

State of North Carolina

Compensation & Benefits Report

February 2007



Office of State Personnel

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COMPENSATION & BENEFITS REPORT: FEBRUARY 2007

I. EXECUTIVE SUMMARY

North Carolina remains in a situation where aggressive strides toward improving total compensation -- financial and benefits offerings -- are required in order to be competitive in the market. Annual salary increases have been small for a period of years, allowing the State to fall further behind the market. This gap was improved to some extent by a 5.5% legislative cost-of-living adjustment in 2006, but in general over the past ten years the state has lagged the overall average market movement. While some job classifications have seen benefit of staying current with labor market through such compensation mechanisms as Career-banding, others have remained behind. The State must consider all feasible options -- including incentive pay, variable pay, bonus pay programs, and proactive compensation management -- to enhance the recruitment and retention of employees across the state's many diverse occupational groups. Health care options have improved with the introduction of the new PPO program, but continue to be costly. Paid time off options can be improved, allowing a direct benefit to employees without high costs to the State. In continuing difficult financial times, we must pursue creative ways to be able to attract and maintain high performing employees. This is especially critical as the average age of the state workforce steadily increases and the need to recruit a new generation of employees becomes necessary. This next generation wants more flexibility in their total rewards package (direct compensation, benefits, and work-life programs).

Legislative support for pay innovations and funding for forward-thinking compensation studies, competency-based pay systems, improving benefits and attention to work life balance issues will clearly move North Carolina closer to its goal as an employer of choice while maintaining a commitment to cost-effective systems for managing its investment in its employees.

Recommendations made from data analysis in this report are as follows:

- In order to bring state employees' salaries closer to market rates, the report recommends a cost-of-living increase as funds will allow, preferably in line with average market movement taking into account the Consumer Price Index. The report also recommends an allocation to each agency and university to use to reward employees based on performance and competencies. This allocation differs from the traditional career-growth increase and performance bonus.
- The allowable categories for the Salary Adjustment fund should be expanded to more fully address agency needs. Language limiting use of the fund should be revised to allow agencies to respond to specific labor market issues.
- Change the State Health Plan Year from July 1 - June 30 to January 1 - December 31, so that SPA employees can better plan their out-of-pocket expenses and strategies for NC Flex contributions.
- Increase the employer's portion of the state health plan premium and allow employees to choose how it is allocated (i.e. family coverage, medical savings accounts, supplemental retirement plans, etc.) according to individual benefits needs and preferences.
- Match a portion of employees' 401(k) contributions to be more competitive with local governments and other Southeastern states (such as neighboring states South Carolina, Tennessee, and Virginia).

- Centralize coordination of supplemental benefits and consolidate supplemental benefit plan offerings in a menu approach for portability and cost savings. Allow employees to select plan products that meet their needs.
- Combine Leave Accrual categories *0-2 years of service* and *2 years of service but less than 5* into one category of *0-5 years of service*. Increase the Vacation accrual rate by 1¼ day per year; increase the Sick leave accrual rate by 3 days per year; increase the number of Holidays by one day in years where eleven are granted.
- In lieu of the above recommendations for leave accrual, implement a comparable unified Paid Time Off leave program.
- Allow development of Career-banding to continue, permitting the more progressive agencies and universities to facilitate rewarding their employees for development and assuming new duties.
- Promote and fund workforce planning and total compensation programs to recruit and retain younger workers as the “baby boomer” generation begins to age out of the state’s workforce.

II. INTRODUCTION

This Compensation & Benefits report responds to the requirements expressed in NCGS 126-7(b) [State Personnel Act] to guide the Governor and the General Assembly in making funding appropriations for State employees’ salary increases. The results of the compensation survey are presented to the Appropriations Committee of the House and Senate no later than two weeks after the convening of the legislature in odd years and May 1st of even years.

This report conveys economic and pay trends, findings and data derived from compensation and benefits surveys that the Office of State Personnel regularly analyzes to determine whether or not salary ranges for state classifications and benefits for employees are competitive in the labor market. The report summarizes key findings and comparative data showing the relationship of the state’s wages to those of competitors in both the private and public sectors. It also presents findings and survey results showing North Carolina’s rank in relation to that of other southeastern states in providing employment benefits for state employees.

North Carolina’s Pay Philosophy

The State Personnel Act, G.S. 126, states *"It is the policy of the State to compensate its employees at a level sufficient to encourage excellence of performance and to maintain the labor market competitiveness necessary to recruit and retain a competent workforce."* This statutory provision expresses the state’s philosophy in the development and administration of compensation policies, rules and practices for all employees subject to the State Personnel Act. However, it is often in direct conflict with other state laws and practices.

Total Compensation

The concept of *Total Compensation* is integral to any review or discussion of the state’s compensation system. Total compensation measures an employee’s base salary, benefits and other perquisites that the employer provides. When comparing compensation with that of other employers, whether public or private, the focus is on total compensation rather than base pay. This report includes comparisons of base pay as well as fringe benefits. It is important for employees to be knowledgeable of the value of their employment in terms of base pay, benefits, and other pay-related assets. When analyzing compensation surveys, base pay is often the common denominator in developing a comparative standard by which we can determine whether or not North Carolina state government compensation is competitive in various labor markets.

III. ECONOMIC REVIEW

Wage & Salary Trends

According to salary surveys conducted by national firms engaged in the practice of compensation planning and consultation, data collected for calendar year 2007 (budgeted) project base pay increase budgets shown in Table 1. Figures include merit, across-the-board, and cost-of-living pay increases.

Table 1 **PROJECTED & ACTUAL BASE PAY INCREASE BUDGETS**

| <u>National Firm</u> | <u>2004 Actual</u> | <u>2005 Actual</u> | <u>2006 Actual</u> | <u>2007 Projected</u> |
|----------------------|--------------------|--------------------|--------------------|-----------------------|
| William Mercer | 3.3% | 3.6% | 3.7% | 3.7% |

Note: The above are projected and actual base pay salary increase percentages of payroll.

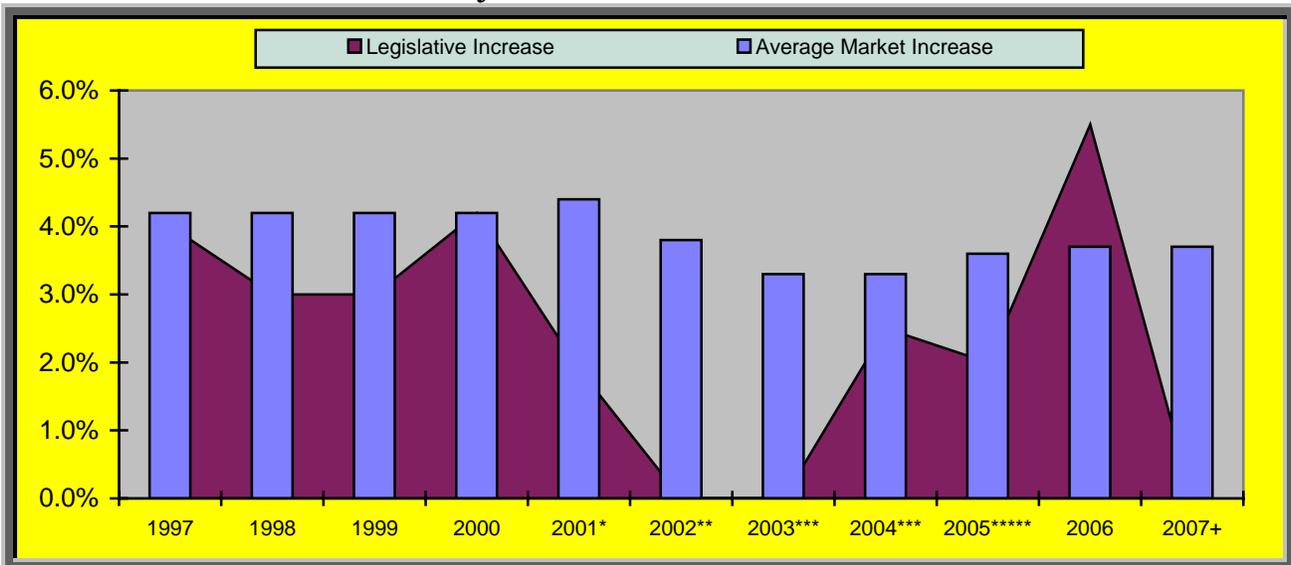
Source: Mercer Human Resources Consulting 2006/2007 US Compensation Planning Survey

Projected and actual wage increases have remained fairly stable at the national level for the best part of the past decade at or about the 4% percent level. Even with improving economic conditions, actual wage increases remained under 4% in 2006. A study conducted by Mercer Human Resources Consulting, *2006/2007 US Compensation Planning Survey*, revealed that during the calendar year 2006, pay increase budgets rose slightly over 2005 to 3.7% overall. For organizations classifying their industry as *Government*, the average 2006 expected increase was 2.9%, but was expected to increase slightly in 2007 to 3.3%.

Analysis of data from a variety of national consulting and business firms places the projected budgeted average wage increase for 2006 at 3.7%. Projections for calendar year 2007 likewise indicate 3.7% increases for Technical/Professional occupations and 3.6% for Nonexempt Clerical/Technical jobs.

In North Carolina, annual salary increases for state employees were less than average market movement in all of the last 5 years, until 2006, as displayed in the chart below. Even when factoring in the 5.5% legislative increase in 2006, salary increases in state government have cumulatively trailed average market increases by 7.7% over the past five years.

NC LEGISLATIVE INCREASES COMPARED TO ACTUAL AVERAGE MARKET MOVEMENT 1997- 2006 AND PROJECTED AVERAGE MARKET MOVEMENT FOR 2007



Source: William Mercer, Incorporated

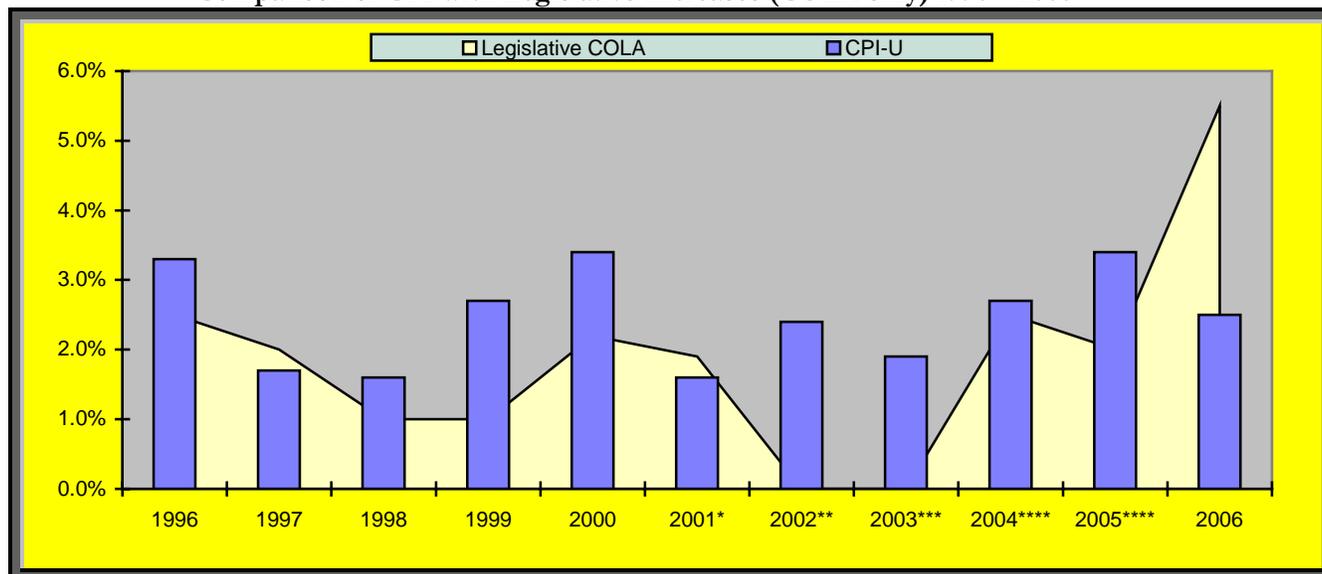
- *1.9% increase is based on a \$625 across the board payment divided by the 2001 average salary.
- **Ten days bonus leave granted in lieu of wage increase during 2002.
- ***Ten days bonus leave plus \$550 non-base building bonus granted in lieu of permanent wage increase during 2003.
- ****2.5% for employees with salaries over \$40K; \$1000 increase for employees with salaries below \$40K during 2004.
- *****The greater of \$850 or 2% for 2005, plus 5 days bonus leave.
- + 2007 percentage is a market increase projection

Consumer Price and Employment Cost Indices

In addition to general labor market movement, the increase in the Consumer Price Index-Urban (CPI-U) for the 12-month period ending in December 2006 was 2.5%. This percentage measures the average change over a specific period of time in the prices paid by urban consumers for goods and services. The CPI-U includes all urban consumers that are roughly 87% of the population in the United States. Since most pay increases for state employees have included a cost-of-living component, the following chart compares the Consumer Price Index-Urban for the years indicated with the percent increase for the cost-of-living portion of legislative increases for the same period. All rates are as of December 31 of the year. [A history of legislative increases for the period 1992-2006 has been included in the Appendix of this report.]

