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Public Sector Compensation in Local Governments

An Analysis

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The purpose of this study was to examine local government compensation practices across the United States and to explore possible correlations of these practices to service delivery. One hundred twenty of the largest cities and counties responded to a mail survey, for a response rate of 40%. The data suggest a large percentage (86%) of local governments faced financial difficulties in the form of a budget shortfall since 2000. In response to these shortfalls, local governments were more likely to reduce their workforce, reduce or eliminate services, and/or raise taxes or user fees rather than scale back wages and benefits. Because of this reaction, more than one half of the respondents experienced a decrease in full-time equivalent employment per 1,000 residents. Collective bargaining status, geographical region, and type of government (county or city) were found to be significant factors in determining compensation practices. Implications for practice and policy are advanced.

Keywords: *public sector compensation; service delivery*

Ray Scheppach, executive director of the National Governors' Association, recently asserted that the public sector has entered into a period of perpetual fiscal crisis (Pierce, 2002). This assertion was echoed by the National League of Cities' report that contends "America's cities were less able to meet their financial needs in 2004, and expectations for 2005 are equally grim" (Pagano, 2004, p. iv). Leading the list of factors contributing to the undue hardships on municipal budgets were the growing costs of employee health benefits (cited by 96% of respondents) and employee wages and pension plans (cited by 93%). A similar report prepared by Carl Vinson Institute of Government for the National Association of Counties found that nearly 72% of the 715 counties responding were facing budget shortfalls (Clark, 2003). The report noted that the gap between revenues and expenditures was

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attributable to rising employee health care and pension costs; declines in sales, income, and tourist tax revenues; and cuts in state aid (Clark, 2003).

Currently, there is a great deal of debate and dialogue about the issue of public sector compensation and retirement benefits. It is difficult to pick up a local newspaper without reading about concerns regarding public sector wages, benefits, and/or pension programs. Concerns have not been limited solely to local media outlets. Major national print publications such as the *Los Angeles Times* and *The New York Times* have underscored the widespread nature of the issue and have weighed in on the benefit levels granted to public sector employees (Saillant, 2004a; Walsh, 2004). This scrutiny has surfaced as state and local governments face revenue shortfalls, service reductions to citizens, and underfunded pension programs.

Some journalists and economists have suggested that state and local governments themselves have brought on the fiscal crisis by their own lack of restraint rooted in excessive increases in employment and compensation of government workers (Broder, 2004; G. H. Miller, 1993; "Public Pensions," 2004; "Spike," 2004). Others have asserted that the drop in revenues, a faltering economy, and increased service demands are largely to blame for the fiscal crisis of local governments (Berman, 2005; Kearney, 2005).

Many potential factors can affect the level of compensation and benefits received by public sector employees. The first purpose of this article is to examine public sector compensation practices and related issues currently confronting local government throughout the United States.

The second purpose of this article is to explore whether there is a correlation between public sector compensation practices and changes in service delivery in those local governments that have experienced budget shortfalls in the past few years.

Conceptual Frameworks

There are several frameworks available to assist in conceptualizing public sector compensation and in determining what relationship compensation may have to service delivery in local governments. The generally accepted principle for determining pay in the public sector is that public employees should be compensated in a manner comparable to their private sector counterparts (Kroncke & Long, 1998). This is consistent with economic and efficiency principles and with concepts of *fairness* and *equity* (Smith, 1977a; Venti, 1987).

A well-designed compensation system includes economic and nonmonetary components, includes criteria of fair pay for fair work, and has important social and symbolic roles in the organization, such as employee commitment and performance (Bloom, 2004). Many common features of a public sector compensation system include seniority contributions (longevity), competency measures, and pay-for-performance plans such as merit pay and bonuses. The public sector has traditionally

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relied on job tenure, cost-of-living increases, and average general increases for its compensation practices. In addition, benefit packages typically include health, pension, vacation, and paid time-off benefits. Seniority usually plays a central role in traditional compensation systems where movement through the pay scale is tied to rank. Merit pay programs reward individual performance and performance differences by granting different increases to base wage or salary. New pay concepts have been emerging in the public sector, such as skill-based pay or competency-based pay, which place greater emphasis on individuals and their capabilities (Risher & Fay, 1997; Roberts, 2004).

There have been several studies comparing the compensation levels of public and private sector employees (Blanchflower & Bryson, 2004; Braden & Hyland, 1993; Gyourko & Tracy, 1988; G. H. Miller, 1993; M. A. Miller, 1996; Nigro & Nigro, 1994; Smith, 2001). Although this area has been the focus of considerable research, there is little consensus on what pay differentials exist and whether these differentials are justified. Public–private comparisons can prove challenging because of confounding factors, such as worker characteristics and wage dispersions (Borjas, 2002).

