

THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

THE DEVELOPMENT OF THE SENIOR EXECUTIVE SERVICE
PERFORMANCE BASED PAY

SENATE STANDING COMMITTEE ON FINANCE
AND PUBLIC ADMINISTRATION

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RECOMMENDATIONS

The Committee recommends that performance based pay not be introduced for the SES until a formal study of the costs and benefits of the proposal has been undertaken and it has been established that significant net benefits are likely. (Paragraph 40)

The Committee recommends that action be expedited on other initiatives to improve SES conditions, particularly the introduction of the SES specialist stream. (Paragraph 41)

The Committee recommends that, if performance based pay is introduced, a task force with membership drawn from both coordinating and line agencies be established to manage its implementation. (Paragraph 45)

The Committee recommends that, if performance based pay is introduced, the implementation task force report to the Public Service Commissioner. (Paragraph 46)

The Committee recommends that performance based pay, if introduced, be implemented first in agencies in which effective staff appraisal systems have operated for at least one year and have been independently evaluated. The system should not be extended to other agencies until their appraisal systems have also operated for at least a year and have been independently evaluated. (Paragraph 48)

The Committee recommends that agencies be permitted to develop their own appraisal systems to Public Service Commission guidelines as currently proposed but that no agency be permitted to implement performance based pay until its appraisal system is independently certified to be effective. (Paragraph 52)

The Committee recommends that the proposed implementation task force devise certification procedures which include surveys that establish staff acceptance of the fairness, validity and reliability of the appraisal system. (Paragraph 52)

The Committee recommends that the full results of the evaluation of the appraisal process be made public. (Paragraph 52)

The Committee recommends that, if performance based pay is introduced, it be introduced for the SES and the feeder groups at the same time and under the same system in each agency. (Paragraph 56)

The Committee recommends that, if performance based pay is introduced, details of any payments be made public. (Paragraph 66)

The Committee recommends that, if performance based pay is introduced, it be paid largely or wholly in the form of bonus payments rather than as a supplement to regular salary payments so that it not be factored into an officer's regular living expenses. (Paragraph 69)

The Committee recommends that, if performance based pay is introduced, the implementation task force devise a continuing system for monitoring the pay scheme to ensure reasonable consistency in performance pay policies across the Service. (Paragraph 72)

Introduction

1. The Committee began its inquiry into the development of the Senior Executive Service (SES) of the Australian Public Service in June 1989. A copy of the terms of reference for the inquiry is at Appendix I. The Committee has so far taken 1551 pages of formal evidence and proposes to report fully on the reference in the middle of 1990. Written submissions were received from 49 persons and organisations, listed in Appendix II, and the Committee heard evidence from 44 witnesses, listed in Appendix III.

2. One issue which emerged early in the inquiry was that of performance based pay for SES officers. The Committee considered it desirable to make public its concerns on this proposal at an early date so that they can be taken into account when decisions are made on the performance pay proposal. If appropriate, the Committee may return to this issue in more detail in its main report later in 1990 and would welcome responses to this document.

The proposal for performance based pay

3. Australian public services, like the civil services of most countries, have traditionally related pay to position occupied and length of service in the position rather than the qualities of the particular occupant. Positions in turn have been classified in a hierarchy of responsibility with individual merit being rewarded by promotion to a higher position rather than by higher payment in the initial position. An alternative approach is to tailor pay to individual performance so that occupants of jobs of similar levels of responsibility may be paid at different levels. There appears to have been some movement in that direction by public services over the past decade.

4. In Australia, the Victorian Public Service adopted a performance based pay system in the mid 1980s and has recently moved to substantially revise the system following implementation problems (Evidence Vic. PSB, p. 43). New South Wales adopted a contract system in 1989 which does not directly link remuneration to performance but is more flexible than the traditional public sector model. Performance based pay systems have applied for more than a decade in the United States and Canada and were adopted for some staff in the British Civil Service more recently. The Committee was told that more than a third of OECD countries now have some system of performance based pay in their civil services (Evidence DIR, p. 568).

5. Initial written submissions to the Committee from the Department of Finance and the Department of Industrial Relations made it clear that the Government intended to move towards performance based pay for the SES and the groups of staff immediately below it (Evidence DIR, DOF, pp. 424, 1050). However, the submissions on this subject gave no indication that the need for a new system was urgent. The Department of Finance, for example, stated:

On balance, Finance considers there is a need to increase remuneration particularly at senior levels of the SES and to provide part of the SES remuneration in an 'at risk' element. (Evidence DOF, p. 1050)

The Department of Industrial Relations commented:

Developments in award restructuring negotiations, and in particular the opportunities for more efficient working arrangements which are being negotiated with unions under the Structural Efficiency Principle of the National Wage Case Principles, provides a good opportunity to introduce performance based pay arrangements.

...

We will keep the Committee informed of progress in the Structural Efficiency Principle negotiations (Evidence DIR, p. 425).

6. The departments with responsibility for SES pay and conditions placed considerable stress in their initial submissions on the risks associated with performance based pay and the need for careful implementation of such a system. Early in its discussion of performance based pay, the Department of Industrial Relations commented:

Overseas experience in the public sector has shown that difficulties relating to, for example, subjectivity in appraisal, lack of valid connections with organisational goals, have been encountered. The development of any performance pay approach in the SES will need to clearly recognise and capitalise on available methodologies to overcome these difficulties (Evidence DIR, p. 423).

The Department of Finance noted:

While strongly attracted to the concept, Finance is well aware that performance-related pay systems are by no means always successful, especially if attempted without a strong underpinning of performance appraisal.

7. Despite these official reservations, negotiations on performance based pay were begun with relevant staff associations in 1989. On 29 January 1990, the Committee was advised by the Department of Industrial Relations that, on 22 December 1989, the Industrial Relations Commission (IRC) had endorsed new pay and structural arrangements for the SES. These included introduction of performance appraisal 'paving the way for the development and implementation this year of a results-oriented, performance pay system to recognise and reward

outstanding achievement' (Evidence DIR, p. 518). The Department stressed, however, that the IRC will not make a final decision on performance based pay until the outcome of a review of paid rates awards.

8. Further evidence that early introduction of performance based pay for the SES was likely came with an announcement by the Minister for Defence Science and Personnel that a similar pay system would be implemented for senior officers of the armed services, subject to IRC approval of the concept (Simmons 1990). This announcement drew public opposition from the Armed Forces Federation of Australia (Scott, 1990).

9. Evidence from the Public Service Commissioner and officers of the Departments of Industrial Relations and of Finance made it clear that, subject to IRC agreement, performance based pay will be introduced as early as 1 July 1990 (Evidence DIR, PSC, DOF, pp. 568-9, 1014, 1106). This was despite acknowledgement by the officers that there were significant potential risks associated with the proposal (Evidence DIR, PSC, DOF, pp. 569, 1021, 1106). At the same hearings, the Committee heard from a range of non-official witnesses, including representatives of staff associations. Almost without exception, these witnesses were sceptical of the plan for performance based pay with particular concern being expressed at the proposed implementation date of 1 July 1990.

10. The Committee found that, although the scheme is to be introduced in a few months, decisions have yet to be made on such important structural and operational features as:

- whether the existence and amount of performance based payments to particular individuals will be public knowledge;
- what proportion of the SES will receive performance based pay;
- whether that proportion will be broadly consistent across departments;
- whether payments will be made as an addition to fortnightly salary payments, as an annual bonus or as some combination of the two;
- how much additional funding will be made available to support the scheme.

11. The Committee found that witnesses from departments and agencies other than the three which are coordinating the proposal had widely differing expectations of these and other aspects of the plan. For example, a deputy secretary of the Department of Community Services and Health expected that almost all his SES staff would receive some performance payment while his counterpart from the Department of Veterans' Affairs expected that the additional payments would be reserved for 'above average performers' (Evidence DCSH, DVA, pp. 923, 930). When the Committee took evidence from a panel comprising the Secretaries of the

Attorney-General's and Defence Departments, the Commissioner of Taxation and the Auditor-General, these very senior officers could do no more than speculate on several of the structural and operational aspects (Evidence, pp. 868-84).

12. The Committee was also concerned to find that very few departments or agencies currently have any formal system of staff appraisal. Officers from the coordinating departments acknowledged that the proposal will depend for its success on the reliability and validity of the staff appraisal system that underpins it. Equally crucial will be staff perceptions of the fairness of the appraisal system. If the performance based pay system is to commence on 1 July 1990, employing agencies of the vast majority of SES officers will need to first implement appraisal systems and then immediately use those appraisal systems to allocate additional payments to staff. The risks associated with that process are obvious.