The graphed data below indicate that the cost-of-living portion of annual legislative increases from 1996 to 2006 trails the CPI-U percentages for the same time period, with the obvious exception of 2006. This differential reflects that compensation for state employees has historically not kept pace with the consumer price index. Cumulatively, over the past five years, the CPI-U has increased 12.9% while N.C. state employee pay has increased 10.0%, effectively creating a -2.9% gap in employee “buying power.”

Comparison of CPI with Legislative Increases (COLA only) 1996 – 2006



Source: US Department of Labor/Bureau of Labor Statistics & NC Office of State Personnel

- *1.9% increase is based on a \$625 across the board divided by the 2001 average salary.
- **Ten days bonus vacation granted in lieu of base pay increase during 2002.
- *** Ten days bonus vacation, plus \$550 one-time bonus, granted in lieu of base pay increase for 2003.
- ****2.5% for employees with salaries over \$40K; \$1000 increase for employees with salaries below \$40K during 2004.
- *****The greater of \$850 or 2% for 2005, plus 5 days bonus vacation.

IV. COMPENSATION TRENDS

A recovering economy, growing job market, and aging workforce are challenging organizations to focus once again on attracting and retaining key talent. Attraction and retention of top talent will become more important as labor markets become more competitive. Job families continuing to earn attention include Health Care, Information Technology, Accounting & Finance and Engineering.

One way to strengthen the state’s compensation program is to incorporate occupation-specific pay programs, pay incentive programs and similar innovations to provide the state necessary tools to compete in an increasingly tight labor market for critical skills.

Table 2 outlines a number of compensation options that are becoming more prevalent among private and public sector organizations. With few exceptions, usage has increased slightly or remained the same over the past two years. Signing bonuses are paid to certain hard-to-hire positions as an incentive to accept a position. More aggressive pay increases are aimed at employees whose skills are critical and retaining them is crucial. Project milestone awards are provided at key interim completion points of a project. Spot cash awards are given to reward a specific project or piece of work successfully completed.

Table 2 **ATTRACTING AND MAINTAINING EMPLOYEES**

| Functional Area | Signing Bonuses | More Aggressive Pay Increases | Project Milestone Awards | Spot Cash Awards |
|------------------------|-----------------|-------------------------------|--------------------------|------------------|
| Information Technology | 67% | 43% | 77% | 85% |
| Engineering | 40% | 28% | 34% | 56% |
| Accounting & Finance | 52% | 25% | 31% | 78% |
| Customer Service | 21% | 5% | 21% | 69% |
| Human Resources | 32% | 7% | 22% | 73% |
| Internal Auditors | 31% | 12% | 19% | 58% |
| Security | 16% | 7% | 12% | 46% |

Source: William M. Mercer 2006/2007 US Compensation Planning Survey

Currently, the State Personnel Act prohibits such modern-day pay programs as monetary incentive awards. Pay increases are determined by the Legislature. Organizations continue to look to variable pay as they struggle to afford and sustain compensation levels. Additional flexibility in this area will help the state to remain competitive. One innovative idea would be to allow agencies to design bonus pay systems that utilize their lapsed salary funds. However, this would require legislative approval and the support of the employee unions.

Recruitment & Retention

Many factors affect the capacity of an organization to recruit and retain a competent and qualified workforce. Given the occupational diversity of North Carolina's state government, managers and employees alike face substantial challenges in recruitment and retention. Principle concerns include citizens’ expectations that state government will protect their health and safety; provide affordable and accessible education; maintain the quality and integrity of the state’s environment; offer diverse programs and services for cultural enrichment; and ensure a viable, safe infrastructure and transportation system. The state must meet these expectations and comply with legislative mandates for services to citizens.

A key challenge to the state and employers in general is that the “baby boomer” generation is beginning to age out of the workforce. It is anticipated that in the next ten to twenty years this will mean a loss of organizational knowledge as senior employees leave the workforce at an accelerated pace. An analysis of this anticipated trend is included in the “Turnover Rates” section of this report, starting on page 13.

Compensation and benefits are obviously key factors in the recruitment and retention of employees for any organization. In North Carolina, pay for state employees has not kept pace for a number of years with

various indices that measure cost-of-living and market movement. Also, North Carolina is significantly behind private and public industry by not offering a match in the State's 401(k) program.

In a report from the Society of Human Resources Management (SHRM), two North Carolina metropolitan areas are in the top 20 for highest projected job growth in the decade from 2003 to 2013 (Raleigh-Durham and Charlotte at numbers 9 and 12, respectively), thus competition for qualified employees will grow. A joint SHRM/CNNfn (Cable News Network-Financial Network) Job Benefits Survey Report indicates the top five benefits most important to overall employee job satisfaction are health care/medical benefits, paid time off, retirement benefits (e.g., defined contribution plans and defined benefit plans, such as 401(k)), dental insurance and a prescription drug plan.

As one example, medical and allied health occupations continue to present particular recruitment and retention concerns. A national shortage of nursing professionals since 1999 has exacerbated the state's chronic difficulty in recruiting and retaining these direct care professionals in the state's psychiatric and prison hospitals, student health services, and similar clinical settings. As reported in past reviews, there are a limited number of psychiatric nurses, as it is a specialized field and many nurses elect to work in other nursing fields. Finally, the mental health reform movement in North Carolina has prompted recommendations to close or consolidate the state's existing psychiatric hospitals. This will likely further diminish the already too few number of nurses who might be interested in employment with the State.

V. BASE PAY - LABOR MARKET DATA

Methodology

Public and private sector organizations rely upon salary surveys to ensure that they are making informed decisions about employee compensation in terms of cost-effectiveness, recruitment and retention. Sound compensation practices ultimately result in a workforce comprised of competent, skilled employees across multiple occupational areas. Their collective knowledge, skills and competencies directly relate to the accomplishment of the organization's mission and vision. Salary surveys are therefore critical in pricing jobs, diagnosing compensation problems, determining wage parity with market competitors, and in monitoring internal pay equity. Survey data is also essential to organizations in terms of analyzing pay trends, identifying effective pay practices, and establishing a systematic method for setting competitive pay ranges for job classes. This report on North Carolina's compensation practices conforms to these purposes for conducting salary and benefits surveys.

The methodology for analyzing data and identifying pay trends is equally important. The information presented in this report derives from multiple national and local surveys, and it reflects benchmark classes that were deliberately selected to represent each of the twelve occupational groups in the state's pay plan. The survey sample included 52 benchmark classes that represent nearly 24% of all employees subject to the State Personnel Act. After identifying the benchmark classes, appropriate labor markets were determined.

Current turnover and vacancy rate data for each class are included in the report.

Market data was collected from the following published sources:

- **William Mercer Human Resource Consulting – 2006/2007 US Compensation Planning Survey – A Study of Pay Increases, Incentive Compensation, and Emerging Practices.** Nearly 1,350 organizations provided data for the 2006/2007 US Compensation Planning Survey, representing pay practices of close to 13 million workers. Data representing similar jobs in government, as well as local private industry, were used in comparisons to the State of North Carolina.

- **Watson Wyatt 2006/2007 Survey Report on Hospital and Healthcare Professionals, Nursing and Allied Services Personnel Compensation.** A comprehensive document with data from 1,301 organizations reporting on 756,761 incumbents in hundreds of positions.
- **Watson Wyatt 2006/2007 Survey Report on Hospital and Healthcare Management Compensation.** A survey of 936 organizations reporting data on 70,107 incumbents in hospital positions other than nursing and allied services.
- **Watson Wyatt 2006/2007 Survey Report on Engineering, Design & Drafting Personnel Compensation.** A survey based on data from 926 organizations with 99,423 incumbents.
- **Watson Wyatt ECS survey of Professional and Scientific Personnel** – A computer based survey of salaries in geographic areas for professional and scientific personnel.
- **Watson Wyatt 2006/2007 Report on Employee Benefits.** Survey results regarding a wide range of benefits from 596 organizations responsible for 4.2 million employees.
- **CompBase USA** – Data compiled from 369 companies compiling data on over 500 non-exempt and exempt jobs in the Administrative, Human Resources, Marketing/Sales, Accounting/Finance, Purchasing/Materials, Information Technology, Maintenance/Facilities, Production/Assembly/Fabrication and Technical Support Fields.
- **Capital Associated Industries – 2006 North Carolina Wage & Salary Survey** – Wage and salary information from designated areas in North Carolina, with pacesetter organizations (600 or more employees) in an area including Wake, Durham, Orange and Alamance counties. Survey provides area-to-area compensation rates.
- **League of Municipalities Survey** - A compilation of salary data for specific municipal jobs located throughout the state.
- **MAPS Group for the Institute of Government – County Salaries in North Carolina – 2006 - Salaries** and wage profiles by position and information about fringe benefits offered by North Carolina counties.
- **2006 Hay Benefits Report** – An analysis of benefits, perquisites and personnel policies for exempt employees in 760 industrial, financial and service organizations throughout the United States. Provides major findings and trends.
- **World at Work - Salary Budget Survey** – 3,272 member responses to a survey presented in both industry and sub-industry and regional categories identifying trends, structures and average salaries broken out in FLSA employment categories (non-exempt hourly non-union, non-exempt salaried, exempt salaried and officers/executives).
- **Southeastern Salary Conference, 2000 to 2006;** salary and benefits information gathered from surveys from fourteen southeastern states (Alabama, Arkansas, Florida, Georgia, Kentucky, Louisiana, Mississippi, Missouri, North Carolina, Oklahoma, South Carolina, Tennessee, Virginia and West Virginia.)

- **Society of Human Resource Management (SHRM) 2006 Workplace Forecast – A Strategic Outlook** – Information based on a survey of human resource professionals and their views on the key issues in demographics, employment, international affairs, politics, society and science and technology that will have the greatest impact on the workplace in the next decade.
- **National Association of Colleges and Employers Salary Survey** – NACE compiles data from career planning and placement offices of colleges and universities across the US. This report consists of starting salary offers made to new graduates by employing organizations in business, industry, and government and by nonprofit and educational institutes.
- **Compdata Surveys – Compensation Data 2006 – Carolinas – Pay and Benefits Survey Results** – survey analysis, pay practices and benefit practices for 223 companies in North and South Carolina, covering 491 jobs in both states.

