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Federal Pay Outpaces Private-Sector Pay

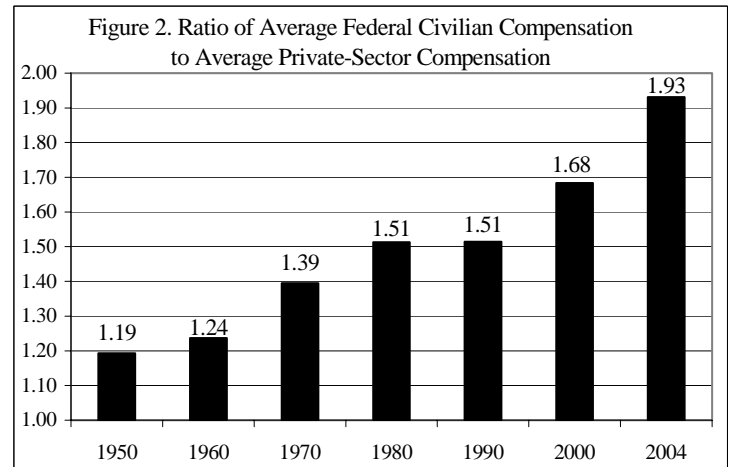
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Compensation for the federal government's 1.9 million civilian workers in the executive branch costs almost \$200 billion annually. Federal wages and benefits have been rising quickly, and by 2004 the average compensation of federal workers was almost twice the average in the private sector. Compensation policies should be examined for possible savings to reduce large federal budget deficits.

Federal Pay Advantage Is Growing

The average federal worker earned \$100,178 in wages and benefits in 2004, which compared to \$51,876 for the average private-sector worker, according to U.S. Bureau of Economic Analysis data.¹ Looking just at wages, federal workers earned an average \$66,558, 56 percent more than the \$42,635 earned by the average private worker.

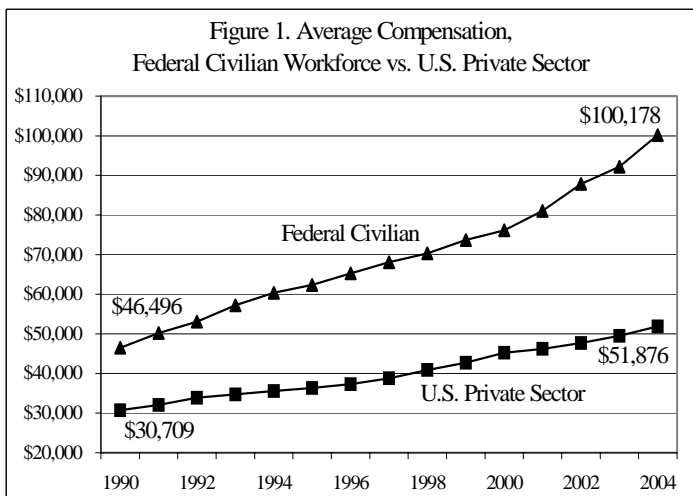
Figure 1 shows that federal compensation has grown more rapidly than private compensation in recent years. Since 1990, average compensation has increased 115 percent in the government and 69 percent in the private sector, while average wages have increased 104 percent in the government and 65 percent in the private sector.



Source: Author, based on U.S. Bureau of Economic Analysis data.

Figure 2 shows the ratio of average federal to average private compensation over time. Between 1950 and 1980, the federal pay advantage rose from 19 percent to 51 percent. During the 1980s, federal benefits grew quickly but wage increases were restrained, with the result that the overall federal pay advantage was stable. But since 1990, the federal advantage has soared, reaching 93 percent by 2004. While the current administration has supported greater pay flexibility and other management reforms, it has presided over large increases in federal pay.

Increases in federal compensation have stemmed from general wage increases, increased locality pay, expansions in benefits, changes in the nature of federal work, growth in the number of high-paid jobs as the workforce has become more top heavy, and other factors. Pay inflation has been fueled by routine adjustments that move workers into higher salary brackets regardless of performance, and by jobs that are redefined upward into higher pay ranges. The federal civilian workforce has become an elite island of secure and high-paid workers, separated from the ocean of private-sector American workers who must compete in today's dynamic economy.



Source: Author, based on U.S. Bureau of Economic Analysis data.

Are Federal Workers Underpaid or Overpaid?