Pay differentials between the private and public sector vary depending on the specific level of government. Previous research has examined the differences between similar positions in the federal government and private industry (Moore & Raisin, 1991; Smith, 1977a). Most studies have a positive differential for federal government workers as opposed to their private sector counterparts. This effect has been prevalent even though pay for many federal positions is based explicitly on equivalent private sector compensation.

Compensation for state and local government employees typically shows smaller differences when compared to private industry (Braden & Hyland, 1993; M. A. Miller, 1996). However, when comparisons between public and private sector employees include benefits along with wages, the gap between the two groups widens, with a positive differential for the public sector (Quinn, 1982; Roberts, 2004). Pay differentials also vary across states, with some state and local governmental employees even showing a negative wage differential with their private sector equivalents (Kroncke & Long, 1998). Differences have been observed when making comparisons between white-collar and blue-collar jobs (M. A. Miller, 1996; Nigro & Nigro, 1994), gender (Choudhury, 1994; Smith, 1977b), and racial categories (Asher & Pophin, 1984). Nigro and Nigro (1994) found compensation for many executive-level and professional employees was lower in the public sector, whereas compensation for lower-level positions in the public sector exceeded the private sector. Several reasons for this variance have been proposed, including occupational mix and the types of compensation packages provided (Braden & Hyland, 1993).

A full private–public comparison analysis is beyond the scope of this article; however, it may be helpful to look at recent differences between public and private

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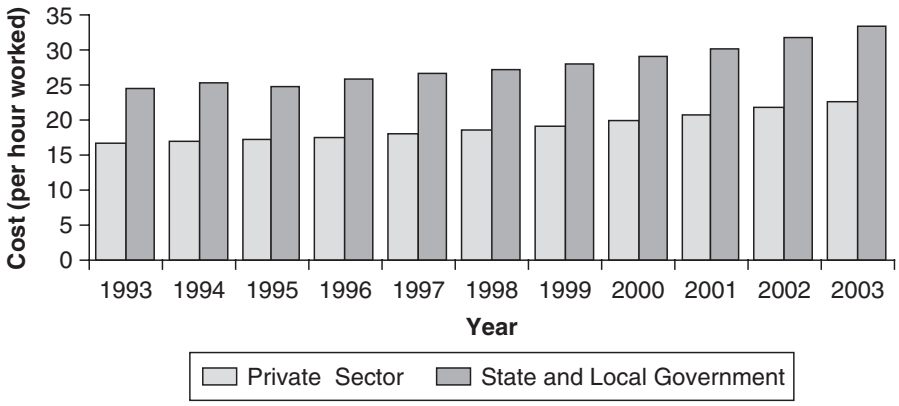
Figure 1
Cost of Compensation, Private Versus Public Sector



Source: Bureau of Labor Statistics (2005a).

compensation at the state and local level. The Bureau of Labor Statistics (BLS) collects annual data on compensation costs for private industry and state and local government. Figure 1 presents differences in compensation levels between the private sector and state and local government, whereas Figure 2 shows the recent rates of change in the two sectors.

According to the latest compensation figures collected by the BLS, public sector employees on the average earn US $11 an hour more than their private sector counterparts ($10 for white-collar jobs and $5 for blue-collar jobs; BLS, 2005a). Figure 2 shows that the recent rates of change for the public and private sectors are roughly the same. These data tend to suggest that the difference in compensation for state and local government employees does not appear to be a passing trend.

Various explanations have been set forth to explain the higher compensation levels of public sector employees. Some researchers propose this higher pay is justified based on worker characteristics, whereas others propose it is because of the earnings dispersion of government pay (Belman & Heywood, 2004; Borjas, 2002). Whether the differences between the public and private sectors are justified is unsettled and continues to spark debate among notable observers (Wiatrowski, 1994).

