current midpoints of the current grades for each of the traditional classes, or the middle salary for the journey level among Career Banded jobs, including any lapsed funds) for the number of authorized positions of the agency/university to determine the salary amount that should be appropriated. Agency/university leadership should then be held accountable for proper expenditure of the funds up to the limits established and within the current guidelines, policies, procedures, restrictions and rules in place for their respective occupations.

- 4. Recommendations for State Policies, including but not limited to those related to BEACON, for attaining accuracy, tracking and integration of other salary and compensation information for appropriations for salaries and benefits and other entities where compensation is exempt from Chapter 126 of the General Statutes but set or predominately financed by the state.**

According to the Office of the State Controller, (OCS) BEACON is a software package that will track and integrate compensation, benefits and other human resources information from all agencies throughout the State for later retrieval and analysis. It will replace PMIS with faster, more accurate and more easily accessible data in a common format.

As the BEACON initiative is currently envisioned, nine of the sixteen universities will eventually be utilizing the standard applications. As a result, production of statewide HR reporting will continue to require the combination of data from fragmented sources to incorporate much of the university data. However, the consolidation process may be more

automated under BEACON than is the case currently thereby making the data more contemporary.

The State should require that all universities not using BEACON download their data in a timely fashion (at least monthly) to BEACON so that one data base exists to allow for State wide analysis of data.

BEACON will also allow the State to implement more effective analysis of employment trends and patterns and allow OSP to improve the auditing of processes that have been delegated to agencies/universities.

BEACON also will enable the State to automate and centralize the recruitment process through on-line recruiting. This should be a centralized function as noted elsewhere in this report.

5. Recommendations to improve effectiveness of all human resources functions including but not limited to the following:

- a. How North Carolina state government can improve its overall personnel system and human resources system given contemporary science and standards determined by the consultant.**

Currently, the State is using an ineffective 70-year-old classification system that serves neither the State nor its employees. In addition, the State does not have contemporary practices in place that will allow the State to quickly hire the right employees who are capable of performing the work that needs to be done. Its promotion policies do not reward competent performance; rather it rewards long-term service. Training and regrowing the workforce are considered in some departments as a luxury, rather than a necessity. As a consequence, some occupations are less well trained than the personnel in private sector companies that they are asked to regulate and/or monitor. Recognizing these issues, and looking forward to the possibility that there will be fewer workers in the workforce, OSP investigated a new program call career banding. The intent of this program was to shift the paradigm, from reactive management to proactive management of personnel. Career banding enables the State, and gives its managers the tools to change how it recruits, classifies, promotes and pays its personnel. Further, it enables managers to critically examine their operations

to determine if they have the right number of employees at the right costs to meet the needs of their constituents. As a result of the change, it has caused some sectors to question if this is the right path for the State. From our perspective, if the State is interested in overcoming the cumbersome practices that it currently has to manage pay and personnel, and is interested in determining what it should do in the future to proactively address the personnel issues of the future, career banding is perhaps the best program that can be envisioned at this time. Therefore, the State should require the implementation of Career Banding for all occupational groups. This system integrates workforce planning, recruitment, selection, hiring, performance management, talent management and compensation in a manner that, if implemented correctly, will transform and improve the overall management of personnel in the State. Such a system should be part of the delegated authority of OSP to the agencies/universities, with the oversight and final approval by OSP regarding implementation decisions.

Currently hard costs of recruiting (e.g., advertising and related expenses) cost the State in excess of \$29 million per year.¹

Recruiting process and technology should be coordinated statewide with the implementation of BEACON and other web based tools. The State may start such a process with hard to recruit positions and expand to others as the process is refined. The implementation of a centralized recruiting process and system is estimated to save approximately \$15 million in reduction of hard cost expenses (specifically advertising costs in each department and miscellaneous expenses) and will result in a greater number of applicants.²

Training should be centralized through the better utilization of the university resources available to the State.

Mandatory mediation should be required to handle grievances.

¹ Estimate from OSP based on average cost per hire including hard costs of advertising, travel costs, recruiter time and miscellaneous expenses for replacement of approximately 10% turnover.

² Estimate based on professional judgment incorporating best practices information and hard data from footnote above.

- b. **How to assure strategic workforce planning to assure sufficient policies and plans for enhancing attraction to state service, recruiting for immediate employee needs, and retaining a solid workforce to respond to immediate, intermediate, and long term human resources needs of the State of North Carolina.** GPAC received reports of concerns about loss of and failure to “re-grow” institutional knowledge stemming from increasing retirement of state employees in professional categories including financial, health care, technology, human resources, and general program management in addition to senior front line employees who perform critical support functions.