Professional survey methodology standards were used to collect and analyze available salary survey data or to conduct surveys to gather pertinent market information. Survey methodology recognizes the following concepts that have been defined for informational purposes:

- *Labor Market Rate* is the average rate of pay that competitors have reported through surveying in a classification similar to that found in state government.
- *Labor Market Pay Gap* is the relationship expressed in percentage terms between the state's average salary for a benchmark class and the average wage reported for a relevant labor market for that class.
- *Turnover Rate* is a percentage reflecting all separations from employment for both voluntary and involuntary reasons compared to the total number of employees over a span of 1 year.
- *Vacancy Rate* is the percent of positions by classification that are vacant among the total number of positions covered by the State Personnel Act for any specific period of time.

Market Analysis

Average Salary Overall Comparison

For 2006, an analysis of salary survey data for the benchmark classes indicates state employees' salaries overall trail their equivalent labor market by 1.94%. Table 3 on the next page shows the average annual salary comparison between North Carolina's benchmark class titles and the overall market averages for the past four years. The percent difference should not be directly compared year-to-year because the classes sampled and the total number of classes for each year is different. Each year should be viewed as a single snapshot. It is interesting to note, however, that between 2005 and 2006 the composite pay gap was decreased by approximately 5.76% -- likely due in large part to the 5.5% across-the-board legislative increase. Further, over 100 classes were presented to and approved by the State Personnel Commission for classification and pay actions, in addition to the ongoing maintenance of Special Minimum Rates and updating of market rates for Career-banded classes.

Table 3

OVERALL MARKET COMPARISON

| Year of Report | North Carolina Pay | Market Pay | % NC Trails Market |
|----------------|--------------------|------------|--------------------|
| 2007 | 45,597* | 46,483** | -1.94% |
| 2006 | 43,215* | 46,543** | - 7.70 % |
| 2005 | 41,787* | 46,035** | -10.2 % |
| 2004 | 41,431* | 46,119** | -11.3 % |

*Average annual salary for NC Benchmark classes only

**Composite market average for NC Benchmark survey comparisons

Survey Findings for Selected Benchmark Classes

Market data collected for the fifty-two (52) benchmark classes in this report were analyzed by staff in the Office of State Personnel and indicate that the average wage for 20 of the 52 classes trailed the market by at least 5% and 11 of the 52 trailed by at least 10% (compared to 34 of 50 and 21 of 50, respectively, in 2005). Table 4 lists selected classes that trail the market as shown under "Labor Market Pay Gap". Data indicating turnover and vacancy rates for the period ending June 30, 2006 also have been included to give a more complete view of potential recruitment and retention issues for these classes. It is evident from the data that North Carolina is at a competitive market disadvantage when attracting qualified candidates and retaining skilled employees in many of the benchmark classes. The apparent pay disparity is likely a prominent factor where high turnover and vacancy rates are shown and presents concerns for remaining competitive. See the Market Data Appendix for a complete list of benchmark classes surveyed including turnover and vacancy rates.

Table 4

SELECTED BENCHMARK CLASSES

| Class Title | NC Average | Market Rate | Market Pay Gap | Turnover Rate | Vacancy Rate |
|--|------------|-------------|----------------|---------------|--------------|
| Electrician II | 34,117 | 40,583 | -18.95% | 8.93% | 5.76% |
| Security Guard | 23,828 | 28,245 | -18.54% | 13.51% | 16.36% |
| Internal Auditor II | 56,770 | 59,047 | -4.01% | 13.95% | 17.54% |
| Executive Assistant | 39,065 | 42,901 | -9.82% | 10.15% | 8.63% |
| Business Technology Applications Analyst | 61,476 | 69,008 | -12.25% | 6.5% | 19.62% |
| Staff Nurse | 45,835 | 49,108 | -7.14% | 28.00% | 20.51% |
| Occupational Therapist I | 55,409 | 54,639 | +1.39% | 18.42% | 30.00% |
| Social Worker II (BSW) | 36,833 | 37,861 | -2.79% | 25.00% | 20.69% |

Note: The State's average turnover rate for all occupations in fiscal year 2005-2006 was **10.8%**

Local and State Government average total turnover rate for all occupations in fiscal year 2005-2006 was **15.8%**

Private Industry's average total turnover rate for all occupations in fiscal year 2005-2006 was **44.9%**

Source: US Department of Labor, Bureau of Labor Statistics 2006, PMIS

Comparison to Southeastern States

Table 5 on the next page shows average salaries for classified employees in North Carolina as compared with other states in the Southeast region over the past four years. As illustrated here, North Carolina's average salary has led other SE States in recent years.

Table 5 **COMPARISON TO SE STATES (CLASSIFIED EMPLOYEES ONLY)**

| | 2003 | 2004 | 2005 | 2006 |
|---------------|--------|--------|--------|--------|
| All SE States | 30,847 | 32,943 | 33,463 | 34,916 |

| | | | | |
|-----------------|--------|--------|--------|--------|
| North Carolina | 33,529 | 34,792 | 35,203 | 38,256 |
| NC Differential | +8.7% | +5.6% | +5.2% | +9.6% |

Comparison to Contiguous States

NC Average Pay Comparison to Contiguous States: A more relevant comparison may be North Carolina to her border states. A pay history comparison with three neighboring states reveals that North Carolina has generally led South Carolina and Tennessee in pay, stayed relatively even with Georgia, and trailed Virginia (see Tables 6-9 below).

Table 6 **COMPARISON TO GEORGIA (CLASSIFIED EMPLOYEES ONLY)**

| | 2003 | 2004 | 2005 | 2006 |
|-----------------|--------|--------|--------|--------|
| Georgia | 32,744 | 35,728 | 36,560 | 37,295 |
| North Carolina | 33,453 | 34,792 | 35,203 | 38,256 |
| NC Differential | +2.2% | -2.6% | -3.7% | +2.6% |

Table 7 **COMPARISON TO SOUTH CAROLINA (CLASSIFIED EMPLOYEES ONLY)**

| | 2003 | 2004 | 2005 | 2006 |
|-----------------|--------|------|--------|--------|
| South Carolina | 31,191 | N/A | 33,907 | 34,416 |
| North Carolina | 33,453 | | 35,203 | 38,256 |
| NC Differential | +7.3% | | +3.8% | +11.9% |

Table 8 **COMPARISON TO TENNESSEE (CLASSIFIED EMPLOYEES ONLY)**

| | 2003 | 2004 | 2005 | 2006 |
|-----------------|--------|--------|--------|--------|
| Tennessee | 28,686 | 30,994 | 32,212 | 34,429 |
| North Carolina | 33,453 | 34,792 | 35,203 | 38,256 |
| NC Differential | +16.6% | +12.3% | +9.3% | +11.1% |

Table 9 **COMPARISON TO VIRGINIA (CLASSIFIED EMPLOYEES ONLY)**

| | 2003 | 2004 | 2005 | 2006 |
|-----------------|--------|--------|--------|--------|
| Virginia | 35,425 | 36,386 | 37,822 | 39,622 |
| North Carolina | 33,453 | 34,792 | 35,203 | 38,256 |
| NC Differential | -5.6% | -4.4% | -6.9% | -3.4% |

Source, Tables 5-9: Southeastern Salary Conference - 2006

Comparison of NC Base Pay Increases to Local Municipalities

The State must compete for qualified candidates to fill vacant positions with private firms and other local government jurisdictions. In some recent years, the state has not provided base pay increases while many counties throughout the State have. In the most recent Fiscal Year, however, 87 NC counties provided cost of living increases with an average increase amount of 2.4%, while the state provided 5.5%. (Source County Survey 2006 (MAPS Group))

Table 10 below offers examples of a few classifications of interest that the state has in common with local municipalities. As illustrated here, the state is competitive in certain areas while lagging in others.

Table 10

**COMPARISON OF LOCAL MUNICIPALITIES
(POPULATIONS OF 10,000 AND ABOVE)**

| NC Class Title | Municipalities Average Pay | North Carolina Average Pay | NC Pay Differential |
|-------------------------|----------------------------|----------------------------|---------------------|
| Public Safety Officer | 35,798 | 34,322 | -4.1% |
| Maintenance Mechanic IV | 33,374 | 35,406 | +6.1% |
| Housekeeper | 22,538 | 22,155 | -1.7% |
| Office Assistant IV | 32,377 | 29,576 | -8.7% |
| GIS Technician | 41,296 | 35,627 | -13.7% |
| Attorney III | 86,970 | 83,132 | -4.4% |

Source: League of Municipalities Survey 2006, PMIS

Comparison of Pay Increases of State Employees and NC Teachers

The General Assembly grants legislative increases to teachers, as well as regular state employees. Table 11 illustrates a comparison of teacher pay increases to state employees. State employees have received smaller increases than teachers in seven of the eight years. Cumulatively, across-the-board teacher pay increases have outpaced state employee pay increases by 14.15% since 1999. Additionally, teachers receive automatic annual step increases and, in certain counties, additional localized pay supplements.

COMPARISON OF TEACHERS TO STATE EMPLOYEES INCREASES

Table 11

| Years | Teacher's Increase | State Employee's Increase | NC Average Teacher Pay | US Average Teacher Pay |
|----------------------|--------------------|---------------------------|------------------------|------------------------|
| 2006 - 2007 | 8.0% (average) | 5.5% | Not yet published | Not yet published |
| 2005 - 2006 | 2.24% | 2.0% or \$850 | Not yet published | Not yet published |
| 2004 - 2005 | 2.5% (average) | 2.5% or \$1,000 | 43,348 | 47,750 |
| 2003 - 2004 | 1.81% | \$550 bonus (Leave) | 43,211 | 46,752 |
| 2002 - 2003 | 1.84% | 0 (Leave) | 43,076 | 45,776 |
| 2001 - 2002 | 2.86% | 1.9% (Average on \$625) | 42,680 | 44,660 |
| 2000 - 2001 | 6.5% | 4.2% & \$500 bonus | 42,959 | 43,395 |
| 1999 - 2000 | 7.5% | 3% & \$125 bonus | Unavailable | Unavailable |
| Total Base Increases | 33.25% | 19.1% | N/A | N/A |

Sources: Legislative Report Page, Public Schools of North Carolina and Annual Approved Budget Act

COMPARISON OF TEACHER PAY TO NATIONAL AVERAGE

Table 12

| Years | NC Average Teacher Pay | US Average Teacher Pay | NC differential | Teacher's Increase |
|-----------|------------------------|------------------------|-----------------|--------------------|
| 2006-2007 | Unavailable | Unavailable | N/A | 8.0% |

| | | | | |
|-----------|-------------|-------------|-------|-----------|
| | | | | (average) |
| 2005-2006 | Unavailable | Unavailable | N/A | 2.24% |
| 2004-2005 | 43,348 | 47,750 | -9.2% | 2.5% |
| | | | | (average) |
| 2003-2004 | 43,211 | 46,752 | -7.6% | 1.81% |
| 2002-2003 | 43,076 | 45,776 | -5.9% | 1.84% |
| 2001-2002 | 42,680 | 44,660 | -4.4% | 2.86% |
| 2000-2001 | 42,959 | 43,395 | -1.0% | 6.5% |
| 1999-2000 | Unavailable | Unavailable | N/A | 7.5% |

Sources: National Center for Education Statistics Digest of Education Statistics, NC Department of Public Instruction Facts & Figures

New Graduates Starting Pay Analysis

The State must compete with private companies and local governments for qualified candidates to fill vacancies. One measure of the State's ability to compete in the labor market is the ability to offer competitive starting salaries for college graduates that are being recruited and hired by competitors. In 2005, the National Association of Colleges and Employers Salary Survey (NACE) showed that employers reported plans to increase college hiring by 13% over 2003-04 levels. They reported a continuing positive trend in starting salaries. Of the 62 disciplines that reported a percentage change in salary offers, 53 reported an increase.