A more recent area of study addresses the growing importance of benefits to public sector workers. Public sector employees typically collect higher benefits as a percentage of final pay than do those in the private sector (Peterson, 2004). The average benefit cost to employers as a percentage of wages and salaries is 31% in the public sector and 24% in the private sector (BLS, 2005b). The near-complete

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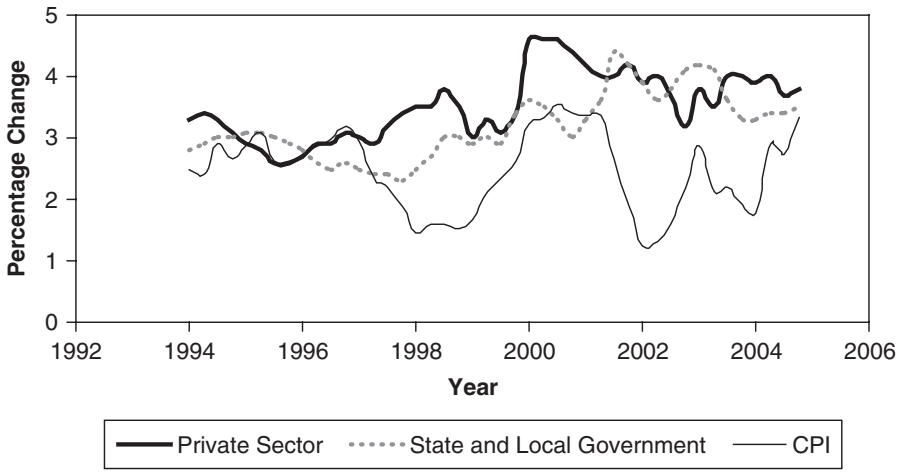
Figure 2
Trends in Total Compensation, Private vs. Public Sector



Source: Bureau of Labor Statistics (2005a).

enrollment in retirement plans by public sector employees is in sharp contrast to the roughly 50% of private workers enrolled in similar plans (BLS, 2005a). Moreover, 90% of public employees have fixed benefit plans (i.e., defined benefit plans) compared to 17% of private employees (Peterson, 2004). As a result, compared to private sector employees, public employees typically bear none of the investment risk of their pensions (Schneider, 2005). In addition, public sector employees can retire on full pensions an average of 5 years earlier than their private sector counterparts can (Clowes, 2004).

Another principle used in setting public sector wages and benefits deals with consideration of the impact wages and benefits will have on future generations of elected officials, public administrators, and citizens. Peng (2004), utilizing the theory of intergenerational equity, suggests, for example, that delaying pension payments in the context of structural or other budget problems or granting wage and benefit increases that government cannot afford simply shifts the financial obligation from the current taxpayers at an increasing cost, thus violating the intergenerational equity principle. Some local governments increased pension benefits (either in flush economic times or as an alternative to wage increases in depressed economic times) in an attempt to be seen as partners with union and employee groups rather than as adversaries. These changes resulted in employees being able to retire at an earlier age, to receive a larger percentage of their working salary, and/or to have a portion

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or all of their health care covered on retirement. As the financial impact of these commitments became apparent, governments found themselves turning to tax increases, service reductions, and/or borrowing to cover these costs (Metha, 2004; "Pension Spike," 2004; Saillant, 2004b). The $1.4 billion pension deficit in the city of San Diego, California, is an example of what can occur when there is a combination of questionable investment practices, deliberate underfunding, and increased benefits. A report completed by Vinson and Elkins L.L.P., the law firm hired to investigate why the growing pension deficit was not disclosed until it was out of control, states, "This situation evolved in a piecemeal fashion through trade-offs between the city and its municipal unions, in each instance reflecting the short-term horizon of the City's budgetary process" (Maco & Sauer, 2004, p. 5).

The "union power" thesis advanced by Wellington and Winter (1971) holds that labor unions in the public sector have the ability to create government wage differentials through political action rather than through collective bargaining. Building on this thesis, Hunter and Rankin's (1988) compensation model suggests that public employees are compensated for providing two sets of services: public services and political services. Public services are those the public expects employees to provide, and political services include activities such as endorsing candidates, raising money or giving campaign donations, and/or providing staffing for particular elections. The authors contended that this helps explain why fringe benefits have grown substantially in the public sector and are larger as a percentage of wages and salaries than the private sector. As previously noted, the average benefit cost for the public sector is approximately 31%, whereas the average benefit package for the private sector is 24% (BLS, 2005b). According to Hunter and Rankin, fringe benefits provide the perfect avenue for political payment because they are usually invisible or unknown to the public. The political power of public sector unions will have a greater impact on fringe benefits than on wages if compensation in that form is least likely to be subjected to public scrutiny (Hunter & Rankin, 1988).

Research conducted by Benecki (1978), Vallenta (1989), and Zax and Ichniowski (1988) found that local government unionism can increase department and city expenditures. However, O'Brien (1994) found that although increased union political activity leads to greater department expenditures, it did not necessarily lead to greater municipal expenditures or revenues.