13. A further source of concern to the Committee is an apparent lack of central coordination of the proposal. The Department of Industrial Relations, the Department of Finance and the Public Service Commission each have carriage of separate parts of the project. The Committee is not confident, after hearing evidence from officers of these agencies, that their activities have been adequately coordinated or that the policy implications of the proposal have been fully considered.

14. The Committee was surprised to learn that the the issue of performance based pay had not been discussed by the Public Service Management Advisory Board (Letter to Committee 2.3.90). The Board is established under section 22 of the Public Service Act to 'advise the Government on significant issues relating to the management of the Australian Public Service; and ... to be a forum for consideration of management activities affecting the Australian Public Service as a whole' (*Public Service Act 1922*, s.22). The introduction of performance based pay would appear to qualify under both these headings and the secretaries of the three coordinating agencies are *ex officio* members of the Board.

15. The Committee was advised that, although the Board had not considered the introduction of performance based pay, it had discussed performance appraisal at its March 1988 meeting. At that meeting, the Board agreed to a proposal by the Public Service Commissioner that the proposed appraisal system focus 'at least for the next few years, on the improvement of the individual's management ability rather than on use in selection and placement' (Letter to Committee 2.3.90, attachment). The Commissioner argued:

It will take the commitment, the time and the energy of senior officers to fully realise the benefits of appraisal. Implementation will be an incremental process. The experience of the British and Canadian Civil Services is that it can take some years for appraisal to be fully accepted as an integral part of the management culture and to build up a high level of skill in setting goals and giving feedback on performance (Letter to Committee 2.3.90, attachment).

16. Thus, in March 1988, the Management Advisory Board, the Government's chief advisory body on public service management, was reluctant to use an untried appraisal system in selection and placement. The Committee was surprised that, less than two years later, and without further reference to the Board, it could be proposed that the same untried system be used to determine pay relativities between individuals. The reservations expressed about use of the appraisal system in selection and placement would seem to apply with equal or greater force to its use in determining pay.

17. Overall, the Committee has serious concerns about the rationale for the introduction of performance based pay for the SES, the proposed arrangements for its introduction and the uncertainty about some structural and procedural aspects. Those concerns are discussed in the following paragraphs.

The rationale for performance based pay

18. The main theoretical justification for linking the pay system to performance is to provide an incentive for improved performance. Other possible reasons for moving to performance based pay are that it is just that merit be rewarded and to prevent possible loss of the best performers to other organisations. It was also suggested to the Committee by some witnesses that the current proposal for the SES involved an attempt to evade the IRC wage guidelines (Evidence POA, p. 723).

19. Dr Michael Keating, the Secretary to the Department of Finance stressed to the Committee that performance based pay was consistent with the broad thrust of other public sector reforms of recent times and should be seen as part of a wider process aimed at producing a more results oriented public service (Evidence DOF, p. 1079). Dr Keating further argued that, given the relative security of tenure in the public sector, 'if anything you need a bit more carrot because you are not going to have much of a stick' (Evidence DOF, p. 1107).

20. Most of these reasons have some intuitive appeal. However, there appear to be particular difficulties for public sector organisations in securing benefits from performance based pay. The Committee was advised by Professor Robert Wood of the Graduate School of Management at the University of Western Australia that three classes of problems are likely in implementing performance based pay in the public sector (Committee paper 17 April 1990).

21. Firstly, Professor Wood argued, there are measurement problems. It is difficult to identify and place a value on changes and to attribute responsibility for them to individuals in much of the public sector. Performance based pay will only work if pay is linked, and is seen to be linked, to performance. But measurement of performance is inevitably highly subjective, especially in the public service. What is quantifiable is often trivial, especially when the job involves provision of advice or

services. The outputs of service and advisory jobs are highly intangible and highly perishable. Their quality is strongly influenced by the client. Comparability across jobs and agencies in this sort of work is also difficult.

22. Professor Wood argued, secondly, that problems with perceptions of equity are likely. The pay system contributes to employees' satisfaction with their jobs and the contribution of performance based pay will be negative if it is not perceived to be equitable. This leads back to the measurement problem. In principle, the equity problem can be avoided if the measurement system is open and acceptable to employees. Alternatively, perceptions of inequity can be avoided by maintaining privacy on performance payments, as is commonly the case in the private sector. It may be also, in the case of the private sector, that expectations of equity are weaker.

23. For reasons discussed later in this report, privacy on remuneration matters is undesirable in the public sector and may well be impossible anyway. Expectations of equitable treatment are likely to be high in the public service. As a result, the problem of perceived inequity in any performance based pay system in the public sector will clearly be important.

24. A third category of likely problem with performance based pay, identified by Professor Wood, is related to the difficulty of changing organisational culture. Problems of this type have arisen with the introduction of performance based pay in other public services. It is not only that public servants, as a rule, are likely to have strong views on the need for equity and the measurement and equity problems described above will be therefore be particularly significant in the public sector. It is also the case that the philosophy of performance based pay is at odds with the traditional professional ethos likely to be strongly represented in much of the public service.

25. This problem was also raised at a Committee hearing by J.R. Nethercote, who said:

[Performance based pay] misinterprets the motivations of our officials ... They want reasonable remuneration but one reason we can have confidence in our senior officialdom is that monetary incentive is not uppermost in their minds. ...Most significantly, [Performance based pay] will be corrosive of a fundamental quality in public departments. To run successfully, they call for a high degree of collegiality and cooperation at senior levels (Evidence p. 1129).

26. The relevant academic literature appeared to lend support to these views. While the Committee was not able to make a full survey of the extensive literature on this question, the Department of Industrial Relations drew its attention to two substantial survey articles on the question. That material provided only limited support for the performance pay concept.

27. The Technical Cooperation Service of the OECD, in a 1988 paper reporting on public sector performance based pay schemes in OECD member countries, concluded:

Although the main rationale for establishing performance related pay schemes is to improve performance, there has been very little evaluation of whether improvements have actually occurred and whether benefits justify costs. ... a major conclusion is that satisfactory implementation requires a considerable amount of time and effort. A number of schemes have suffered from negative reactions on the part of staff because of problems in linking rewards clearly to performance and because they were inadequately funded (Evidence DIR, p. 440).

28. An authoritative review of the merit pay system in the US Federal Civil Service reported that 'most behavioural scientists believe in the merit pay principle and attribute the frequent failures of merit pay to inadequacies in its implementation' (Pearce & Perry 1983, p. 316). The study found that the US merit pay system had suffered 'many difficulties' when introduced and, while action could be taken to resolve these difficulties, it would be inadvisable to extend the scheme immediately to lower grades as had been proposed (Pearce & Perry 1983, pp. 324-5). The principal causes of the difficulties were failure of the performance appraisal system, perceptions of unfairness when quotas led to highly rated managers failing to receive merit payments and the difficulty of defining good performance in the ambiguous performance environment of the public sector.

29. In a lecture given in Canberra in June 1988, David Laughrin, a senior officer of the British Civil Service, reported that the introduction of performance based pay for some elements of the Civil Service encountered a number of problems. It was, he said:

much more difficult to deal with resistance and scepticism about the schemes than many of those responsible ... expected. This was because they challenged the cultural values of the civil service. These values included an attachment to fairness, equity of treatment, openness on remuneration, and work relationships based on teamwork and group results. ... The result was that some of the early recipients, against all expert predictions, refused bonuses, paid them to charity, or shared them with their staff (Laughrin 1988, p. 3).

Mr Laughrin also cited problems in developing an effective staff appraisal system and in securing sufficient funding for the scheme, as well as anecdotal evidence of demotivating effects on those not receiving awards (Laughrin 1988, pp. 3-4).

30. Professor Rainer Koch of the University of the Federal Armed Forces of Germany told the Committee that the introduction of performance based pay in the West German Federal Civil Service in the early 1970s had been unsuccessful and

the scheme had been quickly abandoned. The main reasons he cited were the difficulty of defining individual contributions to corporate performance in much of the public sector and a lack of acceptance of the performance appraisal system by those being appraised (Evidence Koch, pp. 975, 980). Professor Koch argued that the theory on motivation which supports the extension of performance based pay to the public service is incorrect (Evidence, Koch, pp. 959-960, 984-5). The perceptions that individuals hold of their own worth relative to that of others are never likely to coincide with an official ranking and it may be impossible for a public sector employer to pay what individuals perceive to be a just level of remuneration (Evidence Koch, pp. 975-8).

31. Some management experts argue on similar grounds that the costs of performance based pay usually outweigh the benefits. W. Edwards Deming, the originator of the total quality control concept, was recently quoted as saying 'The rating system ...[is] demoralisation, a method to destroy people' (Thomas 1990). Those who expect large improvements from performance based pay might also be depressed by the opinion of another well known management theorist, Peter Drucker, who has commented, 'there are no good executive compensation plans, there are only bad and worse' (Tarrant 1976, p. 257). However, as noted above, other theorists see potential net benefits for performance based pay if implementation is properly managed and, in particular, if the staff appraisal system is effective (Pearce & Perry 1983, p. 316).

