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**REPORT TO THE SENATE COMMITTEE
ON APPROPRIATIONS**

**BY THE COMPTROLLER GENERAL
OF THE UNITED STATES**



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**Department of Defense
Should Change Pay Setting
For Filipino Nationals**

U.S. Forces in the Philippines employ about 22,000 Filipino nationals who are paid more than the local wage rates. The Secretary of Defense should make changes which would bring wages and benefits for Filipino nationals more in line with local rates, improve procedures, and reduce costs.

Department of Defense attempts to follow local prevailing pay practices have been hampered by labor agreements and a strong employee union, and changes will be difficult to make.

FPCD-77-70

OCTOBER 5, 1977

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COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-179343

The Honorable John L. McClellan, Chairman
Committee on Appropriations
United States Senate

Dear Mr. Chairman:

In response to your request of April 29, 1977, we are reviewing the compensation and use overseas of foreign national employees by the Department of Defense, including the possibility of using alternative labor sources that might be less costly to the Government.

This report on foreign national employment practices in the Philippines, the second of a series of reports on five countries, addresses the cost of compensation benefits and separation allowances, possible substitutes for foreign national employees, and barriers limiting U.S. control over wage increases.

Although foreign national labor costs in the Philippines are relatively low by world standards, the Filipino national employee is generously compensated relative to the average worker in that country. In part, this results from agreements with the Philippine Government and the foreign national employees' union which restrict the Defense Department's flexibility as an employer. Compensation costs could be reduced by improving procedures used to determine wages. Accordingly, we are recommending to the Secretary of Defense that several changes be made to wage setting methods.

As requested by your office, we did not obtain formal comments from agency officials; however, we discussed the results of our work with them and considered their comments. Defense was not optimistic that certain of our recommendations could be implemented due to strong union opposition. Because of the political situation surrounding the military base negotiations, we also obtained informal comments on our draft report from the State Department. They questioned the feasibility of implementing our recommendations in the near future; instead, they believe that any changes should be made over a period of several years. While we recognize that Defense's flexibility is limited by labor agreements and the current political situation, we believe every effort should be made to assure that Filipino employees receive the prevailing wage.

B-179343

As agreed with your office, we are sending copies of the report to the Department of Defense. Copies will also be available to other interested parties who request them.

Sincerely yours,


Comptroller General
of the United States

IMPROVEMENTS NEEDED IN FOREIGN NATIONAL
COMPENSATION PRACTICES IN THE PHILIPPINES

BACKGROUND

Section 444 of the Foreign Service Act, as amended, provides that compensation for foreign national employees will be based on locally prevailing wage rates that are consistent with the public interest.

The lead agent for Filipino national personnel policies is the Navy's Commander in Chief, Pacific Fleet, in Hawaii. Interservice coordination for foreign national personnel policies in the Philippines is the responsibility of the Commander in Chief, Pacific Representative, Philippines, who acts on the advice of a Joint Labor Affairs Committee. The Navy and Air Force have one voting member on the Labor Affairs Committee. U.S. civilian agencies in the Philippines and nonappropriated fund activities, who base compensation paid to their local employees on Department of Defense (DOD) wage survey results, may participate as nonvoting members.

Assisted by the Labor Affairs Committee, representatives of the U.S. Pacific Fleet in Hawaii oversee wage surveys of Philippine companies to determine local prevailing practices and thus foreign national compensation benefits. Recommendations for wage increases are forwarded to the Pacific Command's Joint Labor Policy Committee in Hawaii, which coordinates DOD personnel policies in the Pacific area. Acting on the decision of the policy committee, the Commander, Pacific Fleet, in Hawaii, relays revised schedules to the Philippines.

Number of employees and wages

DOD employs nearly 22,000 Filipino nationals at an estimated cost of \$42 million for fiscal year 1977 as shown on the following page.

APPENDIX I

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	Number of employees (<u>note a</u>)	FY 1977 estimated payroll <u>costs</u>	Average cost per <u>employee</u>
(000 omitted)			
Appropriated fund:			
Navy	10,620	\$24,794	\$2,300
Air Force (note b)	<u>3,100</u>	<u>7,101</u>	2,300
Total	<u>13,720</u>	<u>31,895</u>	2,300
Nonappropriated fund:			
Navy	4,100	5,378	1,300
Air Force	<u>3,840</u>	<u>4,768</u>	1,200
Total	<u>7,940</u>	<u>10,146</u>	1,300
Total	<u>21,660</u>	<u>\$42,041</u>	<u>\$1,900</u>

a/Includes full-time, part-time, and intermittent personnel.

b/Includes Department of Defense (62 employees) and Army (2 hires).