Despite the escalation of federal compensation, some government studies have found that federal workers are underpaid, and that they suffer from a “pay gap” compared to private-sector workers.² By contrast, some academic studies have found that federal workers are overpaid.³

Comparison studies that find a pay gap sometimes compare federal workers to those in large businesses. But many U.S. workers are employed by small businesses, which tend to have lower compensation levels.

More important, comparison studies typically look just at wages and don’t consider the superior benefits paid by the government. Federal workers receive health benefits, retirement health benefits, a pension plan with inflation protection, and a retirement savings plan with a very generous match. (By contrast, 40 percent of private-sector workers do not have access to an employer retirement plan at all.) Federal workers typically have generous holiday and vacation schedules, flexible work hours, training options, incentive awards, excessive disability benefits, flexible spending accounts, union protections, and a usually more relaxed pace of work than private workers.

Perhaps the most important benefit of federal work is the extreme job security. The rate of “involuntary separations” (layoffs and firings) in the federal workforce is just one-quarter the rate in the private sector.⁴ Just 1 in 5,000 federal nondefense workers is fired for poor performance each year.⁵ All these federal advantages in benefits suggest that, in comparable jobs, federal wages should be lower than private-sector wages.

A market indicator of the adequacy of federal pay is the quit rate. The rate of “voluntary separations” (quits) in the federal government is just one-quarter the rate in the private sector.⁶ That suggests that pay in most federal jobs is more than adequate, and workers could be attracted with reduced compensation.

Of course, certain federal jobs may be underpaid and others overpaid compared to private markets. For example, the average annual compensation of federal air traffic controllers seems rather high at \$170,000.⁷ To objectively find the proper pay level, one could privatize this activity and let the market decide. Indeed, air traffic control, postal services, and other activities should be privatized to improve industry performance and to allow for more efficient and flexible compensation policies for workers.

Opportunity Cost of Federal Workers

In discussions about the federal workforce, it is often assumed that the government should have the highest-skilled workers and should pay high wages to get them.

However, for the overall economy, federal hiring of top caliber workers is a problem because it draws talent away from high-valued activities in the private sector. With today’s large government, marginal resources are likely to be more efficiently used in the private economy, thus shifting more skilled workers to the government would reduce gross domestic product. An opportunity cost of federal spending on an activity such as space exploration is to draw engineers and scientists away from more productive private space and aeronautical endeavors.

In France, most of the best minds move from the elite schools into the national government, and the economy is weaker for it. In the United States, most of the best minds are attracted to places such as Silicon Valley, not Washington, and we prosper because of it.

Conclusions

In the near term, Congress should restrain federal compensation by freezing federal wages for a period of years and examining fringe benefit programs for possible savings. The Congressional Budget Office has proposed numerous savings ideas for federal retirement plans.⁸

In the longer term, the coming surge in federal worker retirement as baby boomers enter their sixties offers an opportunity to downsize federal agencies without problematic layoffs or buyouts. As government air traffic controllers, space scientists, and others retire in coming years, these activities should be handed over to the private sector so that they can be better managed and have more efficient compensation policies.

¹ U.S. Bureau of Economic Analysis, National Income and Product Accounts data, Tables 6.2, 6.3, 6.5, and 6.6, www.bea.gov/bea/dn/nipaweb/index.asp. Averages are based on full-time equivalents. Data exclude the U.S. Postal Service.

² Congressional Budget Office, “Measuring Differences between Federal and Private Pay,” November 2002.

³ For example, see Steven Venti, “Wages in the Federal and Private Sectors,” National Bureau of Economic Research, Working Paper no. 1641, June 1985. Also see analyses by Wendell Cox at www.publicpurpose.com/ge-ix.htm.

⁴ See U.S. Bureau of Labor Statistics “JOLTS” data for 2004 and 2005 at www.bls.gov/jlt/.

⁵ Chris Edwards, *Downsizing the Federal Government* (Washington: Cato Institute, 2005), p. 74.

⁶ See U.S. Bureau of Labor Statistics “JOLTS” data for 2004 and 2005 at www.bls.gov/jlt/.

⁷ Federal Aviation Administration, “FAA Contract Negotiations with NATCA Reach Impasse,” press release, April 5, 2006.

⁸ Congressional Budget Office, “Budget Options,” February 2005, pp. 219-22.