On-line Recruiting – The applicant pool is not as large as it could be primarily because applicants do not favor hand written applications nor do they want to apply for jobs at each agency/university that has an opening that matches their competencies. To improve the applicant pool, enable on-line application services available to all for any positions available within State government. eRecruitment, part of the BEACON implementation, should greatly enhance the State’s technological capabilities to achieve this.

Recruitment/Promotion - Currently, the graded classes depend on years in service as evidence of eligibility for promotion. This promotes and rewards seniority, not competency to do the work. It is an inefficient way to make the best use of the existing employee talent. Revise the recruitment and promotion program to focus on demonstrated competencies, as opposed to reliance on years of service and seniority as the requirement for hire or promotion. Career banding procedures give managers the capability to make this change.

Increase Applicant Pool – Agencies/universities advertise the full range of pay, when in fact, they have limited capability to hire at the rates advertised. This leads to false expectations on the part of the applicants and potential negative perceptions of the State as an honest employer. Further, when faced with a highly competitive labor market (such as for nurses) the State is not allowed to use hiring incentives to obtain needed employees. The

cost of hiring incentives can sometimes be less expensive than a position that is not filled, or filled by an inadequately prepared employee. Advertise realistic hiring rates that are market competitive and use on-line and national job postings, particularly for hard-to-recruit positions, and allow the use of recruitment and retention bonuses, moving allowances, etc. that have been proven successful in other organizations for special situations.

Public Perception – Job applicants are often times unaware of the variety of occupations and challenges that exist in government service. This is because the State takes no initiative to promote itself as an employer of choice. Frequently, employees must aggressively search and find State employment opportunities. Private sector employers make the process of applying for jobs easy by employing on line applications, and the use of on line web based job sites, such as Monster.com, Career Builder and Hot Jobs. Engage with media and employ other marketing approaches to raise awareness about the significance, competitiveness and challenges of State service.

Budgeting Process – The State has consistently paid below market competitive rates, making it sometimes difficult to fill needed positions. Further, the current rules severely restrict the use of lapsed salary funds to give agencies more flexibility to adjust salaries for critical jobs. Consistent with Section 126-7, (which states that “a. It is the policy of the State to compensate its employees at a level sufficient to encourage excellent performance and to maintain the labor market competitiveness necessary to recruit and retain a competent workforce. To this end, salary increases to State employees shall be implemented through the Comprehensive Compensation System based upon the individual performance of each State employee.” and

“b1. The Comprehensive Compensation System shall consist of the following components: (i) the career growth recognition award, (ii) the cost of living adjustment, and (iii) the performance bonus. The career growth recognition shall be the primary method by which an employee progresses through his or her salary range and shall be awarded annually to employees who qualify for the award.”) The General Assembly should budget positions at the market compensation rate and allow agencies the flexibility to use lapsed

salary funds such as is currently allowed in the universities. Amend Section 126 to allow for the use of lapsed salary funds for recruitment bonuses, moving expenses or retention incentives, as necessary to attract and retain high performing personnel or high demand skills.

Strategic Workforce Planning – Currently, most agencies/universities do not engage in workforce planning because the effort to change the structure of the classifications and pay is too onerous. It is easier to leave such questions for a later time, which never seems to occur. This lack of current and future assessments may not be the most effective way to meet current or future State needs. To encourage agency/management to take an introspective look at the way they do business and the talent needed to perform the work, we recommend that the State continue the implementation of career banding to encourage more focused workforce planning. This process forces managers to conduct a critical assessment of their personnel needs.

Overlapping Term of Service – Currently, State regulations permit only a limited overlap in service to permit knowledge transfer from an outgoing employee to a new one. This severely limits that ability of a new employee to “come up to speed” on their job and permits the loss of institutional knowledge. This practice may appear to save money but it severely impairs the ability of the State to deliver seamless service when an employee leaves. We recommend that the State permit longer overlapping terms of service to provide for knowledge transfer. Further, we recommend the removal of the 6-month restriction on returning to work for the State following retirement, under a “retraining” situation.

Retirement – When a person retires, they take with them years of knowledge, skills and history. Often times an employee would like to continue to work but at a lower time requirement. Approximately 13% of private companies have implemented a phased retirement program to provide for a more orderly retirement and to retain institutional knowledge so that it can be transferred to new

employees.³ We recommend that the State permit phased retirement options to maintain the knowledge base and facilitate knowledge transfer.

Career Banding - as applied in North Carolina, is the most effective method currently available in human resources that will seamlessly integrate workforce planning with the recruitment, hiring and selection of needed employees in the short and long run.