Filipiroy employees also accrue separation entitlements up to 1 month's pay for each year of service, payable upon retirement, disability, death, or reduction in force. If an employee quits before retirement or is removed for cause, he receives no separation benefits. As of June 1977, the total separation liability was over \$23 million (\$18 million appropriated and \$5 million nonappropriated), or about \$1,100 per employee.

Although wage increases have averaged about 8.7 percent since 1971, devaluations of Philippine currency have limited average dollar cost increases to about 6.7 percent annually. However, the 1976 wage increases were sizeable--19 percent for manual employees and 12 percent for nonmanual. Officials predicted the Philippines expanding economy could lead to similar increases in the future; therefore, employment constraints and questionable wage survey techniques now having a limited adverse impact are apt to be more costly in future years.

Constraints on DOD's
employment flexibility

In part, DOD's attempts to adhere to prevailing practice criteria have been constrained by labor agreements and a strong local employees' union. Basic conditions of employment for Filipino employees are laid out in the Base Labor Agreement. The agreement is a diplomatic arrangement signed in 1968 by the Philippine and United States Governments to clarify labor provisions in the 1947 Military Base Agreement. Negotiations for a new bases (and labor) agreement were initiated in April 1976 but have progressed sporadically. As of June 1977, no consensus existed on when or if a new agreement would be reached.

Major provisions in the Base Labor Agreement include:

- Preferential employment. Filipinos will be used in civilian positions except when security or other "special management needs" require a U.S. citizen.
- Joint committee. A U.S./Philippines body for the purpose of hearing and attempting to resolve any dispute brought to it by either side; the committee has no enforcement authority.
- Right of employees to organize and bargain collectively. This provision also specifically bars disruptions to the "orderly and effective operation of the bases" until the joint committee has exhausted attempts to bring about resolution of the issues in dispute.
- Wage setting. Wages and compensation practices of progressive employers will be determined by technical surveys in which the union will participate, and these will be used as a basis for setting wages of U.S. Forces employees.
- Midyear bonus. A 200 peso bonus (about \$27 in June 1977) paid to each employee annually.

In recognition of Filipino rights to organize and bargain collectively, DOD and the employees' union further define employer-management relations in a Collective Bargaining Agreement. The present agreement became effective in 1976 and has a 3-year life. Most of the provisions of the Collective Bargaining Agreement elaborate on provisions of the Base Labor Agreement. However, the bargaining agreement establishes additional restrictions by limiting the

annual wage survey to a current agreed list of 30 companies, with any change to the list requiring both DOD and union agreement.

If the Base Labor Agreement is renegotiated as part of a new base rights package, DOD officials are pessimistic about any relief from past concessions and propose to retain the status quo wherever possible in negotiating a new labor agreement. Moreover, although the bargaining agreement will be subject to renegotiation in 1979, it now provides that current provisions remain in effect unless both signators agree to changes.

Filipino national employees' union

About 16,000 employees--80 percent of the work force--are represented by one union, the largest in the Philippines. According to DOD officials, this union has close ties with the Philippine Department of Labor and the news media. Reportedly, when the union is dissatisfied with a decision affecting employment, they appeal to the Labor Department which pursues the issue with the U.S. Embassy. The union's position on labor issues is also well aired by local newspapers. We were told the union can effectively limit DOD attempts to meet congressionally established criteria of prevailing practices by escalating disputes to a government-to-government level or by threatening to strike.

Both the Base Labor and Collective Bargaining Agreements state that disruptions of base operations before the joint committee has taken its final action may be cause for withdrawing recognition of that organization and disciplining disruptive employees. Even so, officials felt circumstances, political and otherwise, would dictate the control DOD could exert. Because of political sensitivities, we were told that the Navy, Air Force, and the Embassy would be reluctant to confront the union and the Department of Labor to correct some of the concessions discussed later in this report.

WAGE SURVEY IMPROVEMENTS NEEDED

The Collective Bargaining Agreement requires annual wage surveys to ascertain prevailing compensation levels in the Philippine private sector. Survey teams, consisting of one U.S. employee and one Filipino union official, visit private companies to obtain wage data which is summarized and used to establish wage schedules.