32. The common thread here is that performance based pay can have a detrimental effect on motivation. The possible costs of attempting to link pay to performance include the demotivating effect on staff not rated as eligible for performance based pay, antagonism between groups participating in the new pay system and those which do not and adverse effects on group cohesion and cooperation. Performance based pay systems may also produce a disproportionate focus on the reward system, to the detriment of organisational goals and it can be difficult to separate individual performance from group performance. In many parts of the public sector, it may be difficult to define performance at all.

33. The Public Service Commissioner and representatives of the Departments of Finance and of Industrial Relations made it clear that they were fully aware of the likely difficulties of implementing performance based pay. While acknowledging the likely problems, they argued that the benefits of proceeding could be expected to outweigh the costs. They also argued that the expectations of SES officers on the matter were now so high that delay would have an adverse effect on morale.

34. The precise extent of the cost-benefit balance in this case is difficult to determine since most of the official witnesses were vague on the exact nature of the anticipated benefits. The scheme was repeatedly commended more for its contribution to justice than to effectiveness. The Committee was often told of a need to provide greater rewards for the best performers as though that need was self evident. When justification was offered, it rested more commonly on the need to retain staff who would otherwise leave the public service than on the possibility

of motivating other staff to perform better. Some witnesses believed that most SES staff in their agencies would receive performance pay, a situation more suggestive of a disguised pay rise than an incentive for better performance.

35. It would clearly be easy for the primary focus of performance based pay to shift from motivation of better performance to retention of staff whose skills are in high demand outside the public service. The new system would then become market rather than merit related. In evidence to the Committee, Dr Marian Sawyer made this point and commented:

As we have a gender-segregated labour market in which female areas such as human services are generally under-valued, the closer alignment of SES and private sector salaries would effectively exacerbate existing gender inequalities in the public sector. While existing SES salaries may be low compared with salaries in private corporations, they are very high compared with those in non-government community organisations, a factor which has inhibited ... mobility between the SES and community organisations (Evidence p. 1543).

If there is a case for market parity in SES remuneration, it clearly should be argued openly, allowing full consideration of issues like those raised by Dr Sawyer. It would be undesirable to seek to achieve market parity in the guise of performance based pay.

Possible alternatives

36. If loss of better performers among senior staff is the main problem, there are other options for dealing with it. The evidence from the Department of Finance and that of several agencies employing professionals suggested that, to the extent there is a staff retention problem, it is most acute among professionals in a few agencies. The Taxation Commissioner, the Auditor-General and the Secretary to the Attorney-General's Department expressed particular concern at the loss of skilled staff from their agencies. There also appear to be problems in retaining senior staff in locations outside Canberra and, particularly, in attracting and retaining staff in Sydney. In addition, a recent reduction in the age profile of the SES may have blocked promotion opportunities causing some difficulty in retaining talented staff both in the SES and in the groups immediately below it.

37. If it is true that the problem of loss of key staff is concentrated in these few areas, it is likely that solutions directed at specific targets might be more effective than the general introduction of performance based pay. In particular, a decision to expedite development of a specialist stream of the SES, already approved in principle by the IRC, could resolve much of the staff retention problem. It also should be possible to improve substantially the conditions of the few SES staff outside Canberra at relatively little cost. For example, it was suggested by the Auditor-General that it might be possible to pay an allowance to staff affected by

high living costs in Sydney (Evidence, p. 880). Other evidence, which the Committee will consider in more detail in its main report, suggests that there is scope for considerable improvement in the training and development opportunities open to SES officers. Each of these relatively cheap and simple measures could be expected to facilitate staff retention without risking demotivation from faulty or hasty implementation of performance based pay.

38. The evidence before the Committee was unanimous that the introduction of formal performance appraisal in the SES would have beneficial effects even if not accompanied by performance based pay. There was also widespread agreement that performance based pay systems place a significant additional burden on the appraisal process. The proposal to introduce performance based pay at the same time as an appraisal system will clearly place at risk the benefits that could be expected if the appraisal system were introduced by itself.

39. The evidence available to the Committee did not convincingly demonstrate that the benefits of performance based pay would outweigh the costs. Nor did it show that any net benefit that might result would exceed the possible benefits available from alternative measures. Even if performance based pay offers net benefits in the long term, the Committee was concerned that significant unnecessary short-term costs could be incurred by the over-hasty introduction of the scheme. We were particularly concerned that no serious study appeared to have been made of the costs and benefits of the proposal or of possible alternatives.

40. The Committee is far from convinced that it is desirable to introduce performance based pay at all. Some members have already concluded that the concept is inappropriate and fatally flawed. **The Committee recommends, therefore, that performance based pay not be introduced for the SES until a formal study of the costs and benefits of the proposal has been undertaken and it has been established that significant net benefits are likely.**

41. The Committee accepts the evidence of several senior officers to the effect that high expectations of performance based pay have developed in at least some areas of the SES. To counter any adverse effects on morale that might arise from the previous recommendation, **the Committee recommends that action be expedited on other initiatives to improve SES conditions, particularly the introduction of the SES specialist stream.**

Implementation

42. It is clear from overseas experience of performance based pay that success depends on careful implementation. If performance based pay is to be introduced, the Committee believes that the following issues should be considered.

Coordination

43. The Public Service Commission has responsibility for SES staffing including the recruitment process, selection criteria and the performance appraisal scheme. The Department of Finance controls the numbers and levels of SES staff and implements government decisions on levels of funding. The Department of Industrial Relations is responsible for negotiating with staff associations, under the IRC umbrella, on the structure and operation of the proposed performance based pay system. The Committee is not convinced that there is adequate coordination of the activities of these agencies.

44. The Committee was given no evidence of anything approaching an implementation plan. There was obvious confusion about the detail of the proposal among senior representatives of line agencies. Representatives of the coordinating agencies were often not aware of the details of parts of the project that other agencies were undertaking. There was no evidence that an overall assessment of the proposal has been attempted by any of the three agencies responsible. It was not entirely clear who would be accountable, should the project fail.

45. It is widely accepted that the introduction of any discrete new system is a task requiring clear lines of responsibility and control. The task force model of management is a well established means of managing this type of project. The introduction of performance based pay for the SES is a major project involving a material increase in government spending, probably of the order of \$10-20 million per year if current speculation on the likely level of payments is correct. There could be significant costs if implementation is mismanaged. **The Committee recommends that, if performance based pay is introduced, a task force with membership drawn from both coordinating and line agencies be established to manage its implementation.**

46. The main responsibility for SES matters lies with the Public Service Commissioner. In particular, the Commissioner is responsible for the staff appraisal system which is universally acknowledged to be the key to the success of the whole proposal. **The Committee recommends that, if performance based pay is introduced, the implementation task force report to the Public Service Commissioner.**

Phased implementation

47. It appears to have been almost universally the case overseas that significant lessons about the operation of performance based pay were learned during the implementation period. This was also the case in Victoria, where the first version of performance based pay is to be replaced by an extensively modified system. There is thus some argument for phasing in the introduction of performance based pay so that the lessons derived from experience can be promptly applied.

48. This case is greatly strengthened in the case of the Commonwealth SES by the current absence of formal staff appraisal schemes in most agencies. As the Committee noted in paragraph 12, a successful appraisal system is required if performance based pay is to succeed. Scope thus exists to phase in performance based pay by linking it to the introduction and testing of appraisal schemes. The lessons learned from implementation of performance based pay in agencies with functional appraisal schemes could then be applied to other agencies. **The Committee recommends that performance based pay, if introduced, be implemented first in agencies in which effective staff appraisal systems have operated for at least one year and have been independently evaluated. The system should not be extended to other agencies until their appraisal systems have also operated for at least a year and have been independently evaluated.**

49. If performance based pay is found to offer net benefits and its implementation is phased in this way, early access to the benefits of the scheme will be available to the Attorney-General's portfolio. That portfolio already has a functional performance appraisal system and is an area in which the staff retention problem is said to be particularly acute. More generally, phased implementation will allow earliest access to the benefits of the scheme to those agencies which are already meeting the basic management responsibility of providing staff with proper appraisal of their performance. Further phased introduction will continue to reward the best managed agencies. The concept of rewarding good management performance embodied in this proposal is wholly consistent with the thrust of recent public service reforms and, indeed, with the philosophy of performance based pay.