Finally, in Freeman and Medoff's (1984) book *What Do Unions Do*, the authors posited that there are two faces of unions. One face is the undesirable monopoly, which enables unions to raise wages above the competitive level, resulting in a loss of economic efficiency. The inefficiency arises because employers adjust to the higher union wages by hiring too few workers in the employment place. The other face is the more desirable face that allows them to channel worker discontent into improved workplace conditions and productivity (Blanchflower & Bryson, 2004). Under the undesirable monopoly premise, the financial flexibility of local and state government is compromised because of commitments to existing wage and benefit

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levels, and thus, they are unable to add more employees to meet service demands. There is some empirical evidence to support this thesis (Bryson, 2001; Leonard, 1992).

Compensation for public sector employees continues to be an area of interest among researchers, policy makers, and practitioners. Determining appropriate compensation levels for public sector employees can be a challenge because of economic conditions and the structure of governmental institutions.

Method/Measures

A survey dealing with public sector compensation and related issues confronting local governments throughout the United States was administered to human resource directors in the largest 150 cities (populations more than 160,000) and 150 counties (populations more than 360,000) in October 2004. Each mailing contained an introduction letter and a survey instrument as well as a prestamped return envelope. Those not responding to the initial mailings received follow-up phone calls and e-mail reminders. Data collection ended in February 2005. Of the 300 survey recipients, 120 responded, for a response rate of 40%. Analysis of responding and nonresponding local governments can be found in Table 1. A similar number of counties versus cities responded; however, there was an underrepresentation of respondents from the northeast region of the United States. The survey instrument addressed questions on the general fiscal conditions of the local government as well as on compensation, benefits, health insurance, retirement and/or pension plans, merit performance systems, and collective bargaining status. The survey targeted general fund budget expenditures only and did not include schools. In addition, respondents were asked to respond to their largest employee union, if there were multiple plans. The instrument was pretested on financial and human resource directors in local governments.

Results

Survey Responses

Table 2 provides a summary of the survey responses. The data suggest that an overwhelming number of governments, 86%, faced financial difficulties in the form of a budget shortfall since 2000. The economic recession of 2000-2001 is an obvious contributor.

With regard to strategies to address budget shortfalls, governments appeared to rely on a combination approach. The three most popular strategies dealt with reducing their labor force: elimination of vacant positions (79%), instituting a hiring freeze (78%), and employee layoffs (51%). These approaches were followed by reducing and/or eliminating services to the public (39%) and raising taxes and/or user fees (31%). Fourteen

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Table 1
Respondent and Nonrespondent Characteristics

	Survey Sample		Survey Nonrespondents	
	N	%	*N*	%
Type of government				
County	50	41.7	89	49.4
City	62	51.7	87	48.3
Combined	8	6.7	4	.3
Total	120	100.0	180	100.0
Region				
Northeast	10	8.3	35	19.4
Midwest	27	22.5	30	16.7
South	42	35.0	62	34.4
West	41	34.2	53	29.4
Total	120	100.0	180	100.0

percent of governments chose to reduce wages and/or benefits for current employees. Kearney (2005) found similar results in responses to shortfalls experienced in the early 2000s. Municipalities typically raised service fees (88%), froze vacant positions (83%), used reserves (82%), and increased taxes (73%). These statistics clearly indicate governments were more likely to reduce their labor force, reduce services, and raise taxes than cut wages and benefits in response to budgetary shortfalls. Along similar lines, 54% of governments stated they had a decrease in full-time equivalent (FTE) employees per 1,000 citizens since 2000.

The average benefit costs as a percentage of wages and/or salaries were approximately 37%, whereas the average percentage of the government budget dedicated to salaries and benefits was 58%. This relatively high percentage was consistent with expectations, as salaries and benefits usually make up the largest share of local and state government budgets (BLS, 2005b). More interesting was the change in this percentage since 2000. Of responders, 59% stated that wage and benefit cost percentages had increased since 2000, whereas about 33% said this percentage stayed constant. Only 8% of the governments responding indicated a percentage decrease since 2000. This again indicates a strong tendency toward increased wage and benefit preservation in the face of a budget shortfall.

About one half of the governments surveyed offered longevity payments to their employees. A small percentage of governments, 14%, eliminated longevity payments to certain employees since 2000. A larger percentage, 47%, altered the longevity payments in other ways.