Table 13 provides information on the reported average starting pay offers made to graduating students in seven functional areas of interest. North Carolina's class title and minimum pay is compared. An analysis confirms that the State's overall salaries trail most of their equivalent labor markets on average, by as much as 23.7%, as illustrated in Table 13.

Table 13 **NEW GRADUATE'S STARTING PAY ANALYSIS**

| NC Class Title | NACE Starting Salary | NC Hiring Rate | Entry Pay Gap |
|---|----------------------|----------------|---------------|
| Accountant I, Trainee | 43,269 | 35,179 | -18.7 % |
| Personnel Analyst I, Trainee | 36,967 | 28,192 | -23.7 % |
| Applications Programmer I | 46,189 | 37,943 | -17.9 % |
| Registered Nurse | 40,751 | 41,101 | 0.9% |
| SBI Agent, Trainee | 32,275 | 31,006 | -4.0 % |
| Human Services Coordinator I, Trainee | 28,491 | 23,887 | -16.2 % |
| Information & Communications Specialist I | 31,303 | 27,412 | -12.4 % |

Source: National Association of Colleges and Employers 2005 (NOTE: 2006 data was unavailable)

Additional Analysis

Turnover Rates and Cost

Turnover rates vary among industries, organizations, geographic locations, departments, occupations, and by employee characteristics such as age, education, and organizational tenure. For example, younger, newer, unskilled, and blue-collar employees tend to have higher turnover rates than their contrasting groups. For this reason, turnover should be calculated for various categories of interest, as well as for the organization as a whole. For example, an organization may not have a severe organization-wide turnover rate, but may have a severe departmental turnover rate or a high professional employee turnover rate, which requires appropriate action to alleviate. Source: Society for Human Resources Management (SHRM)

The cost of turnover is difficult to measure but is very important for organizations to understand. The cost to an organization for each position turnover has been estimated by the experts at anywhere from 50% to 250% of the departing employee's annual salary depending on the type of position being filled and the performance level of the departing employee. There are many factors included in estimating the cost of turnover. Some obvious costs include advertising the vacancy, the cost in salaries of employment screening panels, and manager's time spent interviewing candidates. Other costs are not so easily quantified such as lost productivity or lost knowledge from the organization. Other costs include required training and higher rates of mistakes made by new hires. Though the costs may be hard to quantify, they are considerable and should be monitored.

Turnover is a measure of employee separations from an agency or university most often expressed as turnover rate. Two types of turnover are tracked: Total Turnover and Voluntary Turnover. Total turnover includes all separations for any reason. The total turnover rate is calculated by dividing the number of separations by the total number of employees at the beginning of a fiscal year. Voluntary turnover includes separations for reasons that the employee has control of such as resigning to take a job with another employer. Voluntary turnover rate is calculated by dividing the number of voluntary separations by the total number of employees at the beginning of the fiscal year.

Table 14 **FIVE YEARS OF TURNOVER RATES – STATE OF NORTH CAROLINA**

| | FY 2001-2002 | FY 2002-2003 | FY 2003-2004 | FY 2004-2005 | FY 2005-2006 |
|-----------------|--------------|--------------|--------------|--------------|--------------|
| Voluntary T/O | 6.8% | 6.8% | 6.9% | 7.4% | 7.3% |
| Retirement T/O | 2.5% | 2.8% | 2.7% | 2.9% | 2.5% |
| Involuntary T/O | 1.2% | 1.1% | 1.0% | 0.9% | 1.0% |
| Total T/O | 10.5% | 10.7% | 10.6% | 11.2% | 10.8% |

Source: PMIS; SPA Permanent Full-Time employees only

The above figures are graphed below to better illustrate ratios of different types of turnover:

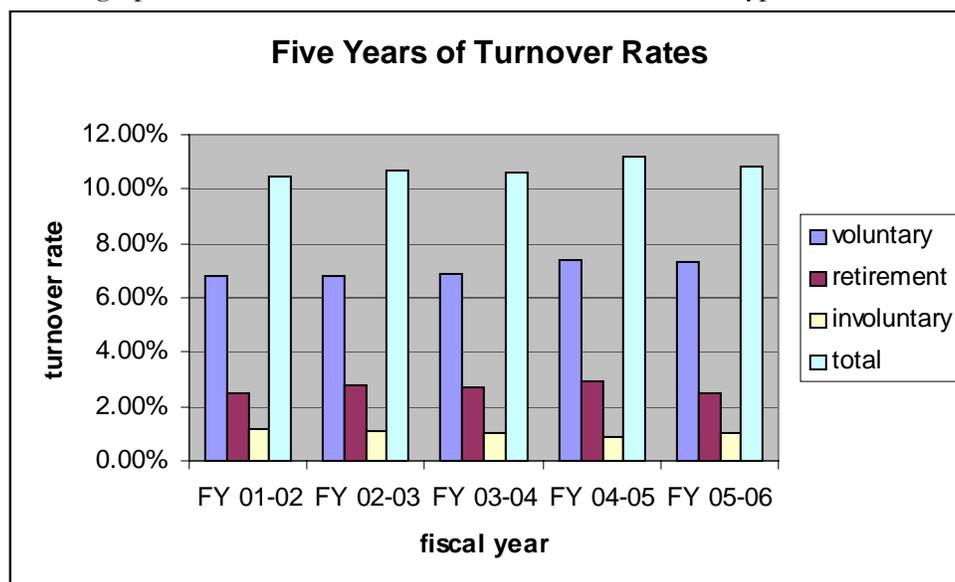


Table 15 **FOUR YEARS OF TURNOVER RATES – STATE AND LOCAL GOVERNMENT**

| | 2002-2003 | 2003-2004 | 2004-2005 | 2005-2006 |
|---------------|-----------|-----------|-----------|-----------|
| Voluntary T/O | 7.0% | 6.9% | 7.2% | 8.2% |
| Total T/O | 14.6% | 14.7% | 14.7% | 14.5% |

Source: US Department of Labor, Bureau of Labor Statistics 2006

Table 16 **FOUR YEARS OF TURNOVER RATES – PRIVATE INDUSTRY**

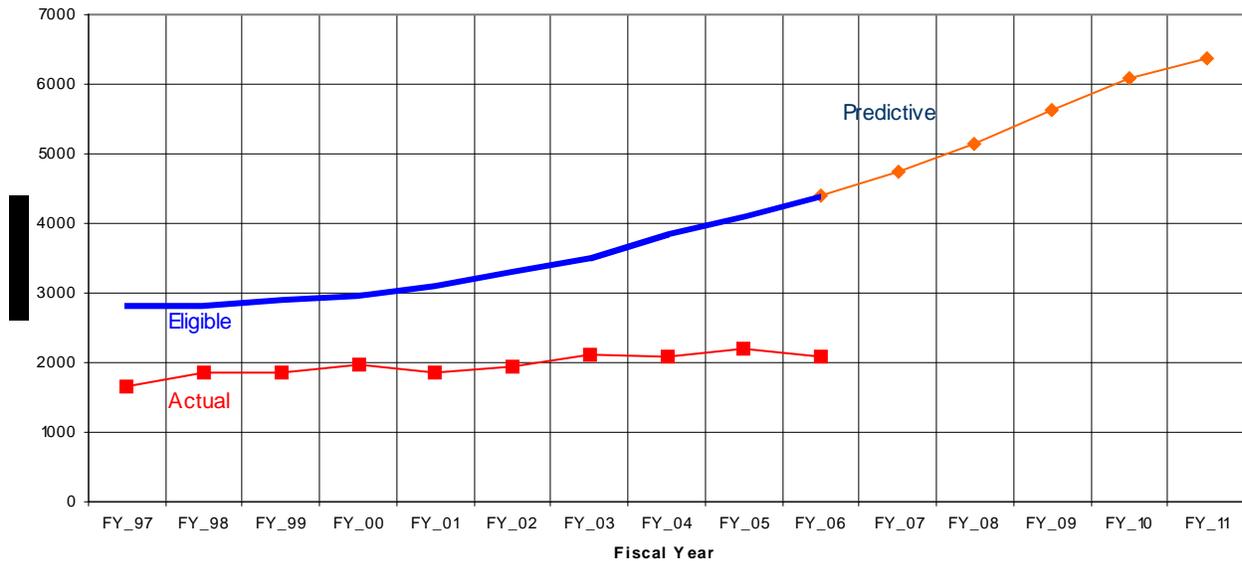
| | 2002-2003 | 2003-2004 | 2004-2005 | 2005-2006 |
|---------------|-----------|-----------|-----------|-----------|
| Voluntary T/O | 22.3% | 22.3% | 24.9% | 26.5% |
| Total T/O | 41.0% | 40.9% | 44.3% | 44.9% |

Source: US Department of Labor, Bureau of Labor Statistics 2006

In FY 2005-2006, the State had a 10.8% turnover rate. Using a conservative 100% cost of turnover, the cost to the state would be approximately \$362 million. Because the cost of replacing workers is so high, we believe this underscores the need to closely monitor turnover, keep salaries reasonably competitive, and maintain a positive work environment. Uncompetitive salaries and poor working conditions can only exacerbate the turnover rate and increase turnover costs.

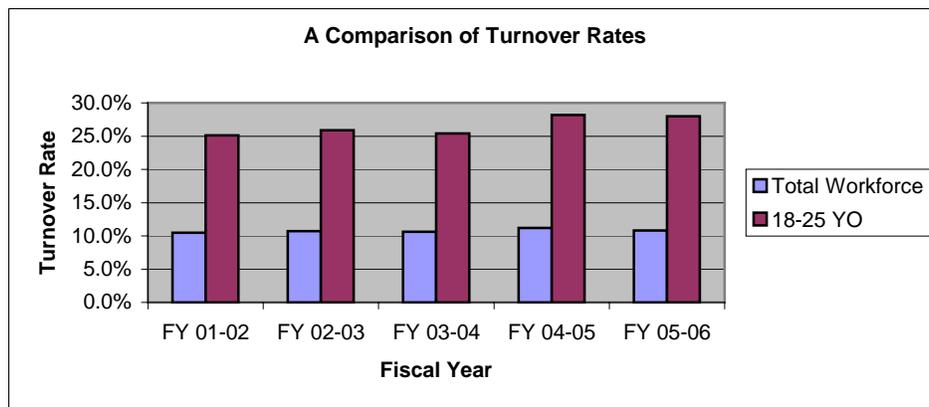
While the retirement rate has remained relatively steady in recent years, it is widely recognized that the “baby boomer” generation will be leaving the workforce at a more accelerated rate in the next 3 to 10 years. This impending workforce crisis is suggested by an analysis of the current state workforce’s retirement trends over the past ten years and projected into the future over the next five years. The graph below shows that the number of retirement-eligible employees has increased steadily in recent years, while the number of actual retirements has increased slightly. It further suggests that the predicted number of retirement-eligible employees will continue to increase dramatically:

Eligible*, Predictive and Actual Retirement Since FY97
 (*Eligible retirees would have full benefits)