Certification of appraisal schemes

50. The current proposal for staff appraisal provides for each agency to establish a separate appraisal scheme consistent with guidelines issued by the Public service Commission last year and reproduced in Appendix IV to this report. Much of the responsibility for design as well as implementation of the appraisal systems will thus be devolved to agency level. There will be scope for considerable variation in appraisal systems across the SES and there is currently no proposal for review of agency performance in appraising staff.

51. While the Committee does not always oppose the concept of devolution, it has argued in other recent reports that devolution of authority always implies the need for enhanced accountability. Agency compliance with government policy should depend on more than the honour system, especially on a matter as important to good personnel management as a staff appraisal system. There is clear scope for some central effort to encourage, monitor and enforce a high standard in appraisal systems across the public service. The establishment of at least 18 separate staff appraisal systems for SES officers also points to the desirability of a central clearing house so that agencies can be quickly made aware of innovations, errors and lessons learned in other agencies or portfolios.

52. The Committee believes that there is scope for more central involvement in the design and operation of appraisal systems than is currently proposed. A simple approach, which would preserve the benefits of devolution, would be a requirement for independent certification of appraisal schemes. **The Committee recommends that agencies be permitted to develop their own appraisal systems to Public Service Commission guidelines as currently proposed but that no agency be permitted to implement performance based pay until its appraisal system is independently certified to be effective. The Committee recommends that the proposed implementation task force devise certification procedures which include surveys that establish staff acceptance of the fairness, validity and reliability of the appraisal system. The Committee recommends that the full results of the evaluation of the appraisal process be made public.**

Feeder groups

53. The Committee has received a substantial body of evidence suggesting that the problems in the SES which performance based pay is intended to address exist in equal or greater measure in the groups immediately below SES level, the so-called feeder groups. The performance based pay proposal extends to the feeder groups but the Committee was told that implementation at that level would be more complicated, largely because of greater involvement by unions in the approval process. There are implications in the evidence presented to the Committee that different schemes may eventually be adopted for the SES and the feeder groups. The Committee is concerned that the proposal to implement performance based pay for the SES before it is extended to the feeder groups may exacerbate morale and retention problems in those groups. The Committee is concerned also that development of different schemes for middle and senior management may have adverse effects.

54. It should be noted first that other recent improvements in the conditions of service of SES officers have substantially widened the gap between the remuneration of staff in the feeder groups and those in the SES. In addition, a recent significant lowering of the age and length of service profiles of the SES, together with tight control on SES numbers, appears to have reduced the promotion prospects of staff in the feeder groups. A recent Department of Finance study, for example, showed that the age profiles of the SES and the main feeder group now differ by 2.5 years compared to a difference of 4.3 years in 1984 (Department of Finance 1990, pp. xvii, xxvi). The early provision of large performance based pay increments to many SES officers, well in advance of their availability to the middle management ranks of the feeder groups, seems likely to cause problems at the lower level by increasing the gap between middle and senior management.

55. There is also, of course, an ethical argument against improving the conditions of SES officers before those of their subordinates. The military axiom that the quality of a force can be judged by ascertaining whether troops are fed before officers shows that this argument can have practical as well as ethical force.

56. If performance based pay is introduced at all, the Committee supports a phased introduction on an agency basis rather than on a grade basis within agencies. The Committee believes that if implementation is to be properly managed along the lines proposed in earlier sections of this report, there will be ample time for further development of the feeder groups proposal. The need to justify the proposal to unions can be expected to improve policy development and may well lead to improvements in the proposal for the SES. **The Committee recommends that, if performance based pay is introduced, it be introduced for the SES and the feeder groups at the same time and under the same system in each agency.**

Structural and operational issues

57. As noted above, several basic structural and operational features of the proposed system of performance based pay have yet to be determined. Four seem particularly important to the Committee: privacy of performance payments; the mode of payment; service-wide consistency; and, the level of funding.

Privacy

58. Although it appears that most performance based pay schemes maintain strict privacy on payments to individuals, some permit publication of details. Most witnesses heard by the Committee favoured privacy. Dr Keating, for example, pointed to possible morale problems among staff receiving little or no performance pay if that fact became public knowledge (Evidence DOF, p. 1102). Dr Keating told the Committee that it was an on-balance judgement whether the benefits of performance based pay outweighed the costs. But if, as in his view they did, 'I would want to minimise the costs and I think ... secrecy ... will help minimise those costs' (Evidence DOF, p. 1102-3).

59. The Auditor-General, John Taylor, considered it unlikely that strict privacy could be maintained. He told the Committee:

I am in favour of performance pay but I have had a careful look at the way that it is implemented in a number of sister organisations around the world and it is not as easy as people seem to be thinking. Word does get around. If I have to come down on one side or another, I think I must come down on the side of being open about it (Evidence, p 874).

Mr Taylor also commented that there is a difference between the private and public sectors and that he considered that people have a right to know what public servants are being paid.

60. The Public Service Commissioner also considered that it would be impossible to maintain secrecy about performance based payments in a public sector environment. He commented that attempts to do so in Canada and New Zealand had failed. However, the Commissioner did not see privacy as essential to the success of the system (Evidence PSC, p.1022).

61. It is clear that it might be impossible to maintain the privacy of individual performance based payments, even if that was considered desirable. A recent report in the authoritative journal *Directions in Government* concluded:

[the] experience in NSW, where SES remuneration packages are handled on separate payrolls, is that the beans are being spilt. (Directions in Government 1990, p. 47)

62. It should be noted that opinion on the privacy issue is also divided in the private sector, which makes wider use of performance based pay than does the public sector. It appears that most private sector performance based pay systems do maintain privacy. But a well known author on private sector management, Robert Townsend, has written:

Secrecy is totally bad. It defeats the crusade for justice, which doesn't flourish in the dark.

Did you ever ask yourself why there's a private payroll? Or why all wages and salaries aren't posted on the bulletin board? According to the lore of the free-enterprise system, money is really a scorecard. So why aren't the scores posted? (Townsend 1984, p. 201)

In similar vein, a Partner in KPMG Peat Marwick Management Consultants, Peter Agars, recently commented that performance based pay is only likely to be an effective motivator if details of the payments are known to peers (Agars 1990). A written submission to the Committee from the management consultants Strategic Alliances Pty Ltd also recommended that information on the composition of senior executive remuneration packages 'should, in principle, be publicly available' (Evidence, p. 1507).

63. J.R. Nethercote, a well-known commentator on public administration, told the Committee that, while he considered the current proposal for performance based pay to be totally misconceived, he thought the case for privacy was compelling if the pay system did change (Evidence, pp. 1128-9). Mr Nethercote suggested that a possible compromise on the privacy issue would be notification to the Public Service Commissioner of all performance based payments, with the Commissioner being responsible for monitoring consistency with the framework of the scheme (Evidence, p. 1128).

64. Robert Townsend, proposing a model for the private sector, has suggested a round of annual salary review meetings at which all executives at a given level would participate in wage setting for all staff at the next level down. This would aim to ensure relative fairness across the organisation and some degree of openness in the setting of pay (Townsend 1984, p. 196).

65. Whatever the private sector practice, performance measurement in the public sector will generally be more difficult, if not impossible. Most private sector organisations can identify some type of measurable corporate result on which to base rewards. The output of the public sector frequently takes forms which are not easily quantified. Where results can be measured, it is often difficult to link them to the performance of individuals. In the absence of clear cut criteria on which rewards can be based, a performance based pay system gives wide scope for improper exercise of patronage. Publicity would provide a defence against such malpractice.

66. The Committee concluded that the case for openness in public administration outweighed any possible increase in efficiency available from privacy on salary matters. Relevant to this conclusion was a belief that these efficiency gains would be, at best, problematic due to the difficulty of measuring public sector performance and the consequent ease with which the system could be manipulated. Public knowledge of levels of performance based payments might actually increase efficiency by forcing a higher general standard of honesty on those operating the system. This conclusion is consistent with the Committee's finding in its December 1986 report, *ABC Employment Contracts and their Confidentiality*. In that report, the Committee concluded:

The actual remuneration for providing services to an authority (whether as employee or contractor) should be available to the Parliament when requested. ...authorities must be prepared to account to Estimates Committees for all aspects of their financial management and administration, even when the information sought may be regarded as private or commercially confidential (SSCFGO 1986, p. 51).

The Committee recommends that, if performance based pay is introduced, details of any payments be made public.

Mode of payment

67. When the Committee held hearings on this matter in early February 1990, no decision had been made on whether performance based payments would be made as an addition to regular salary payments, as a lump sum bonus or as some combination of the two. Civil services overseas have tried each of these options. The elements of the British Civil Service which participate in performance based pay systems, for example, are eligible for both bonuses and salary increments based on performance (Laughrin 1988, pp. 2-3).