We identified the following practices which differ from local prevailing practice, affect the validity of wage survey data, and result in excessive Defense wage costs:

- Relying on wage information from high paying companies in a high paying area.
- Including monetized allowances in base pay computations which inflate other compensation items calculated on base pay.
- Paying midyear bonuses in addition to total compensation reflected in the private sector.
- Matching average private sector earnings to a predetermined wage schedule step, rather than the average work force earnings.
- Selecting key jobs with limited regard to work force composition.

Survey companies not representative

DOD bases its wage increases on wages and benefits paid by 30 companies in the Greater Manila area--high payers in a high wage area. Moreover, the Subic Bay Naval Complex and Clark Air Base are located outside the Manila area in the lower cost, smaller cities of Olongapo and Angeles.

The Collective Bargaining Agreement requires union agreement on any addition or change to the company list. In the past the union has rejected proposals to expand the number of companies surveyed or to include companies from areas around DOD bases. The union has stated that it opposes changes to the company list which might reduce wage survey results.

We compared the results of the DOD survey and a recent Philippine Government survey of 237 private Philippine companies. For 14 comparable key jobs, DOD survey results averaged 75 percent higher than the Philippine Government survey. Examples are shown on the following page.

APPENDIX I

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<u>Job</u>	Annual salary, Philippine Government <u>survey</u>	Annual salary, DOD <u>survey</u>	Percent DOD <u>higher</u>
Clerk	\$ 838	\$1,287	54
Laborer	587	945	61
Electrician	813	1,488	83
Security guard	794	1,676	111
Stenographer	1,076	1,720	60

NOTE: Comparability between Philippine Government and DOD survey positions was established by DOD personnel officials.

DOD officials did not consider the Philippines-wide survey representative of wage rates in the vicinity of the two major bases. We were not able to isolate those companies surveyed in the immediate bases area, but DOD survey results still averaged 73 percent higher than those for 184 firms in the highest cost area--Metro Manila.

Based on the above comparison, DOD is paying considerably more than Philippine industry for comparable positions. By expanding the wage survey to include companies paying more moderate salaries, both inside and outside the Manila area, DOD could expect more representative wage data. Despite predictable union opposition, DOD should initiate actions to amend bargaining agreement clauses that restrict flexibility in company selection.

Monetized allowances inflate base pay

Total compensation paid to Filipino employees includes base salary, a yearend bonus (125 percent of 1 month's base pay), a midyear bonus (about \$27 per employee), and a cost-of-living allowance (about \$82 annually per employee but likely to increase to \$180 after the next wage survey). Other employee benefits include eligibility for premium pay, hospitalization and death benefits, enrollment in Philippine Social Security, and entitlement to a lump-sum separation payment upon retirement, death, or reduction in force.

Wage survey teams identify all compensation paid by private employers, including base pay, cash allowances, bonuses, and payments-in-kind, such as meals, transportation, and company products. To determine base pay rates, DOD monetizes and combines payments-in-kind with private sector base pay rates, which inflates base pay and in turn inflates separation entitlements, premium rates, and bonuses calculated on

base pay rates. We were told that private industry does not compute its separation entitlements, premium pay, and bonuses on base pay plus payments-in-kind, but on base pay alone.

A sample of 1976 wage survey results showed that monetized payments-in-kind equated to about 17 percent of base pay. By separating payments-in-kind from base pay and computing separation liabilities, premium pay, and yearend bonuses on real base pay only, we estimate that a total of \$5.6 million could have been saved in fiscal year 1977.

	<u>Separation liability</u>	<u>Premium pay</u>	<u>Yearend bonus</u>	<u>Total</u>
Appropriated fund:				
Navy	\$2,560,000	\$1,070,000	\$120,000	\$3,750,000
Air Force	<u>550,000</u>	<u>50,000</u>	<u>70,000</u>	<u>670,000</u>
Total appropriated	<u>3,110,000</u>	<u>1,120,000</u>	<u>190,000</u>	<u>4,420,000</u>
Nonappropriated:				
Navy	530,000	90,000	70,000	690,000
Air Force	<u>420,000</u>	<u>20,000</u>	<u>60,000</u>	<u>500,000</u>
Total nonappropriated	<u>950,000</u>	<u>110,000</u>	<u>130,000</u>	<u>1,190,000</u>
Total	<u>\$4,060,000</u>	<u>\$1,230,000</u>	<u>\$320,000</u>	<u>\$5,610,000</u>

Navy and Air Force personnel officials agreed that payments-in-kind should be segregated from base pay. Because the Collective Bargaining Agreement requires DOD to pay wages based on surveys of prevailing practices in the private sector, we believe an appropriate change could be made unilaterally. A similar plan has been successfully implemented by U.S. Forces in Korea.