The average cost-of-living adjustments (COLAs) for fiscal years 2001 through 2005 were 1.96. In both fiscal years 2001 and 2002, the average was 2.23. The average COLA fell to between 1.60 and 1.86 for the next 3 fiscal years. There were also

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Table 2
Summary Statistics

	N[a]	%
Budget shortfall since July 2000?	117	86
Local government response		
Eliminated vacant positions	101	79
Imposed a hiring freeze	101	78
Laid off employees	101	51
Offered early retirement incentives	101	27
Furloughed employees	101	13
Reduced and/or eliminated services to the public	101	39
Raised taxes and/or increased user fees	101	31
Reduced benefits and/or wages to existing employees	101	14
Other	101	20
Decline in the number of FTE per 1,000 citizens < July 2000?	114	54
Benefit costs (as a percentage of wages and/or salaries)?	98	37
% overall budget dedicated to salaries and/or benefits?	97	58
Since July 2000 has this % increased	80	59
Since July 2000 has this % decreased	80	8
Since July 2000 has this % constant	80	33
Offer longevity payments?	117	50
Average COLAs FY 2001–2005	113	1.96
COLA FY 2001	112	2.23
COLA FY 2002	113	2.23
COLA FY 2003	112	1.86
COLA FY 2004	112	1.73
COLA FY 2005	86	1.60
Health insurance		
Employees contribute to the health coverage?	115	70
If yes, what percentage?	63	14.82
Health insurance contributions risen since July 2000?	112	68
If yes, by what percentage?	81	15.56
Increased employee premium contributions	114	56
Increased employee copayments	114	71
Increased employee coinsurance percentage	114	30
Increased deductible amounts	114	56
Increased and/or revised drug formulary	114	56
Retirement		
Participate in a defined contribution plan (DC)?	118	17
Participate in a defined benefit plan (DB)?	118	67
Participate in other retirement plans?	118	3
Contribute toward retiree health care coverage?	116	63
Has the percentage risen since July 2000?	54	24
Increased employer contribution rate	108	39
Increased employee contribution rate	108	24
Increased retirement age	108	3

(continued)

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Table 2 (continued)

	N^a	%
Decreased retirement age	108	6
Other changes to retirement	108	36
Experienced any difficulty in funding pension plan?	113	22
Offer a "pay for performance" and/or merit performance system?	116	57
Allow for collective bargaining for wages and benefits?	117	64
Survey responses	120	

Note: FTE = full-time equivalent; COLA = cost-of-living adjustments; FY = fiscal years.
a. *N* = total responses to question.

fewer responses for fiscal year 2005, as COLAs for that year may have not been determined at the time of the survey.

Regarding health insurance, approximately 70% of governments had employees contribute to their health insurance. A large percentage of governments, 68%, stated that their employer health contributions as a percentage of salaries had increased since 2000. Rising health care costs are not unique to government, and the data paint a portrait of governments shifting some of these rising costs to the employees. Of governments, 56% increased employee premiums, whereas 71% increased employee copayments. A smaller percentage, 30%, increased the coinsurance percentage. Of governments, 56% increased deductible amounts, whereas the same percentage also increased or revised their drug formulary. It is interesting to note, 50% of all governments did opt out of their current plan, suggesting many governments were searching for better alternatives. A small number of governments chose other measures with respect to health insurance, such as eliminating some previously covered services or eliminating duplication of benefits.

Concerning retirement plans for employees, 95% of respondents offered retirement plans, whereas two thirds of the responders stated they offered a defined benefit plan. A smaller percentage, 17%, offered a defined contribution plan. An even smaller number of governments offered a combination plan or other retirement options. With respect to changes in retirement plans, 39% of responders stated they had increased the employer contribution rate, whereas 24% said they had increased the employee contribution rate. Fewer governments chose to either increase (3%) or decrease (6%) the retirement age for their retirement plan. Approximately 36% of governments made other changes to their retirement plans, such as decreasing the contribution or vesting time. Of governments, 63% contributed to their retirees' health care coverage. Only 22% of governments experienced difficulty in funding their pension plan.

Finally, 57% of respondents indicated their city and/or county offered a "pay-for-performance" system and/or merit performance system, whereas 64% of responders stated that their government allows for collective bargaining for wages and salaries.

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Decline in FTEs

A decrease in FTE employment per 1,000 citizens since 2000 was cited by 54% of the respondents. Because of this finding, additional empirical analysis was performed. This is an important result, as fewer employees per citizen may lead to lower quality public services.

The dependent variable for this analysis is FTE. Independent variables are as follows: other expenditure-related variables such as benefits costs as a percentage of wages and salaries (BENPERC), longevity (LONG), average cost-of-living adjustments (AVECOLA), participation in a defined contribution program (DEFCON), participation in a defined benefit program (DEFBEN), an employer's health care contribution to retirees (RETIREECON), a variable for governments experiencing a budget shortfall (SHORTFALL); and other variables such as type of government, that is, county and/or city (TYPE), geographical region (REGION), and collective bargaining status (COLLECTIVE). The empirical formula is as follows:

$$FTE = \exists' X_1 + \gamma_1$$

The results of this logit analysis are presented in Table 3.