68. It might be expected that addition of performance payments to salary would create informal pressure for maintenance of payments after they are awarded. It would be unusual in our society and culture for employees to suffer a reduction in wages. This could occur, however, under the proposed scheme if performance was assessed as declining from one year to the next and if superior performance was rewarded with a salary increment. The possibility thus arises that performance increments, once granted, will continue indefinitely, adding little or nothing to motivation. The Committee has been privately advised that such an informal floor applies in relation to the performance based pay system of a large private sector organisation in Australia.

69. The Public Service Commissioner expressed a preference for a bonus approach to avoid this problem (Evidence PSC, p. 1025). The Committee agrees, noting that the motivational effect of performance pay, if it exists at all, depends on the additional payment being at risk. 'That way', the Economist magazine recently noted, 'executives tremble their way alertly towards their bonanzas' (Economist 1989). **The Committee recommends that, if performance based pay is introduced, it be paid largely or wholly in the form of bonus payments rather than as a supplement to regular salary payments so that it not be factored into an officer's regular living expenses.**

Service-wide consistency

70. One of the major justifications for the formation of the SES in 1984 was to make the senior echelon of the public service 'a more unified and cohesive group' in the words of the relevant Minister at the time (Evidence PSC, p. 223). Mobility and other provisions relating to the SES were designed to promote a service-wide outlook in SES officers. If there is serious inconsistency between agencies in their operation of a performance based pay system, much of this effort to create a broader outlook will be wasted.

71. The performance based pay proposal as presented to the Committee included no mechanism for ensuring reasonable consistency across the service. The Public Service Commissioner expressed the view that such consistency would be needed and appeared confident that it would be provided by guidelines issued by the Department of Industrial Relations (Evidence PSC, p. 1023).

72. The Committee believes that service-wide consistency on SES pay remains desirable. Inconsistent pay policies could be expected to produce a bidding or leap frogging process likely to conclude with all agencies paying all their staff the maximum performance payment. The Committee does not believe that a consistent approach will arise spontaneously. Nor is it likely to be secured by merely issuing guidelines. **The Committee recommends that, if performance based pay is introduced, the implementation task force devise a continuing system for monitoring the pay scheme to ensure reasonable consistency in performance pay policies across the Service.**

Level of funding

73. As noted in paragraph 27, inadequate funding has been a common cause of the failure of performance based pay systems in other countries. It was clear to the Committee that the coordinating agencies are well aware of this risk. Officials from the Department of Finance and the Department of Industrial Relations, while unable to give more than indicative figures, assured the Committee that funding for the scheme would be adequate. The Department of Industrial Relations suggested that about 10% of the current SES salary budget might be a likely figure for the performance pay pool (Evidence DIR, p. 574).

74. The Committee accepts that, if performance pay is to be introduced, a pool of about 10% of total SES salaries would represent adequate funding. If performance based pay is restricted to a small number of top performers, additional payments in the range of 20 to 30% of base salary would be available to those officers. Payments of that size would imply, of course, that the majority of SES officers would receive little or no performance loading. As the group in receipt of performance pay broadens, the top payments will decline and the system will come closer to approximating a general pay rise.

75. The motivational effects of the system will clearly depend on the quality of judgements on the size and composition of the group in receipt of performance payments. The Committee can offer no suggestions on how those judgements should be made, other than to stress that subordinate and peer perceptions of the fairness of the system will be crucial to its success. If performance based pay is introduced, the Committee will examine this aspect of its implementation with interest.

Conclusion

76. The Committee accepts that the objective of the proposal for performance based pay is to provide increased incentives for improved performance in the public service. We sympathise with that objective and have considerable sympathy for the officers who may have to implement the new pay system. The high incidence of failure of such systems in other countries and the numerous problems in schemes that have continued to exist suggest that their task, if it eventuates, will be difficult. Indeed, some Committee members consider it to be impossible.

77. The Committee has two major concerns based on the evidence so far presented. Firstly, it is by no means clear that performance based pay will produce net benefits and, even if it does, there seem to be other and more urgent priorities in public service personnel management. Secondly, the rush to implementation in this case will greatly add to the already substantial risks of the proposal with no commensurate increase in the possible benefits.

78. David Leaver, an executive of the Professional Officers' Association, told the Committee:

We still believe that it is being done ... to get around the [wage] guidelines rather than because people have thought through the whole process. That is the wrong reason and that is a recipe for a stuff-up (Evidence POA, p. 723).

The Committee hopes that Mr Leaver is wrong but the evidence lends support to his conclusion.

79. The Committee has chosen to make a special report on this matter so that our concerns can be given some weight when the decision on performance based pay is made. It is clear that the proposal requires close review before a final decision is made.

John Coates
CHAIR

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TERMS OF REFERENCE

Development of the Senior Executive Service

To examine and report on the development of the Senior Executive Service (SES) with particular reference to:

- the overall management effectiveness of the SES structure;
- optimal conditions of service, including remuneration;
- mobility within the SES and between the Service and the private sector.

Adopted by the Committee 10 May 1989.

LIST OF SUBMISSIONS

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1	Mr S.R. Eleftheriou	18. 4.90	1182
2	Mr Kirk Bendall	18. 4.90	1184
3	Dr James Elliott	18. 4.90	1187
4	Dr Leo Dobes	18. 4.90	1188
5	Professional Officers Association	31. 1.90	612
6	Private Submission	—	—
7	Administrative and Allied Officers Association, Australian National University	18. 4.90	1192
8	Commonwealth Director of Public Prosecutions	18. 4.90	1198
9	Australian Government Senior Executives Association	3.11.89	60
10	Australian Government Lawyers Association	18. 4.90	1203
11	Office of Parliamentary Counsel	18. 4.90	1205
12	Department of Primary Industries and Energy	18. 4.90	1208
13	Ms A.E. Jackson	18. 4.90	1220
14	Dr Marion Sawyer	31. 1.90	770
15	Auditor-General	31. 1.90	839
16	Mr Phill Boas	18. 4.90	1275
17	Department of Finance	1. 2.90	1030
18	Mr Paul Varma	18. 4.90	1283

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19	Public Sector Union	31. 1.90	591
20	Australian Federal Police	18. 4.90	1299
21	Prime Minister	18. 4.90	1315
22	Australian Institute of Management	18. 4.90	1336
23	Insurance and Superannuation Commission	18. 4.90	1366
24	Relocation Management Services	18. 4.90	1369
25	Department of Defence	31. 1.90	787
26	Department of Community Services and Health	1. 2.90	887
27	Dr Edward R. Cawthron	18. 4.90	1380
28	Department of Transport and Communications	18. 4.90	1418
29	Department of Veterans' Affairs	1. 2.90	895
30	Minister for Administrative Services	18. 4.90	1429
31	Department of Employment, Education and Training	18. 4.90	1446
32	Department of Industrial Relations	31. 1.90	408
33	Australian Bureau of Statistics	18. 4.90	1452
34	Minister for the Arts, Sport, the Environment, Tourism and Territories	18. 4.90	1458
35	Mr Andrew Moran	18. 4.90	1485
36	Commissioner of Taxation	31. 1.90	810
37	Mr Ian Radbone	18. 4.90	1489
38	The Association of Professional Engineers Australia	31. 1.90	601
39	Attorney-General's Department	31. 1.90	834
40	Public Service Commission	20.11.89	218

41	Private Submission	—	—
42	Professor P.J.O. Self	20.11.89	152
43	Australian Government Senior Executives Association	18. 4.90	1544
44	Private Submission	—	—
45	Private Submission	—	—
46	Department of Industrial Relations	31. 1.90	517
47	Australian National Audit Office	31. 1.90	844
48	Commissioner of Taxation	31. 1.90	825
49	Strategic Alliances Pty Ltd	18. 4.90	1496

PROGRAM OF PUBLIC HEARINGS

1. MELBOURNE – Friday 3 November 1989

Public Service Board of Victoria

Dr R.F.I. Smith	Acting Chairman
Mr F. Burke	General Manager Personnel Management Division

Australian Government Senior Executives Association

Mr R.A. Gray	Council Member
Mr B.W. Lewis	Federal Secretary
Dr A.J. McHugh	Vice-President
Mr M. Storey	Branch Councillor
Mr D. Reynolds	Member
Mr W. Connick	Member
Mr L.T. Malempre	Member
Mr B.L. Cody	Member
Mr T.G. Fahy	Member

Egon Zehnder International S.A.