Midyear bonus paid in addition
to prevailing compensation

As an incentive to the Philippine Government for signing the 1968 Base Labor Agreement, DOD and State Department negotiators agreed to pay an annual 200 peso (about \$27) midyear bonus to each employee. Because of the extenuating circumstances concerning midyear bonuses, DOD wage specialists consider midyear bonuses payable in addition to compensation based on annual wage surveys. For example, if an employee's annual wage is determined to be \$2,000 after wage survey data has been analyzed, he then receives \$2,000 plus his midyear bonus, or \$2,027.

In line with prevailing practice criteria, the midyear bonus should be considered as part of total employee compensation. Wage survey data already includes midyear bonuses paid in the private sector (about 20 percent of surveyed employees received midyear bonuses in 1976). Using the above example, the employee should receive \$1,973 in other wages plus the \$27 midyear bonus, or \$2,000.

By considering midyear bonuses as part of total compensation, appropriated fund activities could have saved about \$370,000 in 1977 (\$290,000 by the Navy and \$80,000 by the Air Force). Another \$220,000 would be saved by nonappropriated activities.

Need to match average prevailing rate to average earnings

Presently, the average local wage determined by the DOD survey is established as step 4 of the Filipino employees' 20-grade, 7-step wage schedule. In a 1975 report on U.S. Federal blue-collar employees, GAO suggested that private sector average pay rates should be related to a point in the pay range equal to the average step of employees rather than a predetermined step. Federal white-collar wages are determined by equating average private sector rates with the average Federal rate. The Office of Management and Budget, the Civil Service Commission, and GAO reasoned that this was appropriate because private sector averages represented neither an entry rate nor a final rate, but instead, a rate earned by persons who averaged an unknown number of years' experience and an unknown number of pay increases corresponding to Federal within-grade increases. The Secretary of Defense commented on this point in a recent letter to the Chairman of the Senate Armed Services Committee endorsing Federal blue-collar wage reform in the United States. He reported:

"True comparability cannot be achieved, however, as long as there is a requirement for any fixed step as the payline rate. It can only be achieved by comparing average private industry earnings as determined by surveys to the average earnings of Federal blue-collar workers and then making adjustments in rates to bring Federal rates in line with local prevailing rates."

In our view, this should also apply to determining foreign national wages. The Filipino national work force currently averages step 5. If 1976 wage survey results

had been pegged to this average rather than step 4, about \$930,000 in appropriated funds (\$720,000 by the Navy and \$210,000 by the Air Force) would have been saved in 1977. An additional \$300,000 (\$160,000 by the Navy and \$140,000 by the Air Force) could have been saved by nonappropriated fund activities.

Key job selection should reflect
work force composition

The Defense survey in the Philippines establishes new wage rates by obtaining prevailing rates for about 100 "key jobs." Selecting key jobs that are representative of the work force is essential to determining valid prevailing wage rates.

Although the Navy employs over 75 percent of the Filipinos paid with appropriated funds, it does not periodically inventory its work force--that is, determine how many clerks, accountants, carpenters, etc., are employed. As a result, the Navy cannot determine whether survey key jobs give a valid representation of prevailing wage rates for its work force. Although the Air Force and the major nonappropriated fund employers could identify the number of employees in such positions, they had not reviewed the key job list to ensure representation.

We believe DOD would benefit by updating and revising its key job list. For example, white-collar key jobs make up over half the positions surveyed, but white-collar employees account for only one third of DOD's work force. Also, DOD's key jobs represented less than 9 percent of U.S. Embassy local employees, even though the Embassy and other U.S. civilian agencies base annual wage increases on DOD surveys.

We suggested, and officials agreed, that work force composition should be monitored and key jobs appropriately updated. In addition, key job selection should be coordinated with all U.S. Government agencies in the Philippines.

LIMITED OPPORTUNITIES TO INCREASE
U.S. CIVILIAN HIRES

Although, relative to the private sector, Filipino employees appear to be generously compensated, Filipino wage costs remain well below U.S. civilian costs. On a one-for-one basis, it is unlikely that a Filipino employee could

be cost effectively replaced by a U.S. civilian. In addition, DOD is limited in its employing of U.S. civilians in Filipino positions by a preferential employment clause in the Base Labor Agreement.