- c. **Training and development of employees at all levels and the extent to which there should be more statewide training programs offered by a central training and executive development program to complement training offered by individual state agencies exclusively to their employees. The consultant should identify best practices within agencies or by educational institutions that could be used as models or scaled up to accommodate the state employee community.**

The State currently has an enormous resource available to it for training and upgrading its workforce: the State universities and colleges. This resource is currently not adequately used to identify occupational training programs to train and retrain its workforce. Agency management often does not allow employees to be trained, nor in some cases does the State pay for professional certification. Best practices in industry suggest that a minimum 2.2% of salary should be devoted to training.⁴ It is not possible to identify how much the State now spends. The State should require at least 2% of each agency/university personnel budget should be devoted to training. Mission critical employees should be required to obtain 20-40 hours of training each year, or 60-120 hours every three years, related to their job. Consideration should be given to extending university on-line and other educational resources to agencies to meet training needs. E-learning should be embraced, facilitated by universities and integrated into the career development program of every State employee. With career

³ The Aging of the U. S. Workforce: Employer Challenges and Responses, Ernst & Young, January 2006

⁴ American Society for Training and Development, "State of the Industry in Leading Enterprises", 2006.

banding, the State will have the information available to identify the competencies and training that is needed to develop a coordinated approach. At the very least, resources should be made available to allow employees to retain and achieve needed licenses and certifications of their profession. Specific attention should be given to personal safety training for employees at risk from custodial populations. OSP should facilitate the identification of specific training solutions to address HR issues with each agency.

For example, OSP should continue to provide training in the general areas of:

- Management and supervisory skills
- Performance evaluation
- Equal employment opportunity
- Customer service
- Certified Public Manager program

These courses should be mandatory for supervisors and managers, and may be augmented by additional departmental training for specific agency applications and situations.

- d. Improving basic functions of position classification and reclassification, recruiting, selection, compensation, discipline, termination, separation, and appeals. However, the consultant should not conduct a detailed management or process oriented review of such functions, but instead determine if basic functions should be continued as operated, improved, or discontinued if there is a cost-effective alternative.**

Classification - We advise the State to abolish the current classification system. It is not repairable, does not assist the State to achieve its objectives in the near or long term, and is more costly to that State in terms of pay increases, managerial and employee time and Office of State Personnel oversight than career banding. The system is obsolete, and needs to be replaced. Career banding should be implemented to replace the current system.

Recruiting - eRecruitment, and other web-based solutions should be integrated as a statewide system of recruiting, selecting and

hiring personnel for all agencies throughout the State. The number and quality of the applicants will increase substantially.

Compensation - The State has not funded the compensation system according to Chapter 126. Chapter 126 states “(a) It is the policy of the State to compensate its employees at a level sufficient to encourage excellent performance and to maintain the labor market competitiveness necessary to recruit and retain a competent workforce. To this end, salary increases to State employees shall be implemented through the Comprehensive Compensation System based upon the individual performance of each State employee.” and

“(b1) The Comprehensive Compensation System shall consist of the following components: (i) the career growth recognition award, (ii) the cost of living adjustment, and (iii) the performance bonus. The career growth recognition shall be the primary method by which an employee progresses through his or her salary range and shall be awarded annually to employees who qualify for the award.”

Consequently, this has forced managers to sometimes hire poorly qualified employees, or seek out alternative ways to reward good employees, such as through in-range adjustments, reclassification requests and other techniques. Often times these practices are seen as “gaming the system.” The State could significantly reduce these practices by funding the currently authorized compensation programs at a level that is consistent with market competitiveness and sound human resource practices.

Discipline/Termination/Separation/Appeals – Currently, the process of discipline/termination/separation and appeals is costly, time consuming and adversarial. It could be argued that such a process does not serve the employees or the State very well. Progressive organizations have adopted a mediation process that is considered less adversarial. Some agencies have used this approach and found it to be more effective for correcting an issue early. Further, the process is quicker, more respectful of the employee and far less costly to the State than the current process. We recommend that the State adopt a mandatory mediation policy for all grievances and potential separations. This would not

eliminate the grievance process, but would be a step prior to legal action.

6. **The primary purpose of the project is to evaluate the overall personnel system and to identify needed improvements. Career Banding is to be evaluated in the context of the system-wide review. The evaluation of the Career Banding component shall include but not be limited to:**

- a. **A historical review of Career Banding as implemented outside North Carolina including references and web links to professional literature about its applicability to state government.**

Career Banding has been in existence in state government since 1996. No other state implements career banding in the same fashion that the State of North Carolina does, therefore there are no other models to compare the State to because the process used by the State is a more complete and thorough process. Most other states have simply modified the salary range, but have not incorporated competency assessment as the State has. We believe that it may be the only process at the present time that will meet the State's need for identifying the right number of employees, performing the right tasks at the right level of compensation. No other classification or compensation system integrates all these aspects into one consistent system. The State would be wise to proceed with its implementation as fast as it is possible, given the current staff.