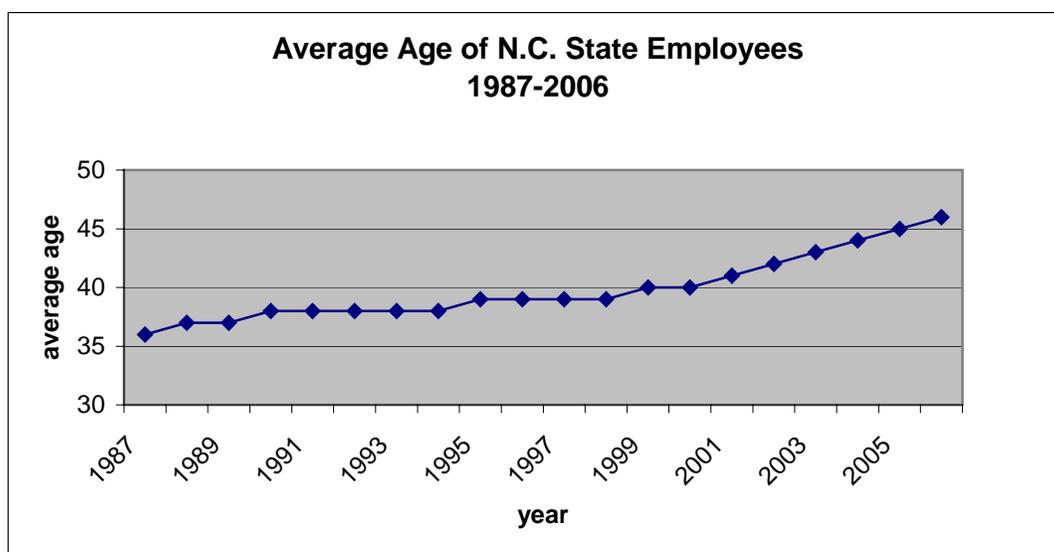


Source: PMIS; predictive model by Office of State Personnel

The above is considered especially critical in light of the fact that the state consistently has trouble retaining younger employees entering the workforce. This is suggested by the below comparison of turnover rates of 18-25 year old workers vs. the overall turnover rates for state government over the past five years (source: PMIS):



Meanwhile, the average age of N.C. state employees has steadily increased over the past two decades, further illustrating the impending aging workforce issues.



source: PMIS

Use of Salary Adjustment Funding

One valuable tool that helps keep salaries competitive is the Salary Adjustment Fund. The Salary Adjustment Fund is used to increase salaries in occupational fields, such as those listed in Table 4, where some salaries are significantly below the market. The primary funding mechanism, transferring legislative increase funds remaining after employees receive their legislative increase, continues to be inadequate to address occupational areas where salaries are below the market. Last year, \$18.6 million was allocated to the Salary Adjustment Fund for agency requests totaling \$19.0 million. Their total needs are considerably higher. This problem will get worse as projected retirements will create significant vacancies in many occupational areas in the State's workforce, including those that are critical to the delivery of services to citizens. As a result, many agencies will be facing extreme difficulty in filling critical vacancies without sufficient funds to maintain competitive recruitment.

Another significant problem with the Salary Adjustment Fund is limitations on its use. Currently, the Fund can only be used for range revisions and reallocations. Other employee salary increase types are used by agencies to increase employee salaries in response to labor market difficulties but are not allowed with the current restrictive language.

VI. BASE PAY AND SALARY ADJUSTMENT FUND RECOMMENDATIONS

Recommendations

- **Base Pay Increase:**

In order to help bring state employees' salaries to market rates, a cost-of-living increase as funds will allow – consistent with average market movement and the consumer price index -- and an allocation to each agency and university to use to reward employees based on competencies and performance is recommended. This allocation differs from the recent legislative increases that provided the same increase for all employees, regardless of performance or competency level. Identical increases for all employees tend to overcompensate poor performers and under compensate high performers, the very employees that the State can ill afford to lose to its competitors.

- **Salary Adjustment Fund:**

It is important to increase funding for the Salary Adjustment Fund using a realistic projection of actual needs rather than relying on funds remaining from the Legislative Increase. With market movement averaging around 3.7% per year and with certain job classifications already considered to be behind the market, it is recommended that the legislature request the Office of State Personnel provide market-based data to support additional funding for the Salary Adjustment Fund each year.

It is also recommended that restrictive language be removed from the Base Budget Act that directs specific transactions that can be funded from the Salary Adjustment fund so that agencies can focus the money on their most critical needs that sometimes do not fit the restrictive Legislative language.

- **Additional Compensation Programs:**

Expand the number of compensation programs available to State workers, such as Employee & Team Incentive Pay, in order to match the variety of offerings by many of our competitors.

VII. FRINGE BENEFITS

In 1992, the Government Performance Audit Commission [GPAC] recommended that . . .

...the State should offer full, flexible, and portable benefits; determine the most appropriate contribution method; and determine a contribution philosophy for each covered group. The State's employee benefits programs are fragmented and not cost-effective.

In a survey conducted by Watson Wyatt Data Services of 644 organizations that provided benefits information on over 5 million employees, growth in benefit costs continues to outpace wage and salary growth. After adjusting for inflation, overall benefit expenses are growing three times faster than compensation. Medical benefits costs average 46% of the total benefits expenditure costs for employers. Employers continue to shift a portion of the cost of medical benefits to employees. Increasing employee contributions as a cost saving measure was being planned by over half (62.5%) of the surveyed employers in 2006. Higher deductibles were being planned by 22.6% of the surveyed employers. Overall, surveyed employers planned on passing along 29.9% (same as 2005) of cost increases to their employees through some combination of the three – increased premiums, deductibles and co-payments. A similar pattern of

increased cost sharing is found with prescription drugs, where co-pays are being increased by 27.1% of employers in 2006. The 2006 Hay Benefits Report indicates that health care premiums have risen 6.4% for single participants and 7.8% for family coverage. It also reports that the prevalence of completely employer-paid coverage continues to decline with 13% providing 100% employer-paid premiums in 2006 for single coverage and 6% for family coverage compared to 28% and 10% in 2001, and 29% and 12% in 1996. This report showed North Carolina's premium cost for individuals and families was lower than the overall average of the survey participants in all types of medical benefit plans.

In the SHRM 2006 Workplace Forecast Survey, a comparison of "Very Important" job satisfaction aspects showed *Benefits* as being a close second to *Compensation/Pay* for employees at all ages. The survey also reflects the rise in health care costs as the number one key economic trend, and a rise in retiree benefit costs as the second highest economic trend.

In 2006, the state's benefits programs improved somewhat with the addition of PPO options for employee health coverage. However, the state's monetary contribution to employee health care remained the same as in 2005. Separate elements administered by different agencies kept the overall benefits package fragmented. Employee benefits are key ingredients in the total compensation package that is a primary attraction in the recruitment of prospective employees particularly in occupations where skills are scarce in the labor market. Benefits are equally critical in the retention of high performing employees. Benefits as a percentage of total compensation are depicted in the chart below. The state needs to communicate this important aspect of employees' compensation to both current and to prospective employees. One view of a Total Compensation model is shown in Table 17. The average percentage of benefits in NC's model for 2007 is 43.12%.

Total Compensation Model

Table 17 **BENEFITS AS AN AVERAGE PERCENTAGE OF SALARY & WAGES**

| CATEGORY | PERCENTAGE OF TOTAL COMPENSATION | VALUE |
|--|----------------------------------|--------------------|
| Holidays | 4.62% | \$1,781.42 |
| Sick Leave | 4.62% | \$1,781.42 |
| Vacation Leave | 7.60% | \$2,930.48 |
| OASI – DI [Social Security] | 7.65% | \$2,949.76 |
| Retirement | | |
| Retirement Systems Pension Fund | 2.66% | |
| -Death Benefit Trust Fund | .16% | |
| -Retiree Health Plan Reserve | 3.80% | |
| -Disability Income Plan | .52% | |
| | 7.14% | \$2,753.11 |
| Health Insurance | 9.99% | \$3,853.68 |
| Longevity Pay | 1.50% | \$578.39 |
| Total Benefit Value | 43.12% | \$16,628.26 |
| In determining the <i>Percentage of Total Compensation</i>, the average years of state service are 10.5 years and an average salary of \$38,559 as of 12/31/06. The total percentage is added to employees' base pay. | | |
| | Total Base Pay | \$38,559 |
| | Total Benefit Value | \$16,628 |
| | Total Compensation | \$55,187 |

Source: Office of State Personnel, Office of State Budget and Management and the NC Retirement Systems Div.

Paid Time Off Analysis

Paid time off referred to here is employees' time off for which they continue to receive pay. Categories of Paid Time Off include Vacation Leave, Sick Leave, and Holiday pay. The contiguous states of South

Carolina, Tennessee and Virginia report similar responses to the figure shown for the southeastern states, and so, were not reflected separately. Recommendations follow.

Vacation

Southeastern states average 13.77 days of vacation leave based on 1-4 years of service. Similar to North Carolina the average accrual rate progressively increases to reflect the concurrent increases in years of service. By comparison, North Carolina provides the lowest number of vacation days accrued for employees with 0-2 years of service and is at the average for 5-14 years. However, North Carolina’s average accrued vacation days are higher than average for employees with more than 15 years of service. Most of the states accrue leave in whole days, (e.g. 12 or 15 days annually), while North Carolina accrues leave in decimal fractions of a day (e.g. 13.75 days annually). This makes it more difficult to explain our vacation benefits package to employees.

Table 18 **VACATION LEAVE**

| Years of State Service | North Carolina | SE States | Differential in Days |
|---------------------------|----------------|-----------|----------------------|
| 0 but less than 5 | 13.75 | 13.77 | Negligible |
| 5 but less than 10 years | 16.75 | 16.80 | Negligible |
| 10 but less than 15 years | 19.75 | 19.73 | Negligible |
| 15 but less than 20 years | 22.75 | 22.12 | +0.63 |
| 20 but less than 25 years | 25.75 | 24.04 | +1.71 |
| 25 years or greater | 25.75 | 24.57 | +1.18 |

2006 Southeastern States Benefits and Pay Practices Survey

Sick Leave

Southeastern states grant an average of 13.64 days per year sick leave for employees with up to 3 years of service. North Carolina is below the average for all southeastern states at 12 days per year of employee sick leave. Two other states [Arkansas and Tennessee] among those surveyed grant the same number of sick leave days as North Carolina. Some other states [Kentucky, Louisiana, Mississippi] start employees with 12 days but increase the allotment with service time. The most frequently reported number of sick leave days granted per year among southeastern states is 15 days.

Table 19 **SICK LEAVE**

| Sick Leave | North Carolina | SE States | Differential |
|------------|----------------|------------|--------------|
| Accrual | 12 Days | 13.64 Days | -1.64 Days |

2006 Southeastern States Benefits and Pay Practices Survey

Holidays

North Carolina is competitive with the other southeastern states in recognized holidays. The total average for all southeastern states in the survey was 11.39 holidays. That is slightly greater than the 11 holidays normally granted state employees in North Carolina (note that the NC number varies year to year depending on whether 2 or 3 holiday days are granted around Christmas).

Table 20 **HOLIDAYS**

| Holiday Leave | North Carolina | Southeastern States |
|---------------|----------------|---------------------|
| Days per Year | 11 | 11.39 |

2006 Southeastern States Benefits and Pay Practices Survey

Please see recommendations for increases to leave accrual rates on pages 25 and 26 of this report.

Health Insurance

State employees continued to express concern about health care coverage in response to increasing out-of-pocket costs as well as diminished options for coverage. In 2006 the State launched a PPO option to address State Health Plan members’ requests for greater affordability and choice in obtaining coverage. The PPO option was offered to all eligible State Health Plan members, along with the Comprehensive Major Medical Plan (indemnity plan), during an open enrollment period. The PPO became effective in October 2006. With a well-designed PPO choice, the State Health Plan anticipates significant cost savings to members by avoiding deductibles and co-insurance for doctor visits, and reducing premiums for all dependent coverage. Also, there is an Employee-Spouse tier with the PPO, an option which is not available with the Comprehensive Major Medical Plan. This is very positive progress in answering employees’ requests for more affordable health care options. During the 2006 open enrollment period, approximately 330,000 State Health Plan members switched from the traditional indemnity plan to one of the PPO options. “The PPO will save North Carolina taxpayers more than \$25 million dollars from October 1, 2006 through October 1, 2007. Most State Health Plan PPO members and their families will also realize notable health care savings,” said Executive Administrator George C. Stokes.