The SHORTFALL variable is highly significant ($p < .001$), and it has a positive coefficient. This follows from the above analysis that governments faced with a budget shortfall often choose to reduce their labor force as the primary response. The RETIREECON variable is also statistically significant ($p < .05$) and has a positive coefficient. This result suggests that governments contributing to retiree health care may be more likely to have a decline in FTEs. This is consistent with expectations, as payments for retirees leave fewer funds available for current wage and salary outlays.

The COLLECTIVE variable is highly significant ($p < .001$) and has a large positive coefficient. This suggests a relationship between collective bargaining ability and a decline in FTEs. Again, this is consistent with expectations and the discussion provided above involving unionization and compensation. It appears that governments often choose to lay off employees rather than cut wages and benefits, and even more so when a collective bargaining agreement is in place.

Collective Bargaining, Geographical Region, and Type of Government

Additional analyses were performed comparing collective bargaining (COLLECTIVE), geographical region (REGION), and type of government (TYPE) and their effect on overall budget shortfalls and compensation practices, such as average COLA, merit pay, and longevity payments. A high percentage, 86% of local governments, indicated they had experienced a budget shortfall since 2000. A logit

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Table 3
FTE (Full-Time Equivalent) Employee Logit Analysis

	b	*SE*	Wald	Significance
SHORTFALL	3.792	1.148	10.912	.001*
BENPERC	–.014	.027	.263	.608
LONG	–1.221	.677	3.257	.071
AVECOLA	–.062	.316	.039	.844
DEFCON	23.963	40193.183	.000	1.000
DEFBEN	24.766	40193.183	.000	1.000
RETIREECON	1.610	.786	4.201	.040**
TYPE	.215	.375	.328	.567
COLLECTIVE	2.924	.900	10.555	.001*
REGION	.253	.414	.374	.541

Note: SHORTFALL = budget shortfall; BENPERC = benefits costs as a percentage of wages and salaries; LONG = longevity; AVECOLA = average cost-of-living adjustments; DEFCON = defined contribution program; DEFBEN = defined-benefit program; RETIREECON = employer's health care contribution to retirees; TYPE = as type of government, that is, county/city; COLLECTIVE = bargaining status; REGION = geographical region.
*$p < .01$. **$p < .05$.

analysis was performed (Table 4.1) to see if collective bargaining, geographical region, and type of government may have contributed to budget shortfalls. The independent variable for the analysis was SHORTFALL. The type of government (county vs. city) variable is highly significant ($p < .01$). The coefficient is negative, suggesting an inverse relationship between type of local government and budget shortfalls. Stated differently, county governments tended to have fewer budget shortfalls than city governments did.

In the next analysis (Table 4.2), AVECOLA was the independent variable. Collective bargaining was highly significant ($p < .000$), with collective bargaining increasing the average COLA. When merit pay (MERITPAY) was used as the independent variable (Table 4.3), collective bargaining was again significant ($p < .01$), however, in this case had a negative effect. Regarding longevity payments (Table 4.4), the region variable (REGION) was significant ($p < .01$) and negative; the Northeast and Midwest appear less likely to offer longevity payments.

Discussion

The fiscal crisis facing local governments is occurring as citizens increasingly demand more efficiency, better outcomes, increased services, and fewer taxes (Osborne & Hutchinson, 2004). Aharoni (1981) characterized citizens as wanting a "no-risk society" where they demand fewer regulations and lower taxes while simultaneously

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Table 4.1
SHORTFALL Logit Analysis

Variable	Coefficient	*SE*	*p* <
TYPE	–1.551	.569	.006*
REGION	–.442	.514	.390
COLLECTIVE	–.557	1.177	.636

Note: SHORTFALL = budget shortfall; TYPE = as type of government, that is, county/city; REGION = geographical region; COLLECTIVE = bargaining status. Dependent variable: Yes/No, does county/city face budget shortfall?
*$p < .01$.

Table 4.2
AVECOLA Logit Analysis

Variable	Coefficient	*SE*	*p* <
TYPE	–.032	.105	.764
REGION	.070	.111	.530
COLLECTIVE	1.396	.209	.000*

Note: AVECOLA = average cost-of-living adjustments; TYPE = as type of government, that is, county/city; REGION = geographical region; COLLECTIVE = bargaining status. Dependent variable: Average of COLA, 2001 to 2005 fiscal years.
*$p < .01$.