Mr C. Thomas	Managing Partner
Mr P. Kronborg	Principal

2. Canberra – Monday, 20 November 1989

Public Service Commission

Mr J.D. Enfield	Public Service Commissioner
Ms R. Oxe	Senior Executive Adviser and Assistant Commissioner
Mr G. Hannaford	Acting Director, Selection
Ms L. Smith	Acting Director, Appraisal

Dr J. Halligan**Professor R.S. Parker****Professor P.J.O. Self**

3. **Canberra – Wednesday, 31 January 1990**

Department of Industrial Relations

Mr M.G. Coghlan	First Assistant Secretary Pay and Structures Division
Mr D.C. Gillespie	Acting Principal Adviser Pay and Structures Division
Mr S.J. Linton	Acting Director APS Conditions Branch
Mr M. Manthorpe	Acting Principal Adviser Pay and Structures No 2 Branch

Australian Public Sector and Broadcasting Union

Ms A.M. Forward	Joint National President
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Professional Officers Association

Mr D.C. Leaver	President, SES Branch
Mr E.H. McGrath	Industrial Officer, SES

Association of Professional Engineers Australia

Mr J. Vines	Executive Director
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Attorney-General's Department

Mr A. Rose	Secretary
------------	-----------

Australian National Audit Office

Mr J.C. Taylor	Auditor-General
----------------	-----------------

Department of Defence

Mr A.J. Ayers	Secretary
---------------	-----------

Australian Taxation Office

Mr T.P.W. Boucher	Commissioner of Taxation
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Mr J. Pomeroy

Dr M. Sawyer

4. **Canberra – Thursday, 1 February 1990**

Public Service Commission

Mr J.D. Enfield	Public Service Commissioner
Ms R. Oxe	Senior Executive Adviser and Assistant Commissioner
Mr J.T. Popple	Director, Selection Section
Ms L. Smith	Acting Director, Appraisal

Department of Finance

Dr M. Keating	Secretary
Mr A.S. Podger	First Assistant Secretary Education and Employment Division
Mr G.W.B. Moffatt	Assistant Secretary Classification Management Branch

Department of Veterans' Affairs

Mr K.T. Lyon	Deputy Secretary
Ms H.R. Swift	Assistant Secretary Departmental Support

Department of Community Services and Health

Mr M.J. Roche	Deputy Secretary
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Professor R. Koch

5. Canberra — Friday, 2 February 1990

Public Service Commission

Mr J.D. Enfield	Public Service Commissioner
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Department of Finance

Mr A.S. Podger	First Assistant Secretary Education and Employment Division
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Mr J.R. Nethercote

Professor P. Weller

**PERFORMANCE APPRAISAL:
GUIDELINES FOR APPRAISAL
OF SENIOR EXECUTIVES IN THE
AUSTRALIAN PUBLIC SERVICE**

**Public Service Commission
Canberra
March 1990**

Refer para 50

Introduction

This paper sets out the guidelines for performance appraisal of senior managers in the Australian Public Service. The appraisal process has been designed to improve management performance at senior levels of the Service. It has its basis in the December 1983 paper Reforming the Australian Public Service which clearly stated the Government's intention that

"...departments will be required to develop and introduce appraisal schemes in accordance with general guidelines issued by the Board [the former Public Service Board]. Appraisal will be of the individual's performance against objectives and criteria determined in advance. The guidelines will provide for the protection of the rights of individuals (including the right to comment on appraisals and rigorous control over access to them) and will try to ensure that there is sufficient uniformity to facilitate a Service-wide approach".

2. Following the introduction of pilot schemes in five departments * in 1986, the Management Advisory Board in 1988 endorsed a broad approach to appraisal developed by the Public Service Commission in consultation with departments.

3. These appraisal guidelines have been based on the following broad principles:

- that responsibility for appraisal rests with individual departments, and this means that the processes for its introduction will in each case be different;
- that the emphasis on objective setting and on integration with departmental corporate plans will complement recent Service-wide reforms in planning;
- that developmental and career planning activities will be based on how well an officer measures up against the SES core skills or competencies;
- that there is a need to recognise the subjective nature of appraisal of work performance and to minimise this;
- that individuals' rights to privacy and equity should be protected; and
- that the appraisal process should be designed to allow for the introduction of merit pay.

Background

Pilot Schemes

4. In 1985, Secretaries met to consider the Government's intentions for appraisal of senior managers and supported an approach which recognised that:

- each department was free to develop its own scheme within certain core Service-wide requirements;
- there would be a linkage of appraisals to corporate plans and program management;
- there would be no compulsory use in selection; and
- adequate training in goal setting and performance feedback was essential.

* Note: throughout these guidelines the word 'departments' should be taken to include other Commonwealth agencies.

5. In 1986, pilot schemes were introduced in five departments. These schemes had two main components:

- the identification of SES core job skills and common SES job responsibilities; and
- the testing of three different forms of appraisal, each tied either fully or partially to corporate plans, with or without rating scales, and with varying degrees of structured performance feedback.

6. At the time of the changes in the roles, responsibilities and structure of government departments in 1987, these pilot schemes were still in the early stages of implementation. Appraisal activity declined in departments most affected by the restructuring and the charter for SES performance appraisal passed from the Public Service Board to the new Public Service Commission (PSC).

Management Advisory Board

7. In 1988 the Management Advisory Board approved an approach to appraisal developed by the PSC on the basis of the pilot schemes and other developmental work that had been carried out by the PSC. This approach focused on management improvement rather than selection and placement, and recognised that it can take some years to establish fully the skills needed for the successful implementation of appraisal schemes and for the concept of performance appraisal to gain widespread acceptance.

8. The core elements of the proposed approach included:

- training in objective setting and the giving and receiving of feedback;
- setting objectives against corporate plans at the beginning of the appraisal cycle;
- using the SES core skills;
- emphasising two-way communication so that staff are able to give feedback on how well they are being managed; and
- developing, in consultation with staff, procedures for custody of, and access to, appraisal records.

9. In addition, the Management Advisory Board agreed that the main roles of the PSC in performance appraisal were to:

- act as a consultant and facilitate networking of staff responsible for implementation;
- provide guidelines;
- act as an information-exchange; and
- publish a short booklet on the subject. (The booklet Appraisal: "How to kill it and how to make it work" was published as a Senior Executive Staffing Unit Occasional Paper in March 1989).

Guidelines

Responsibility

10. Responsibility for the introduction of performance appraisal rests with Secretaries and Heads of Agencies who will make decisions about issues outlined in these Guidelines. These include the approach the organisation will take to criteria and standards, what training will be put in place, how the concept will be 'sold' within the organisation, how resources will be allocated, how the scheme will be introduced, and how it will be administered.

Objectives of performance appraisal

Service-wide objectives

11. The Service-wide aim of performance appraisal in the SES is to improve management performance. This includes:

- improving performance against the corporate goals;
- improving individuals' understanding of their work responsibilities and the performance standards expected of them; and
- improving communication between managers and their staff.

12. Performance appraisal is also designed to provide:

- opportunities for meeting the development needs of individual officers;
- career and advancement opportunities of SES officers; and
- mobility and flexibility in the deployment of senior managers.

13. These are the objectives against which Service-wide evaluation of performance appraisal will be based. In addition, performance appraisal will provide a basis for any future merit pay system.

Departmental objectives

14. Organisational aims in performance appraisal should be consistent with the Service-wide aims. Other purposes may be added to suit organisational needs.

Performance agreements

15. At the start of each appraisal cycle, managers and officers will meet to develop, in writing, a mutually agreed statement of work objectives, indicators of achievement of those tasks, and expected standards of performance. There should be full participation of the officer in establishing the objectives defined in this performance agreement.

Clear performance criteria and standards

16. The basic requirement in performance appraisal is the establishment of criteria or benchmarks against which performance can be assessed. There are a number of criteria that have been used in performance appraisal. These include character traits, attitudes, skills, knowledge, and many variations of objective-setting and results-oriented approaches. The two kinds of criteria required in these Guidelines are results criteria and the SES core skills. Results-oriented criteria are used to assess the actual outcomes or products of work and are usually related to the corporate plan. The core skills are underlying characteristics which result in effective and/or superior performance in a job. Each criterion will require some way of setting standards so that it can be assessed as unambiguously and as objectively as possible.

Results Criteria

17. The primary criterion will be performance oriented to results, preferably tied to corporate plans or program objectives. Setting accurate results criteria is intellectually demanding and, at least in the initial cycle, will take time. Criteria need to be reviewed when people change their jobs or when there are changes to the organisation's corporate plan.

18. There are a number of techniques for developing results-oriented criteria and Attachment A outlines the general approaches that can be taken. The methods take into account changing priorities and resources and ensure that the focus is on the important aspects of the job. Secretaries and Heads of Agencies are free to develop an approach based on the methodologies described here.

19. The benefits of this process go beyond establishment of assessment criteria for performance appraisal. Benefits may include necessary revisions to the organisation structure, giving united direction to departmental activities and improving clarity of expected job outcomes.