DOD employs about 1,160 U.S. civilians in the Philippines, including about 540 teachers for DOD dependents. Non-appropriated activities employ an additional 530. DOD's U.S. civilian payroll will total nearly \$23 million in fiscal year 1977, or about \$21,000 per full-time employee (excluding change-of-station costs).

About 500 of these U.S. civilians are hired locally through the DOD dependent-hire program or through overseas limited appointments. Local hires receive no change-of-station benefits, area differentials, or quarters allowance, and they are generally not eligible for civil service retirement. Even so, foreign national costs remain well below U.S. local-hire costs. We estimate that locally hired U.S. civilians cost four to five times more than Filipino employees in comparable positions.

Article I, paragraph 1, of the Base Labor Agreement provides that Filipino citizens will be used in civilian positions except when security or other special management needs require a U.S. citizen. The Collective Bargaining Agreement further defines special management needs as when duties require (1) an understanding of U.S. cultural or ethnic characteristics, (2) technical advice sensitive to policy decisions or actions on behalf of the bases, and (3) direct discipline or control of U.S. citizens involved in recreational or social activities.

The Collective Bargaining Agreement also requires that whenever a position occupied by a U.S. civilian is vacated, the position will be reevaluated to determine whether the special management needs still exist. The Filipino employees' union frequently questions U.S. civilian positions and recently requested that 100 U.S. positions be redesignated as Filipino positions.

In a July 28, 1976, letter to the Secretary of Defense (FPCD-76-79, B-182312), GAO questioned the preferential employment clause in the labor agreement on the grounds that it may violate section 106 of Public Law 92-129, approved September 28, 1971, which provides:

"* * * Unless prohibited by treaty, no person shall be discriminated against by the Department of Defense or by any officer or employee thereof in the employment of civilian personnel at any facility or installation operated by the Department of Defense in any foreign country because such person is a citizen of the United States or is a dependent of a member of the Armed Forces of the United States * * *."

DOD has argued that the agreement has the same binding effect as a treaty and therefore is exempt from the provisions of section 106. As of March 1977 no lawsuits were pending to test this interpretation.

The House Appropriations Committee has also taken issue with the preferential employment clause and believes DOD should renegotiate those agreements which provide little or no flexibility to the military service to employ the type of labor that it believes to be lowest in cost, most efficient, or necessary for the welfare of its personnel.

Local officials believe the preferential clause does not adversely affect base operation costs because Filipino costs are considerably lower than U.S. civilian costs. Moreover, DOD dependents have less need to work in the Philippines than in higher cost areas, such as Germany or Japan. Officials also believe they retain some flexibility in hiring DOD dependents. For example, we were told that the Navy and Air Force recently hired an additional 470 DOD dependents under a Summer Hire Program (paying \$1 per hour) with no strong union opposition.

CONCLUSIONS AND RECOMMENDATIONS

DOD appropriated fund activities employ nearly 14,000 foreign national employees in the Philippines with payroll costs exceeding \$31 million and a separation liability of \$18 million. The 1976 wage survey resulted in sizeable pay raises, and future raises were expected to be significant.

Although wages in the Philippines are relatively low by world standards, DOD's employees are paid considerably more than prevailing private sector rates--the criteria for compensation established in the Foreign Service Act. For example, DOD is limited by the agreement with the employees' union to surveying high paying companies.

Other questionable wage practices differ from prevailing practice, add to wage costs, and affect the validity of wage survey data. These practices are

- including monetized allowances in base pay computations,
- paying midyear bonuses in addition to total compensation based on prevailing private sector practices,
- matching average private sector wage rates to a predetermined wage schedule step, and
- selecting wage survey key jobs with limited regard to work force composition.

We recommend that the Secretary of Defense direct the military departments to:

- Initiate action to obtain control over the selection of companies surveyed.
- Separate monetized allowances from base pay, thereby reducing the basis for computing separation pay liabilities, premium pay, and yearend bonuses. (Estimated \$4.4 million savings annually to the Government plus an additional \$1.2 million for nonappropriated activities.)
- Make midyear bonuses part of, instead of an addition to, total compensation based on prevailing amounts. (Estimated \$370,000 annual savings to the Government plus \$220,000 for nonappropriated activities.)
- Apply average survey results to the Filipino average step rather than to a predetermined midpoint step. (Estimated \$930,000 annual savings plus \$300,000 for nonappropriated activities.)
- Develop and coordinate occupational inventories to ensure that survey key jobs represent the work force of DOD and U.S. civilian agencies.