Table 4.3
MERITPAY Logit Analysis

Variable	Coefficient	*SE*	*p* <
TYPE	.087	.207	.673
REGION	.036	.209	.862
COLLECTIVE	–1.167	.426	.006*

Note: MERITPAY = merit pay; TYPE = as type of government, that is, county/city; REGION = geographical region; COLLECTIVE = bargaining status. Dependent variable: Yes/No, does county/city offer merit performance pay?
*$p < .01$.

seeking increased protection and special interests. The need to prioritize scarce resources is paramount, and although public scrutiny is not new, as state and local governments face revenue shortfalls, service reductions to citizens, and underfunded pension programs, focus will undoubtedly turn to public sector compensation practices.

The findings that have emerged from the current study of public sector compensation practices across large local governments in the United States produced several

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Table 4.4
LONG Logit Analysis

		Selected Variables	
Variable	Coefficient	*SE*	$p <$
TYPE	–.215	.206	.295
REGION	–.476	.217	.028*
COLLECTIVE	.314	.400	.432

Note: LONG = longevity; TYPE = as type of government, that is, county/city; REGION = geographical region; COLLECTIVE = bargaining status. Dependent variable: Yes/No, offered longevity payments?
*$p < .05$.

interesting findings. The significant number of governments facing a budget shortfall since 2000 underscores the fiscal crisis facing local governments. In response to these shortfalls, the data suggest that governments prefer to reduce their workforce, reduce or eliminate services to citizens, and/or increase taxes and/or user fees, rather than scale back wages and benefits. However, some local governments increased employee contributions for higher health care costs. Because of these reactions, more than one half of the responders experienced a decrease in FTE employment per 1,000 citizens. In addition, for more than 90% of governments responding to the survey, the percentage of the overall budget dedicated to salary and benefits increased or stayed constant since 2000. These data reiterate the reluctance, or inability, of local governments to reduce wages and benefits to employees in the face of financial difficulty.

During the study period, governments were also faced with rising health care costs, as 68% of responders cited increases. It is not surprising to note, these health care costs were often shifted to employees who faced higher premiums, copayments, and deductibles. With regard to retirement plans, 95% of local governments surveyed offered retirement plans to their employees, and the majority of governments offered their employees a fixed or defined benefit plan. In addition, the majority of responders contributed to retirees' health plans. This is clearly in contrast to the private sector, where roughly 50% of private workers are enrolled in retirement plans offered by their employer, and contribution to retiree health plans is low (BLS, 2005b).

The results of the empirical analysis (logit analysis) set forth at the outset of the current study found positive correlations concerning the decline in FTEs. Local governments encountering a budget shortfall were more likely to face a decline in the number of FTEs per 1,000 residents. As mentioned earlier, this was the preferred response of local governments to fiscal difficulties. The reluctance to address wage and benefit levels in the face of budget shortfalls and instead reduce service levels and raise taxes will be increasingly difficult to defend as public awareness on the growing disparity of wage and benefit levels between government workers and

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private sector workers becomes known. The impact of contracting-out strategies of local governments facing fiscal stress was not measured. Fewer FTEs per 1,000 population may reflect a shift toward (private sector) contractor-provided services and not a lowering of overall service levels. The contribution to retiree health care was also significantly correlated to a decline in FTEs. The long-term financial obligation suggests payments for retirees leave fewer funds available for current wage and salary outlays.

The findings from this research also indicated that collective bargaining, geographical region, and type of government were significant factors in determining compensation practices and local governments' responses to budget shortfalls. The local governments that responded to the survey had workforces that were much more unionized than the public and private sectors were. Almost two thirds of responders stated they participated in collective bargaining with their employees. Union membership as a percentage of state and local government employees has been between 38% and 40% for the past decade, whereas union membership in the private sector is less than 10% (Hurd & Pinnock, 2004). This higher rate of unionization could be a result of surveying larger counties and cities where collective bargaining practices may be more common.

Local governments that had collective bargaining agreements were more likely to face a decline in the number of FTEs per 1,000 residents. In addition, collective bargaining was related to the increase in average COLAs and made it less likely that local governments employed merit-based compensation practices. Hence, governments may be more likely to reduce the labor force, through layoffs and elimination of vacant positions, rather than to decrease salary and benefit levels (particularly where bargaining power is strong). This interaction may lead to inefficient outcomes during times of financial stress, with government employees receiving above-market wages and benefits, and, in turn, citizens facing reduced service capacity.