20. Any results criteria chosen should allow for a single overall rating of performance based on an assessment against the results criteria. The purpose of this single rating is to provide for the award of merit pay, should this happen. To provide broad Service-wide comparability, this rating will be on a five-point scale, as explained at Attachment A.

SES core skills

21. In addition to the assessment of performance outcomes, there is to be a separate assessment of the SES core skills or competencies. These criteria correspond closely to those used in many private and public sector appraisal schemes. Behavioural rating scales have been developed to provide a standard approach to assessment of the SES core skills. These scales provide examples of behaviour expected at different levels of competence and will also be assessed on a five-point rating format. See comments on rating scales for the SES core skills at Attachment B.

22. The purposes of this assessment are to:

- identify skills which must be developed if the individual is to perform broader SES roles;
- help in planning for each officer's advancement;
- provide officers with a base for developing their own staff development and career path;
- provide departments with a base for their SES development plans; and
- provide the PSC with data for its expanded Senior Executive Data Base.

23. The Public Service Act enables the Commissioner, in certain circumstances, to have departments further notify or advertise a vacancy, where that is desirable in the interests of the Service. The existing computer data base now held by the PSC (ie. name, birth date, birth place, gender, appointment and promotion dates and current position) is not sufficient for this purpose. It is proposed that the data base be expanded to include qualifications, experience, career preferences and assessments of the core skills of all SES staff (ie. information similar to that already addressed in selection reports held by the PSC). To allow further consultation with Secretaries on this proposal, assessment of the SES core skills, and collection of this data by the PSC, may be deferred until at most one year after introduction of each department's appraisal program.

Appraisal cycle

24. The appraisal cycle is the period between the establishment of the performance agreement and the formal performance assessment interview. The cycle should in most cases be one year in length. In many cases, the timing of the appraisal cycle will be linked to the corporate planning cycle of the organisation. The length of the cycle may need to be varied to handle special cases such as SES officers on probation and those approaching the end of contracts.

Performance assessment interviews

25. Regular discussion and evaluation is central to appraisal. Apart from establishing a performance agreement, there is a need to review progress at least once during the cycle.

26. A review interview should provide feedback on performance to allow for assistance in improving performance and so that there are no surprises at the later interview. Review interviews can include:

- reviewing standards of performance so far;
- checking the relevance of the performance agreement, and adjusting it if the nature of the job (ie. priorities, objectives or resources) has changed substantially; and
- making provision for training, development and coaching.

27. Secretaries and individual managers may wish to develop and adjust contracts and conduct progress reviews more frequently. The outcome of these reviews should be documented.

28. At the end of the cycle, each officer and their manager meet to discuss the officer's performance against the previously set performance criteria and standards. Evidence for the assessment may be obtained from sources other than the supervisor. The performance criteria and standards for the coming cycle should be negotiated and agreed at this time or shortly afterwards.

29. There should be an emphasis on open two-way communication that includes full participation of the officer. Some departments may wish to provide the opportunity for officers to give feedback on how well they feel they have been managed.

30. The SES core skills assessments would normally be kept separate from those of the performance outcomes because of their differing aims. There are advantages and disadvantages in discussing assessments of SES core skills separately from assessments of performance. Separation assists free discussion about the development needs of individuals and associated career planning. However, combining the two will allow attention to be given to development needs identified from performance outcome assessments.

Privacy and equity

31. All schemes must include privacy safeguards and provisions for equitable and fair appraisals:

Unjustified discrimination

32. Care must be taken in establishing criteria and standards, and making assessments, that are applicable to all members of the SES including those SES officers in EEO target groups. In particular, criteria and standards must not result in

indirect discrimination. This can occur where a criterion or standard has a disproportionate impact on one group as opposed to another and is not objectively justifiable.

33. Performance agreements should include generic management criteria which have indicators relating to departmental EEO plans. Indicators of EEO and other Service - wide management concerns (eg human and financial resource managements); can be applied to all agreements in a particular department.

Privacy

34. Departments, in consultation with staff, must develop procedures for the use, custody, access, disclosure to third parties and period of retention of the appraisal documentation consistent with Information Privacy Principles. At attachment C are model procedures for custody and access to performance appraisal records.

Review mechanisms

35. While there will not be any formal appeal arrangements, there will be provision for review of performance agreements and appraisal comments, generally by the appraiser's manager. The senior manager should also provide for a source of independent quality control ensuring as far as possible that performance agreements in a department are of comparable worth, that the indicators are capable of objective assessment and that the agreed results are assessed at comparable standards.

36. Appraisal documentation should allow for comment by the officer appraised. Officers wishing to discuss their assessment in an independent setting may also have access to the PSC's Senior Executive Adviser, as they would on any other personnel matter.

Implementation

Training

37. Staff participating in the scheme will need training to prepare for performance appraisal. The responsibility for training rests with the Secretaries or Heads of Agencies. Training will need to be undertaken by all participants in all of the following:

- the development of results-oriented objectives and indicators;
- the application of standards to indicators;
- an understanding of common errors in making judgements;
- the use of rating scales on the SES core skills;
- the giving and receiving of feedback; and
- the detailed procedures of the particular scheme.

Arrangements for staff changes

38. Where staff change jobs or take extended leave during the cycle, performance agreements should be negotiated as soon as possible. Appraisal should not occur until agreements have been in place for six months.

Senior executive development

39. Staff development plans for departments should address gaps and deficiencies identified in the appraisal of performance and skills. Individual development plans should be based on personal assessments.

Monitoring and evaluation of the scheme

40. **Programs** will need arrangements for reporting to departmental management on its effectiveness. A basic element in evaluation is the establishment of clear objectives and specific indicators to assess whether or not these objectives are being met. The **monitoring and evaluation** mechanism will be necessary both during implementation, to allow for modification, and after the scheme has been running for several years to assess its continuing effectiveness.

Role of the Public Service Commission

41. The PSC has a responsibility to ensure that performance appraisal schemes in departments meet acceptable standards as expressed in these Guidelines. When details of programs are finalised, the PSC will review them to assist departments in meeting these Guidelines.

42. The PSC will require statistics on the number of appraisals completed, the number of people who have sought a review of their appraisal, information on equity issues and competency profiles.

43. The PSC will review the Guidelines two years after schemes have been introduced in departments.

Attachment A

Results-oriented performance criteria

There are a number of approaches to performance appraisal. These include the now discredited character-trait assessment, assessment centres, ranking and forced choice techniques, narrative methods, behaviour rating scales and the many objective-setting and results-oriented approaches.

2. The Commission has recommended the latter two as appropriate for SES appraisal. There are two broad methods for setting up criteria or yardsticks for assessing performance. These are to assess either how the work is done (eg. skills, processes), or the objectives of that work (eg. responsibilities, end results, outcomes). This Attachment concentrates on the objective-setting and results-oriented approaches.

3. Organisations using purely objective-based schemes include Westpac, CIG, ICI and the Victorian SES.

Objective-Oriented Schemes

4. All of the objective-oriented schemes have:

- identified key objectives or responsibilities or results to be achieved by the job occupant during the appraisal cycle;
- developed performance criteria or performance indicators which allow progress and success in delivering those results to be monitored; and
- set standards which clearly indicate the level of performance which is expected on each criterion or indicator.

5. An important element of most of the schemes using this approach is the development of a performance agreement between managers and officers. The agreement covers each of the three issues listed above.

6. The precise methods for establishing objectives/indicators and difficulty levels constitute the main variables in the differing objective setting methods.

Advantages and disadvantages

7. Objective-setting methods have the advantage of being closely allied to specific work in the organisation, and the people to be assessed contribute to the development of their own assessment criteria. These methods also clarify the nature of the job and its goals, and focus on the key elements of the job. The rationale for objective-oriented schemes is easily aligned with that for program budgeting and corporate planning.

8. A common difficulty with these schemes is found in achieving directly comparable levels of difficulty for different types of tasks. There are other problems in that:

- the initial development and to a lesser extent the maintenance of objectives can be very time consuming;
- there may be a tendency to focus on easily measurable factors at the expense of other subtle issues (including equity, morale and staff relations); and
- assessing individual needs for development can be difficult because these approaches concentrate on performance in specific jobs at a specific time.

Major differences between the approaches

9. Three major issues are handled differently in the varying approaches to objective-oriented schemes. These are:

- the use of quantitative performance indicators as opposed to a mixture of both qualitative and quantitative indicators;
- the methods used for arriving at overall performance ratings; and
- varying emphasis on the importance of appraisal skills training.

Qualitative and quantitative performance indicators

10. Some approaches encourage the use of quantitative performance indicators while others encourage a mixture of both qualitative and quantitative indicators. In order to be objective, qualitative indicators include the use of behavioural rating scales (such as those associated with the SES core skills). Clearly the more objective and rigorous the scales used, the more credible and equitable the process.