The information below is used to compare North Carolina’s current indemnity plan to other organizations.

Comparison to Southeastern States

A review was conducted of health insurance coverage for employees in fourteen southeastern states. The results indicate that 10 of 14 southeastern states subsidize their employees’ dependent care coverage. Only North Carolina, Alabama, Kentucky and Mississippi do not subsidize dependent care coverage. Amounts subsidized varied greatly by state and type of health plan employees selected. North Carolina contributes \$321.14 per month for Employee Only coverage but zero additional allowance is made for Dependent (Family) coverage.

SURVEY OF HEALTH INSURANCE COVERAGE FOR DEPENDENT CARE AND CHOICE OF PLAN

Table 21

| Survey Participants | Percent that Subsidizes Dependent Coverage |
|---------------------|--|
| Southeastern States | 71% |

Source: 2006 Southeastern States Benefits and Pay Practices Survey

Comparison to Local Government Practices

In surveys, local governments report on choice of health plan, deductibles and employee and agency cost. The comparative results are in Table 22 on the next page.

Table 22 **SURVEY OF LOCAL GOVERNMENT’S HEALTH INSURANCE PRACTICES**

| Agency | Choice of Plans | Normal Deductible | Normal Co-pay | Amount Employee Pays | Amount Agency Pays |
|--------|-----------------|-------------------|---------------|----------------------|--------------------|
|--------|-----------------|-------------------|---------------|----------------------|--------------------|

| | | | | | |
|--------------------------------|------------|-----------------|----------------|---------------|-----------------|
| Charlotte | YES | | | 0% | 100% |
| Fayetteville | NO | | | 0% | 100% |
| Wilmington | NO | | | 10% | 90% |
| Asheville | NO | | | 0% | 100% |
| Raleigh | YES | | | 0% | 100% |
| Winston-Salem | YES | | | 0% | 100% |
| Buncombe County | NO | \$0.00 | \$15.00 | \$30.44 | \$423.71 |
| Cumberland County | YES | \$500.00 | 20% | \$21.00 | \$342.42 |
| Durham County | YES | \$0.00 | \$20.00 | \$0.00 | \$404.84 |
| Guilford County | YES | \$0.00 | \$15.00 | \$22.10 | \$368.44 |
| Mecklenburg County | YES | No data | No data | \$0.00 | \$385.37 |
| Wake County | YES | \$300.00 | \$25.00 | \$25.00 | \$348.00 |
| State of North Carolina | YES | \$350.00 | \$15.00 | \$0.00 | \$321.14 |

The above information applies to employee only coverage; NC data applies to the Indemnity Plan. Source: North Carolina League of Municipalities 2004 Survey of Municipal Fringe Benefits (biannual report) and the County Salaries in North Carolina 2006

Supplemental Insurance Products (Post-Tax & Pre-Tax Plan)

In 1985, GS 58-31-60 was passed establishing an Employee Insurance Committee designed to review insurance products currently offered through payroll deduction to the State employees in the Employee Insurance Committee's Payroll Unit. These committees are responsible for selecting the type of insurance products that reflect the needs and desires of the employees in the Employee Insurance Committee's Payroll unit.

In the past, there were several attempts made by various committees to address establishing a statewide insurance committee similar to the statewide Flexible Benefits Program Advisory Committee and locating centralized administration in the Office of State Personnel or any other appropriate agency. In the report of the Senate Select Committee on State Employee Insurance Issues dated April 18, 1996, a draft bill with an act to amend the laws governing employee insurance committees was prepared. Legislation was passed to combine the 22 insurance committees within DHHS into one committee so those employees within the department could have the same post-tax supplemental products. This enables employee's portability of their benefits within that department, and reduced rates for employees. The legislation was accordingly passed and changes were implemented.

We are now facing a similar situation where employees cannot carry over some of their benefits to other agencies when they get transferred or hired by a different agency/university, as the two agencies/universities may have different benefits. Two important benefits, term life insurance and short-term disability, are often requested by agency Benefit Representatives to be made available to all employees. In 2005, a pre-tax Voluntary Term Life Plan was available to all State employees.

Statewide Flexible Benefits Program (NC Flex)

In 2005, NC Flex piloted an online enrollment program with participants from two agencies, two universities, and two community colleges. The pilot was a success in all participating organizations, with the entire enrollment process completed online, without any paperwork involved. Phase II of the online enrollment process has started by adding more community colleges, universities, and non-central payroll agencies. Currently there are over 161,000 participants, from the agencies, universities, and community colleges who have taken advantage of the pre-tax savings offered by the this program administered by the Office of State Personnel.

The State's Flexible Benefits Program now includes the following pre-tax plans:

- Health Care Flexible Spending Account allows for a pre-tax payroll deduction to place money in an account to pay for eligible health and dental care expenses not covered by insurance (note: employees may opt to use a Debit Convenience Card for eligible Spending Account expenses)
- Dependent Day Care Flexible Spending Account allows for a pre-tax payroll deduction to place money in an account to pay for day care expenses (note: employees may opt to use a Debit Convenience Card for eligible Spending Account expenses).
- Dental Plan has two options available, High Option and Low Option. Depending on the plan chosen, these options cover expenses for preventive, basic, major, and orthodontia.
- Vision Care Plan has two options, Plan 1 and Plan 2. Depending on the plan option chosen, these plans cover eye exams and materials such as eyeglass lenses, frames, and contact lenses.
- Voluntary Accidental Death & Dismemberment Insurance pays a benefit if a loss is suffered as the result of a covered accident, as well as a disabling injury.
- Supplemental Medical Plan pays a benefit directly to the employee for physician's office visits and inpatient hospital stays. This plan is designed to supplement – not take the place of -- health insurance.
- Voluntary Group Term Life Insurance provides new employees the option to purchase up to \$100,000 of term life insurance without providing evidence of insurability, when first eligible. Employees may elect coverage in increments of \$10,000, with a minimum of \$20,000 and a maximum of \$500,000, not to exceed five times the base annual earnings.
- Cancer Insurance offers two plan options, High Option and Low Option, depending on the desired coverage and benefit paid. This plan also provides benefits for 29 other specified diseases, such as Muscular Dystrophy, Multiple Sclerosis, Tuberculosis, Sickle Cell Anemia and Cystic Fibrosis. Upon initial enrollment for new hires, no evidence of insurability is required.

Retirement

The percent factor used by southeastern states to calculate retirement benefits ranges from 1.6% to 2.5% times Average Final Compensation. North Carolina's factor used to calculate pension benefits is 1.82%. Five southeastern states (Alabama, Georgia, Kentucky, Louisiana, Oklahoma, and West Virginia) have a factor that is higher than North Carolina's 1.82%.

In North Carolina, the employer contribution on behalf of employees in the Teachers & State Employees Retirement System [TSERS] has dropped from 5.33% in 2000/2001, to the current level of 2.34%.

The percentage of active full-time employees who retired in 2006 is shown in table 23 on the following page. Also shown are the percentages of active full-time employees considered eligible for retirement in 2006, and projected out for the next five years. Further implications of this are discussed in the "Turnover" section on pages 13 to 16 of this report.

ACTUAL RETIREMENT AND RETIREMENT PROJECTIONS

Table 23

| CATEGORY | Percent of Workforce | TOTAL |
|------------------------------|-----------------------------|--------------|
| TOTAL RETIRED IN 2006 | 2.7% | 2,396 |

| | | |
|--------------------------------|-------------|--------------|
| TOTAL ELIGIBLE IN 2006* | 4.9% | 4,403 |
| PREDICTED ELIGIBLE** | | |
| 2007 | 5.3% | 4,744 |
| 2008 | 5.8% | 5,145 |
| 2009 | 6.3% | 5,630 |
| 2010 | 6.8% | 6,098 |
| 2011 | 7.2% | 6,374 |

Source: PMIS; predictive model by the Office of State Personnel

* Defined as eligible to retire with unreduced benefits.

** Defined as eligible to retire with unreduced benefits; based on current number of SPA PMFT employees (89,034 as of 12/31/06)

Supplemental Retirement Programs

Besides the traditional retirement program, the State offers voluntary supplemental retirement programs (**a 401(k) plan, a 457(b) plan and a 403(b) plan.**) North Carolina does not match employee contributions. According to Mercer Consulting, 78% of public and private organizations offer an employer match that averages 4% of an employee's pay. The key driver in determining the value of a Deferred Contribution plan is the amount of an employer's contributions.

The following are the results reported for the 100 North Carolina County governments. A review of the past three years reveal that more than half of North Carolina's 100 counties have consistently made matching 401(k) contributions (see Table 23). This year, 54% of the counties offered an employer match or contribution averaging 3.81%. North Carolina State Government provides no contribution to 401(k) except for law enforcement employees. Clearly, the State of North Carolina is behind market by not offering a match, which greatly affects the State's perception as being an employer of choice.

Table 24 **THREE-YEAR COMPARISON OF COUNTY GOVERNMENT 401(K) PLANS**

| Program Plan | % Counties in 2004 Contributing to 401(k) Programs | % Counties in 2005 Contributing to 401(k) Programs | % Counties in 2006 Contributing to 401(k) Programs* |
|-------------------------------------|---|---|--|
| 401(k) contributions in NC Counties | 54% | 49% | 49% |

Source: County Survey 2006 (MAPS Group) – *only counties reporting data were used in calculation

SURVEY OF LOCAL GOVERNMENT DEFERRED COMPENSATION/RETIREMENT PROGRAMS

Table 25

| Municipality | 401(k)/457(b) Match | 401(k)/457(b) Contribution | Municipality Contributes to Retirement Program? |
|---------------------|----------------------------|-----------------------------------|--|
|---------------------|----------------------------|-----------------------------------|--|

| | | | |
|--------------------|----------------------------|-----------------|-----|
| Charlotte | - | 3% 401(k) | Yes |
| Durham | Up to 5% 401(k) | - | Yes |
| Fayetteville | No | No | Yes |
| Greensboro | - | 2% 457(b) | Yes |
| Raleigh | \$2 for every \$1 457(b) | - | Yes |
| Winston-Salem | No | No | Yes |
| Buncombe County | No | No | Yes |
| Cumberland County | Yes | 1% 401(k) | Yes |
| Durham County | 5% either 401(k) or 457(b) | - | Yes |
| Guilford County | - | 5% 401(k) | Yes |
| Mecklenburg County | Up to 5% 457(b) | Up to 5% 401(k) | Yes |
| Wake County | - | 5% 401(k) | Yes |

Source: Office of State Personnel Survey January 2006, 2007 and County Survey 2006 (MAPS Group)

Half (50%) of the southeastern states provide a match to either their 457(b) Deferred Compensation plan or 401(k) supplemental retirement programs.

NUMBER OF SOUTHEASTERN STATES CONTRIBUTING FOR EMPLOYEES

Table 26

| Program Plan | # of States that contribute |
|--------------------------------|-----------------------------|
| 457(b) Deferred Compensation | 5 |
| 401(k) Supplemental Retirement | 4 |
| Both 457(b) and 401(k) | 2 |

Source: 2006 Southeastern States Benefits and Pay Practices Survey

Some states have established a **Partial Lump Sum Option Payment (PLOP)** for certain retirees and benefit recipients. The PLOP is an option at retirement that allows a recipient to initially receive a lump sum benefit payment along with a reduced monthly retirement allowance. The PLOP is a method in which a member, at the time of retirement, may elect to receive a partial lump sum payment amount and a reduced monthly allowance. The lump sum payment cannot be less than six times or more than thirty-six times the monthly amount that would be payable to the member under the plan of payment selected and shall not result in a monthly allowance that is less than fifty percent of that monthly amount. The total amount paid as a lump sum and a monthly benefit shall be the actuarial equivalent of the amount that would have been paid had the lump sum not been selected. As a lump sum distribution, the PLOP is fully taxable and is subject to division of property orders, if applicable.