County governments tended to have fewer budget shortfalls than did city governments. There could be several reasons for this relationship. Counties may contain a wider geographical area and therefore receive tax revenue from more diverse sources. Counties tend to rely more heavily on property taxes, which is a more stable form of taxation and is more likely not to have wide shifts compared to sales tax or similar fees that are more sensitive to the economy. Alternatively, city governments may miss tax revenue from some more affluent areas outside the city limits, or some cities may be at a lower point in the public revenue waterfall. Regardless, county governments appeared to be more insulated from shortfalls than did city governments. Longevity payments appeared to take on a regional significance. The practice of awarding longevity payments to public employees seems more prevalent in the South and West. This could be a result of the inability or reluctance to remove these practices from collective bargaining agreements in these geographical areas.

In light of this discussion, it is important to consider limitations to this study. First, data collection methods in this study relied on self-reports that may be susceptible to

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response bias. Additionally, the survey sample focused on larger local governments. The extent that smaller local governments have similar or different experiences and practices is not clear. As mentioned earlier, there was an underrepresentation from the Northeast region of the United States when survey respondents and nonrespondents were compared. Finally, the survey did not capture the size of the budget shortfall, and this may have influenced the choice regarding some responses such as the labor responses. Despite these limitations, this research offers important insight into public sector compensation practices in the United States.

Conclusion

Economic, political, sociodemographic, and environmental conditions all have a profound impact on local government budgets, compensation practices, and service delivery, as well as their causes and available remedies. The results of this exploratory research suggest that collective bargaining, geographical region, and type of government may have important impacts on compensation practices, which in turn have an impact on local government budgets because employee wages and benefits make up such a significant portion of the budget. The research also suggests that local governments, when faced with budget shortfalls, generally do not reduce employee wages and benefits but take actions that result in reductions in service delivery (elimination of services or a reduction in the labor force) and/or the raising of additional revenue through increased taxes or user fees. Public sector compensation practices and the relationship to service delivery will continue to be important issues in need of attention from academics and practitioners in the field of public administration. The reality of permanent fiscal constraints on government (whether as a result of changes in economic conditions or imposed spending and revenue limitations), coupled with the escalation of wages and benefits in the public sector (compared to the private sector), will result in serious ramifications if not addressed proactively. As the public becomes increasingly aware of the increased cost of employee wage and benefit packages, the reality that many public pension programs are underfunded, and the extent to which governmental services are being reduced or eliminated, appropriate local government responses to public questions and criticism will be critical. Although these issues can be politically explosive to confront, ignoring them may have more serious ramifications and result in widespread public anger and hostility. An upset citizenry could lead to increased pressure for spending limitations, voter disapproval of tax increases, and even voter approval of changes to public sector compensation benefits. These direct democracy techniques with respect to compensation benefits are already being realized in cities such as Houston, Texas, and San Diego, California (Nissimov, 2004; Vigil, 2005). Therefore, local governments should begin to affirmatively address the following issues related to public sector compensation.

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Public Versus Private Sector Compensation

In recent years, there have been many studies comparing the compensation levels of public sector employees to those of private sector employees. Although this area has been the focus of considerable research, there is little consensus about whether pay differentials exist and whether these differentials are justified. Local governments need to determine whether their compensation practices rely too much on internal equity rather than on the market to determine the value of jobs and examine how public sector compensation compares to the private sector to determine whether any differential between the two is justified. Additional research that includes salary and benefit comparisons and compares equivalent jobs and workers is needed. Strategies utilizing market comparison studies should be required when considering public sector wage and benefit levels. This will ensure that equity and fairness principles are incorporated into public sector compensation practices.

Increased Transparency

More transparency with the public concerning public sector compensation practices is warranted. Local governments should include more public discussion of employee wage and benefit packages. In making decisions about public sector compensation and benefits, the financial impact of changes must be clearly discussed and analyzed to determine whether there is sufficient revenue to fund the changes without the need to increase taxes or fees and/or the need to reduce or eliminate services. COLA increases that exceed inflation and pay increases that are not based on merit or performance will need to be more clearly justified. Local governments need to be prepared to explain to their citizens why wage and benefits reductions are not considered when dealing with budget shortfalls.

Public Sector Employee Retirement Benefits

Local governments must confront the issue of underfunded retirement and/or pension plans before the problem increases. Changes to retirement benefits, including enhanced benefits, incentives to early retirement, and payment of retiree health care, must be carefully considered prior to implementation, especially the long-term financial commitments that may affect future generations of public officials and citizens.

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