Different levels of task difficulty

11. Different approaches tackle in different ways the issue that exists for all results-oriented performance appraisal schemes; the issue being that different tasks have different levels of difficulty, and a rating of an occupant's success in delivering a result needs to take account of that.

12. Available appraisal processes usually deal with this in one of the following ways. It is important that departments adopt a consistent approach.

- The manager and officer are asked to make **subjective** judgements about task difficulty and to allow for this in setting standards and in judging results. Although not ideal, this method will suffice where there is a high level of trust and commitment between the parties; and
- The manager and officer are encouraged to make **less subjective** judgements about task difficulty by using a more structured procedure. This can be undertaken:

retrospectively, at the time when results are being assessed. (Often a rating is made of such factors as external environmental conditions which made the task more or less difficult; resource availability; changes in policy direction; or unforeseen circumstances of any kind which impact on the likelihood of success); or

prospectively, when performance agreements are being developed. (This approach usually requires the officer and the manager to spell out the activities which job occupants can reasonably be expected to anticipate and control or make allowances for unforeseen circumstances at the start, rather than try to contain retrospectively the slippage which is inevitable in these processes).

Overall ratings

13. Variations exist in the methods used for arriving at overall performance ratings

The most subjective approach is to review performance against all criteria and standards and, allowing for task difficulty, to make a subjective overall judgement.

14. More objective approaches try to use more rigorous methods, either averages or systems of weighting, allowing for the fact that some tasks are more important and time consuming than others. Again, it is important that departments settle on one consistent approach.

15. A weighted overall rating would be derived as follows:

Assessment	Weight	Product
4	2	8
3	1	3
5	2	10
2	2	4
4	3	12
Total	10	37

Overall rating = $37/10 = 3.7 = 4$

16. Ratings on individual indicators and single overall ratings will both be on a five-point scale with five being at the high end of the scale. Care should be taken to limit the number of officers who are assessed at each of the five rating levels on each performance indicator or overall result. This assists in distinguishing between levels of performance amongst groups of SES officers and also provides for a standard approach across departments. The exact figures at each level depend on circumstances in particular departments, and departments could set their own figures. For example, the Service-wide percentages could be expected to be:

Rating level	Approximate %
5	around 10%
4	around 20%
3	around 50%
2	around 20%
1	possibly none, or very few.

17. The definition of these rating levels for indicators could be, for example:

5. Outstanding
Performance far exceeds the agreed standard set for this indicator
4. Above competent
Performance exceeds the agreed standard set for this indicator
3. Competent
Performance fully meets the agreed standard set for this indicator
2. Adequate
Performance just meets the agreed standard set for this indicator
1. Less than competent
Performance does not meet the agreed standard set for this indicator

18. Similarly, the definition of the rating levels for single overall ratings could be:

5. Outstanding

- Performance far exceeds the standard expected of competent officers at this classification level
4. Above competent
Performance exceeds the standard expected of competent officers at this classification level
 3. Competent
Performance fully meets the standard expected of competent officers at this classification level
 2. Adequate
Performance just meets the standard expected of competent officers at this classification level
 1. Less than competent
Performance does not meet the standard expected of competent officers at this classification level

Emphasis on appraisal skills training

19. Some methods put more emphasis than others on the importance of skills training for managers who will be involved in appraisal processes. Such skills training can be a significant cost in the implementation of appraisal. In general, more emphasis is placed on the value of skills training in approaches which use largely subjective methods, as a good deal of their success depends on a high quality of trust and communication between the parties.

Attachment B

The skills orientation in performance appraisal

As mentioned in Attachment A, there are two broad methods for setting up criteria or yardsticks for assessing performance. This attachment describes the assessment of the SES core skills.

SES core skills

2. A job skill is an underlying characteristic of a person which results in effective and/or superior performance in a job. The SES core skills, are those characteristics necessary for effective management performance in the SES.

3. The current core skills are being revised and at the time of going to press are not available. Early indications are that some of the current skills remain and others have taken a slightly different emphasis. There are also some new elements.

4. The SES core skills are not intended to cover functional, technical or responsibility aspects of SES jobs, although some of the core skills will be required of specialists.

Other skill systems

5. The SES core skills are similar to skills identified in other executive appraisal models. The management literature reports many empirical studies of the components of effective managerial performance and a large measure of agreement is developing.

6. Skills-based appraisal programs are used by GMH, Amatil, CSR and the Reserve Bank. These programs use factors similar in nature, and often identical to SES core skills. Many organisations choose to use both objectives and skills. This course has been followed by the ABC, Western Australian SES, the PSC internal scheme, Ampol, ACI, BHP, IBM and Pacific Coal.

Advantages and disadvantages of job skill models

7. The advantages of the job skill models are that:

- there is specific relevance to jobs, while reducing performance into component skills (they provide a good basis for developmental activities);
- they establish the same comparable factors for all SES jobs (this helps achieve government-wide personnel objectives, ie. job placement, mobility, EEO, staff development, selection, etc., all of which require equitable comparisons); and
- they can remain relevant for many years across a wide range of jobs.

8. The disadvantages are that the initial development costs can be high, and that the assessments required are based on abstract qualities which may not be closely matched to the job.

Assessment of officers against the SES core skills

9. Rating scales will be developed for use in assessing the revised skills and will provide for a five point rating scale similar that being used for assessing results criteria.

Attachment C

Custody of and Access to Performance Appraisal Records

The Guidelines indicate that departments, in consultation with staff, must develop procedures for the use, custody, access, disclosure to third parties and period of retention of the appraisal documentation consistent with Information Privacy Principles.

Both the *Privacy Act, 1988* and the *Freedom of Information Act, 1982* have implications for appraisal records. The PSC is seeking legal clarification of the status of appraisal records as there have been insufficient court decisions on either selection or appraisal documents to be entirely sure of the situation. However, there are four main issues to be considered.

CONTENT AND PURPOSES OF APPRAISAL RECORDS

Staff must be informed about what information is collected and why. The information will be used for purposes indicated in these Guidelines and as determined by the departmental Secretary, in consultation with staff concerned.

The Service-wide aim of performance appraisal in the SES is to improve management performance. This includes:

- improving performance against the corporate goals;
- providing opportunities for meeting the development needs of individual officers; and
- forming the basis of performance pay.

The content of performance appraisal records is directed towards meeting these objectives and will include:

- full details of the criteria upon which the assessments will be made (ie the performance agreement and the core skills);
- the assessments made against the performance agreement and the core skills; and
- development plans.

QUALITY AND INTRUSIVENESS OF INFORMATION

There should be minimal or no personal information collected which might intrude into an officer's private affairs.

Officers should have the opportunity to ensure that the information contained in appraisal records is accurate and up to date. Accordingly, there will be provision for comment and signature by the subject officer, the appraising officer (the manager) and the reviewing officer.

Also to ensure accuracy, there will be provision for review of performance agreements and appraisal assessments and comments, generally by the appraiser's manager. In cases of dispute, this reviewing officer will carry the decision. There will be no formal procedures for appeal in SES appraisal. Appeal and review procedures for ASO 7s and 8s will be as determined in negotiation with staff organisations. Access to the MPRA and Federal courts exists.

To further ensure quality, measures should be taken towards having performance agreements that are of comparable quality across the department, that there is consistency of ratings across the department and that the ratings are equitable and are based on the performance agreements.

SECURITY AND RETENTION OF APPRAISAL RECORDS

Records of performance appraisals should be kept in secure storage under arrangements agreed with the staff concerned. For example, records may be held under the direct control of the Head of Management Services, or in smaller organisations by the Chief Executive Officer. The records should not be kept on personnel files.

There should be at least one formal appraisal per year. Therefore records will be kept at least until the next report has been made. This will help ensure that all actions to be taken on the basis of the previous report will have been addressed. However, decisions should only be made against the most recent appraisal.

An accumulation of appraisal records is likely to increase the risk of intrusion by an inevitable widening of access. In that there may be value in identifying trends over time, records may be kept for three years, but the period set should be as determined by the Secretary in consultation with appraisees. Records should be regularly culled and destroyed as indicated in Archives Schedule 11 for Staff and Establishment Records..

ACCESS TO RECORDS

Officers will have an absolute right of access to the record of their appraisal at all times. The appraising officer, the reviewing officer and the Chief Executive Officer will also have access.

Disclosure to third parties, including selection advisory committees, will not occur except with the prior consent of the officer subject to the report and except as required by law. Appraising officers who form part of a selection committee should not refer to the records as part of the selection procedures except with the consent of the officer or unless the record is submitted by the officer. No coercion may be applied to obtain consent to provision of appraisal records.

Attachment D Reading list

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