- b. **A critical analysis of Office of State Personnel Career Banding policies and procedures including but not limited to identification of strengths and weaknesses.**

The State has implemented the Career Banding system of classification and compensation that is more complete and integrated than any other in the country. Procedures are in place to handle all personnel transactions with the appropriate oversight and controls by the OSP. Its full implementation should be continued.

Its weaknesses are that it is new and employees and managers have to adjust to new rules and procedures. That is not a fault of the system, but a change management issue. It can be overcome.

c. How to assure that agencies do not abuse Career Banding to escalate state salary costs without legislative authorization and budgetary control.

The current system of legislative authorization for salary increases under the traditional classification system does not contain salary increases. We found that the current classification and compensation system costs the State more in salary increases than Career Banding. The procedures in place for Career Banding control potential salary abuse whereas the current graded system has not. Average salary increases under career banding have been about half of the average increases under the traditional system (\$1,236 for career banded classes and \$2,365 for traditional classes).

d. A summary conclusion by the consultant concerning whether Career Banding should or should not be continued in North Carolina

Career Banding should be implemented throughout all but a few public safety positions in the State. Corrections officer classes may not be appropriate for career banding.

e. Any changes to the current Career Banding system recommended by the consultant if the consultant concludes that Career Banding should be continued.

We are of the opinion that the current format and process of career banding is one of the most well thought out and cohesive programs in the country. It should be implemented as quickly as it can be done. There are, however, areas that could be improved, specifically:

Consistent Pay Policy – Currently the State has one pay policy for teachers, but at a different policy for State employees. For teachers, the policy is to pay at market competitive levels. For State employees, there is no such policy. This is inconsistent. The State should adopt a consistent pay policy and pay in accordance

with its policy.

Pay Consistency – Currently, under Career Banding, the same job may be paid a different rate in different agencies because of need. This is inconsistent with the State being one employer, and makes each agency a competitor with all other agencies. There should be pay consistency among agencies for similar jobs. Pay consistency should be defined as within 10% of median pay levels. The State should be perceived as “one employer” rather than having separate pay practices (pay levels) for each agency.

Oversight and Approval – With any new program, it is important that the same rules apply to all employees. Until career-banding implementation is complete, OSP should continue to provide oversight, guidance, and approval of career banding agency and university efforts.

Performance and Competency Linkage – Currently, the performance evaluation instrument and the competency assessment tools have different scales. This is confusing and requires a cross walk from one to the other. It should be simplified. OSP should link the performance appraisal rating scale with the competency assessment ratings.

Evaluation and Assessment – Even though career banding has been in place in the State for a number of years, the experience base has been minimal. With any new program, it should be assessed with objective data. While an attempt has been made in this report to provide that data, the PMIS does not capture it, or it is in a form that is not accessible. With BEACON, this should be remedied and data should be more easily accessible on performance criteria that we have used in this report. The General Assembly should audit the implementation of career banding two years after the last occupational group has been banded, with a specific focus on its effects, costs, management resources required, consistency of application and impact on workforce quality, in comparison with the current graded classes. Measures of turnover, recruitment quality, grievances, compensation, should be obtained for the graded classes and new data on the career-banded classes should be collected to assist in the comparison effort.

- f. Any creative alternatives to Career Banding that may be recommended by the consultant along with potential strengths and weaknesses. Alternatives to Career Banding should be explored and reported even if the consultant recommends continuation of Career Banding.**

Career banding is at the peak of refinements of currently available progressive classification and compensation techniques. There are no other practices that are better than Career Banding for implementation of a cohesive, consistent program to enable the right number of the right employees to be hired, doing the right things for the right amount of money. Skill based pay does not achieve each of these objectives as well as career banding, consolidating titles or broadbanding will not accomplish these objectives and incentive pay programs or pay for performance programs alone will not solve the State's talent management concerns.

The State should require that Career Banding be implemented and should fund the pay levels to assure its success. The salary cost to the State to achieve market parity is estimated to be approximately \$350 million in additional salary and benefits costs. This is approximately 7% of the total salary and benefits budget for State Personnel Act employees.

- g. Suggested timetables for implementation steps for recommendations and what state offices should be responsible for any future actions related to Career Banding or alternatives to Career Banding recommended by the consultant.**

OSP believes that career banding can be implemented in all occupational groups within 3 to 5 years. This will require OSP leadership, training, guidance and oversight. It will also require dedicated support and time from agency management and agency HR professionals if this process to be successful. The process should be required. Estimated cost for implementation of salary adjustments that will be required is \$350 million over three years.