Work Hours

The following table reflects the standard employee work hours as reported by several local governments. State government employees have longer workweeks than three local government jurisdictions within the Wake, Durham City, Durham County, and Orange county area where approximately 35,000 State workers are employed. Overall, five of the twelve jurisdictions reported that they offer work schedules less than the State government's standard 40 hours.

Table 27 SURVEY OF LOCAL GOVERNMENT WORK HOURS

| Jurisdiction | Work Hours Weekly | Jurisdiction | Work Hours Weekly |
|--------------|-------------------|--------------|-------------------|
|--------------|-------------------|--------------|-------------------|

| | | | |
|---------------------------------|--------------|-----------------|--------------|
| Mecklenburg County | 40 | Wake County | 40 |
| Charlotte | 40 | Raleigh | 38.75 |
| Cumberland County | 40 | Buncombe County | 37.5 |
| Fayetteville | 40 | Asheville | 37.5 |
| Guilford County | 40 | Durham County | 37.5 |
| Greensboro | not reported | Durham (City) | not reported |
| New Hanover County | 40 | Orange County | 40 |
| Wilmington | 40 | Chapel Hill | 37.5 |
| | | | |
| Survey Average | | | 39.2 |
| North Carolina State Government | | | 40 |

Source: League of Municipalities 2004 Survey of Fringe Benefits (biannual report) & County Survey 2006 (MAPS)

VIII. *Benefit Recommendations*

- Change the State Health Plan Year from July 1 - June 30 to January 1 - December 31, so that SPA employees can better plan their out-of-pocket expenses and their strategy for taking advantage of the NC Flex program.
- Match a portion of employees' 401(k) contributions. State matching may be phased in by granting 1% in the current year and an additional 1% each of the next years to 5% total matching contribution by the State for non-law enforcement employees.
- Centralize coordination of supplemental benefits and centralize coordination of supplemental benefits and consolidate supplemental benefit plan offerings in a menu approach for portability and cost savings. Allow employees to select plan products that meet their needs.
- In order to be competitive in the market, we recommend the following:
 1. Combine Leave Accrual categories 0-2 and 2 but less than 5 into one. Increase the Vacation accrual rate by 1¼ day per annum for employees in all categories, which also adjusts to reflect a whole number of accrual days, making North Carolina's benefits package more attractive and matching other leading southeastern states in vacation leave benefits (see Table 27).
 2. Increase the Sick leave accrual rate by 3 days per annum, making North Carolina's benefits package more attractive and matching other southeastern states in sick leave benefits (see Table 28).
 3. Increase the number of holidays by one day in years where eleven are presently granted (see Table 29). Adding the holidays will make North Carolina's overall benefits package more attractive to employees and prospective employees.

Table 27 **PROPOSED INCREASES TO VACATION LEAVE ACCRUAL**
Vacation Leave

| Years of State Service | Current Days Granted Each Year | Additional Days Granted Each Year | Proposed Total Days Granted Each Year |
|-------------------------|--------------------------------|-----------------------------------|---------------------------------------|
| 0 but less than 5 years | 13 ¾ | 1¼ | 15 |

| | | | |
|---------------------------|--------------------------------|-------------------------------|----|
| 5 but less than 10 years | 16 ³ / ₄ | 1 ¹ / ₄ | 18 |
| 10 but less than 15 years | 19 ³ / ₄ | 1 ¹ / ₄ | 21 |
| 15 but less than 20 years | 22 ³ / ₄ | 1 ¹ / ₄ | 24 |
| 20 years or more | 25 ³ / ₄ | 1 ¹ / ₄ | 27 |

Table 28 **PROPOSED INCREASES TO SICK LEAVE ACCRUAL**
Sick Leave

| Current Days Granted Each Year | Additional Days Granted Each Year | Proposed Total Days Granted Each Year |
|--------------------------------|-----------------------------------|---------------------------------------|
| 12 | 3 | 15 |

Table 29 **PROPOSED INCREASES TO HOLIDAY LEAVE**
Holiday Leave

| Current Days Granted Each Year | Additional Days Granted Each Year | Proposed Total Days Granted Each Year |
|---------------------------------------|---|---------------------------------------|
| 11 in some years* 12 in some years | Add 1 day in years where only 11 days are granted | 12 |

*Currently 11 Holidays when Christmas falls on Monday or Friday and 12 Holidays when Christmas falls on Tuesday, Wednesday, or Thursday

If the above recommendations are not implemented, it is strongly recommended that the following be seriously considered:

- Develop an employer supplemental benefit enhancement program providing a fixed amount of \$500 annually with employees having the option to apply towards:
 - a. dependent health coverage, or
 - b. NC Flex benefits package, or
 - c. 401(k) {457(b)} {403(b)} contributions, or
 - d. post-tax supplemental benefit plans.
- Provide leave time in the amount of **3** days, which would move from current earned sick leave and moved to vacation leave. Employees could elect to use three days from current earned sick leave time for personal reasons.

Appendix 1

Market Data

- ◆ *History of Legislative Increases, 1992-2006*
- ◆ *List of Benchmark Classes*

*History of Legislative Increases for NC State Employees
1992 - 2006*

| <i>Year</i> | <i>Cost-of-Living Increase</i> | <i>Career Growth Increase</i> | <i>Bonus Increase</i> |
|-------------|---|-------------------------------|--|
| 1992 | \$522 | 0 | 0 |
| 1993 | 2% | 0 | 1% Bonus |
| 1994 | 4% | 0 | 1% Bonus |
| 1995 | 2% | 0 | 0 |
| 1996 | 2.5% | 2% | 0 |
| 1997 | 2% | 2% | 0 |
| 1998 | 1% | 2% | 1% Performance Bonus |
| 1999 | 1% | 2% | \$125 Performance Bonus |
| 2000 | 2.2% | 2% | \$500 Bonus |
| 2001 | \$625 | 0 | 0 |
| 2002 | 0 | 0 | 10 days, one-time, Leave |
| 2003 | 0 | 0 | \$550 Bonus plus 10 days, one-time, Leave |
| 2004 | 2.5% for salaries over \$40K; or \$1000 / yr for salaries under \$40K | 0 | 0 |
| 2005 | \$850 or 2.0% (whichever is greater) | 0 | 5 days, one-time, leave |
| 2006 | 5.5% | 0 | 0 |

Benchmark Classes Labor Market Data Summary

| Class Titles | North Carolina Salary | Market Rate | Labor Market Pay Gap | Turnover Rate (FY 05-06) | Vacancy Rate (as of 12-06) | Ees |
|---|-----------------------|-------------|----------------------|--------------------------|----------------------------|-------|
| Accountant I | 47,385 | 42,593 | 10.11% | 11.52% | 11.79% | 205 |
| Accounting Manager I | 78,741 | 68,245 | 13.33% | 9.52% | 9.52% | 80 |
| Accounting Technician III | 35,664 | 36,203 | -1.51% | 9.37% | 9.56% | 395 |
| Administrative Secretary III | 35,119 | 35,806 | -1.96% | 12.54% | 9.48% | 339 |
| Artist Illustrator II (Graphic Artist) | 35,663 | 36,360 | -1.95% | 14.44% | 12.62% | 90 |
| Business Technology Applications Analyst | 61,476 | 69008 | -12.25% | 6.5% * | 19.62% | 893 |
| Chemist II | 48,996 | 46,795 | 4.49% | 3.70% | 15.62% | 26 |
| Clinical Dietitian I (Registered) | 42,980 | 41,083 | 4.41% | 6.67% | 8.90% | 44 |
| Cook II (Dietary Cook) | 24,219 | 27,100 | -11.90% | 22.90% | 9.21% | 140 |
| Correctional Officer (includes trainee class) | 28,083 | 26,574 | 5.37% | 19.80% | 7.88% | 9,615 |
| Electrician II | 34,117 | 40,583 | -18.95% | 8.93% | 5.76% | 180 |
| Environmental Engineer II | 58,854 | 62,242 | -5.76% | 6.67% | 8.33% | 168 |
| Executive Assistant I | 39,065 | 42,901 | -9.82% | 10.15% | 8.63% | 135 |
| Facility Mechanical Engineer I | 60,978 | 55,851 | 8.41% | 5.00% | 13.63% | 19 |
| Forester I | 38,063 | 34,984 | 8.09% | 14.71% | 17.30% | 35 |
| Health Care Tech I | 24,245 | 23,200 | 4.31% | 18.81% | 6.87% | 3,513 |
| Housekeeper | 22,151 | 20,488 | 7.51% | 12.37% | 10.47% | 2,104 |
| HVAC Mechanic | 37,148 | 37,955 | -2.17% | 8.93% | 5.76% | 207 |
| Information and Communication Spec II | 42,350 | 41,367 | 2.32% | 8.73% | 16.58% | 166 |
| Information Technology Manager | 80,345 | 93,214 | -16.02% | 5.88% * | 12.40% | 341 |
| Internal Auditor I | 45,790 | 47,930 | -4.67% | 10.53% | 34.48% | 19 |
| Internal Auditor II | 56,770 | 59,047 | -4.01% | 13.95% | 17.54% | 47 |
| Librarian II | 39,855 | 45,588 | -14.39% | 18.75% | 26.32% | 14 |

Benchmark Classes Labor Market Data Summary

| Class Titles | North Carolina Salary | Market Rate | Labor Market Pay Gap | Turnover Rate (FY 05-06) | Vacancy Rate (as of 12-06) | Ees |
|------------------------------------|-----------------------|-------------|----------------------|--------------------------|----------------------------|-------|
| Maintenance Mechanic IV | 35,419 | 35,082 | 0.95% | 9.19% | 9.96% | 467 |
| Mechanic II | 36,153 | 40,496 | -12.01% | 2.84% | 6.12% | 139 |
| Medical Laboratory Technologist II | 43,095 | 42,790 | 0.71% | 14.10% | 12.50% | 84 |
| Networking Technician | 46,808 | 47,300 | -1.05% | 2.65% * | 7.92% | 152 |
| Nurse Supervisor I (Head Nurse) | 53,565 | 62,187 | -16.10 | 20.00% | 14.28% | 6 |
| Occupational Therapist I | 55,409 | 54,639 | 1.39% | 18.42% | 30.00% | 41 |
| Office Assistant IV | 29,609 | 30,777 | -3.95% | 12.10% | 12.60% | 2,014 |
| Operations & Systems Specialist | 76,878 | 64,400 | 16.23% | 3.59% * | 11.24% | 232 |
| Operations & Systems Technician | 37,071 | 33,426 | 9.83% | 4.62% * | 7.14% | 171 |
| Paralegal II | 40,451 | 45,540 | -12.58% | 16.67% | 12.28% | 51 |
| Park Superintendent III | 54,424 | 49,001 | 9.96% | 0.00% | 0.00% | 9 |
| Personnel Analyst II | 52,994 | 48,542 | 8.38% | 10.84% | 6.32% | 90 |
| Personnel Officer III | 65,404 | 72,869 | -11.41% | 16.67% | 0.00% | 6 |
| Pharmacist (Licensed) | 90,027 | 79,097 | 12.14 | 11.59% | 6.41% | 74 |
| Physical Therapist I | 55,919 | 61,105 | -9.27% | 0.00% | 18.18% | 7 |
| Physician Extender I | 66,205 | 70,636 | -6.69% | 7.14% | 36.84% | 13 |
| Practical Nurse II | 31,556 | 33,603 | -6.49% | 22.22% | 19.35% | 27 |
| Public Safety Officer | 34,607 | 36,044 | -4.15% | 18.69% * | 18.18% | 347 |
| SBI Agent I | 41,424 | 44,407 | -7.20% | 1.54% | 3.37% | 84 |
| Security Guard | 23,828 | 28,245 | -18.54% | 13.51% | 16.36% | 79 |
| Social Worker II (BSW) | 36,833 | 37,861 | -2.79% | 25.00% | 20.69% | 48 |
| Social Worker III (MSW) | 39,472 | 42,588 | -7.89% | 12.35% | 10.82% | 177 |
| Speech and Language Pathologist I | 50,936 | 53,516 | -6.19% | 13.79% | 30.77% | 59 |
| Staff Nurse (RN) | 45,835 | 49,108 | -7.14% | 28.00% | 20.51% | 27 |
| Transportation Engineer I | 49,132 | 43,000 | 12.48% | 10.63% | 21.93% | 283 |
| Rehabilitation Counselor I | 36,923 | 35,363 | 4.23% | 24.22% | 10.63% | 169 |
| Welder II | 36,195 | 36,076 | 0.33% | 3.57% | 12.90% | 25 |

Note: Column Header "Ees" is the number of employees in the class

* Turnover rates for these Career-banded classifications may not be entirely accurate given that these classes were implemented by some agencies and universities at different times prior to or over the course of the fiscal year. They are now fully implemented.

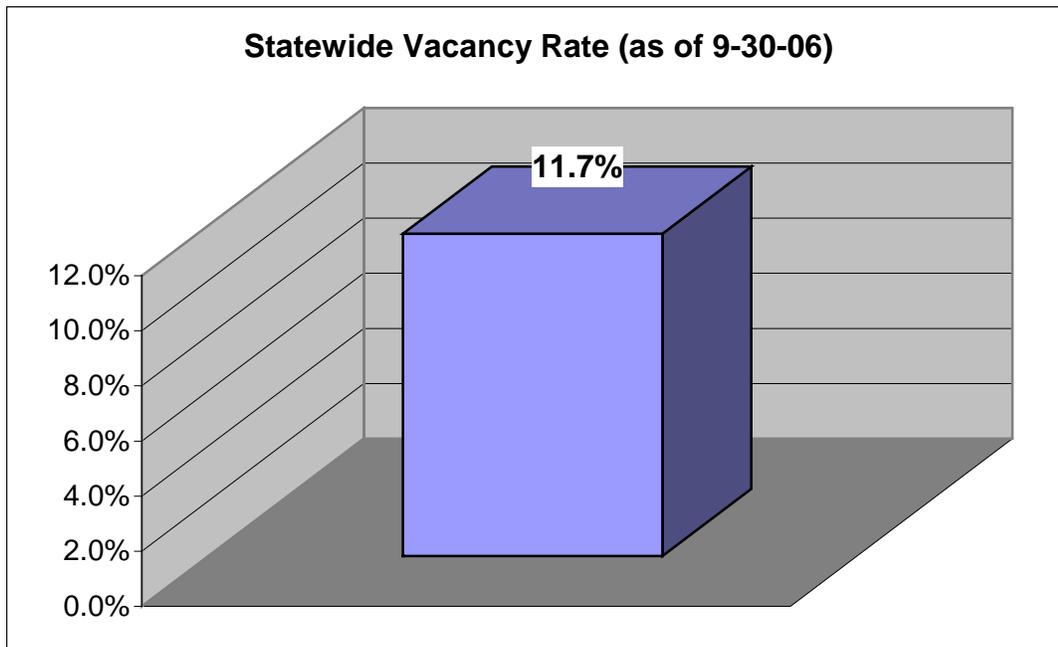
Appendix 2

Dashboard Data

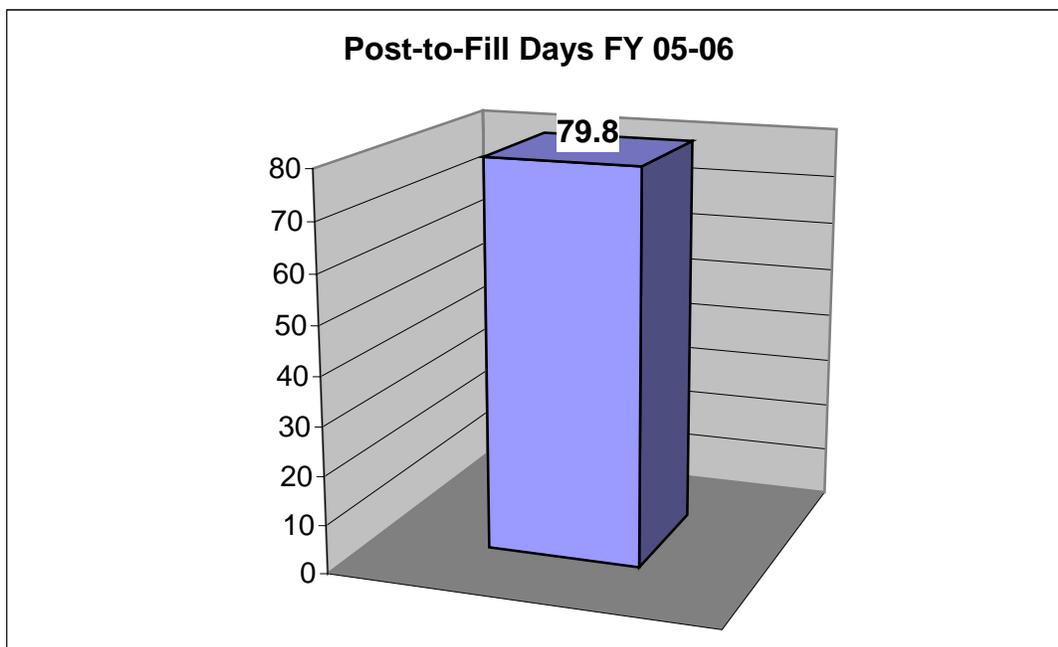
- ◆ *Statewide Hiring*
- ◆ *Statewide Retention*
- ◆ *Statewide Compensation*

The following charts are samples of data initially compiled by the Office of State Personnel for use in allowing agencies to assess their Human Resources functions in relation to overall statewide trends. Data shown here is statewide only, and will be used in subsequent annual compensation reports to show statewide comparisons and trends from year to year. These charts are “snapshots” and should be considered for informational purposes only.

I. STATEWIDE HIRING DATA

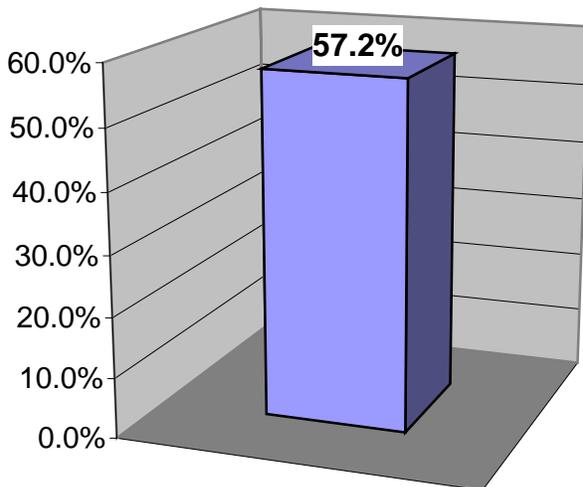


This chart shows the statewide percentage of positions vacant as of September 30, 2006. The vacancy rate can be indicative of the success of recruitment and retention efforts.



This chart shows the average amount of time it took to fill vacant positions, from the date posted for recruitment to the date filled. Post-to-fill time is critical because quality candidates can be lost to other employers when the hiring process takes too long.

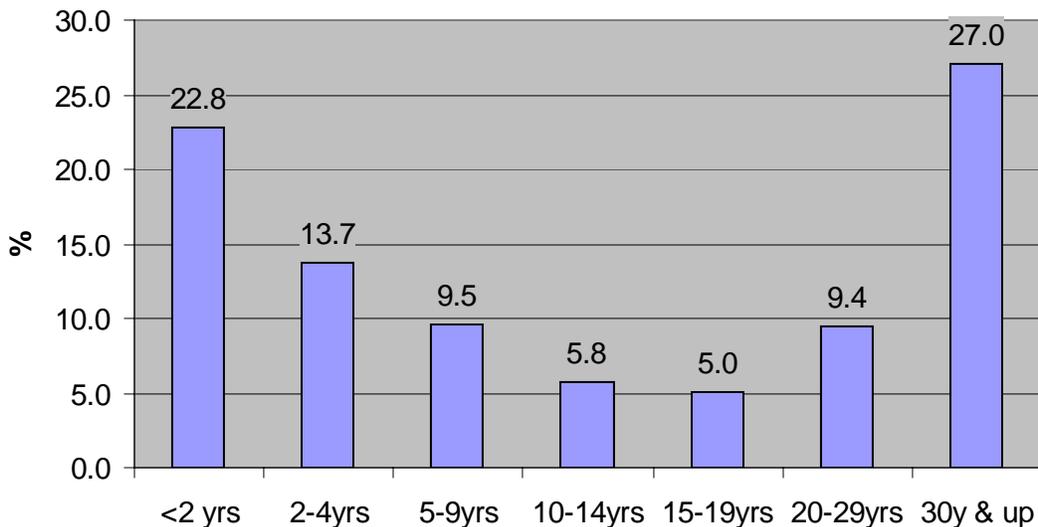
Percent of New Hires Completing Probationary Period FY 05-06



This chart shows the percentage of newly hired employees completing probation. This data can be indicative of a recruitment program's success, i.e., if the right candidates are being hired then likely more of them will complete probation.

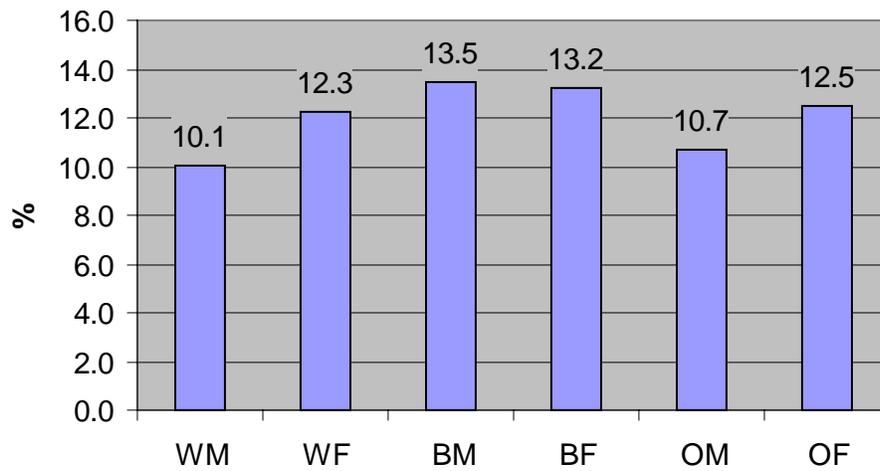
II. STATEWIDE RETENTION DATA

Total Percent Turnover by Length of Service



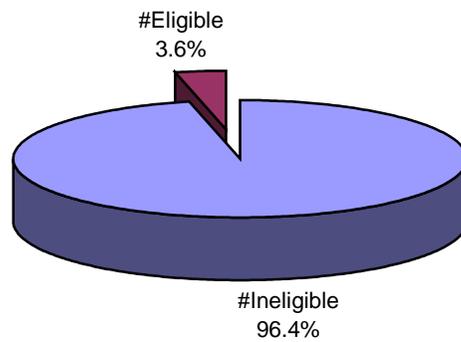
This graphic outlines the retention of length-of-service workforce segments. Particular attention should be paid to the data for early tenure employee retention, a segment of the workforce that is critical to recruit and retain.

Total Percent Turnover by Race & Gender



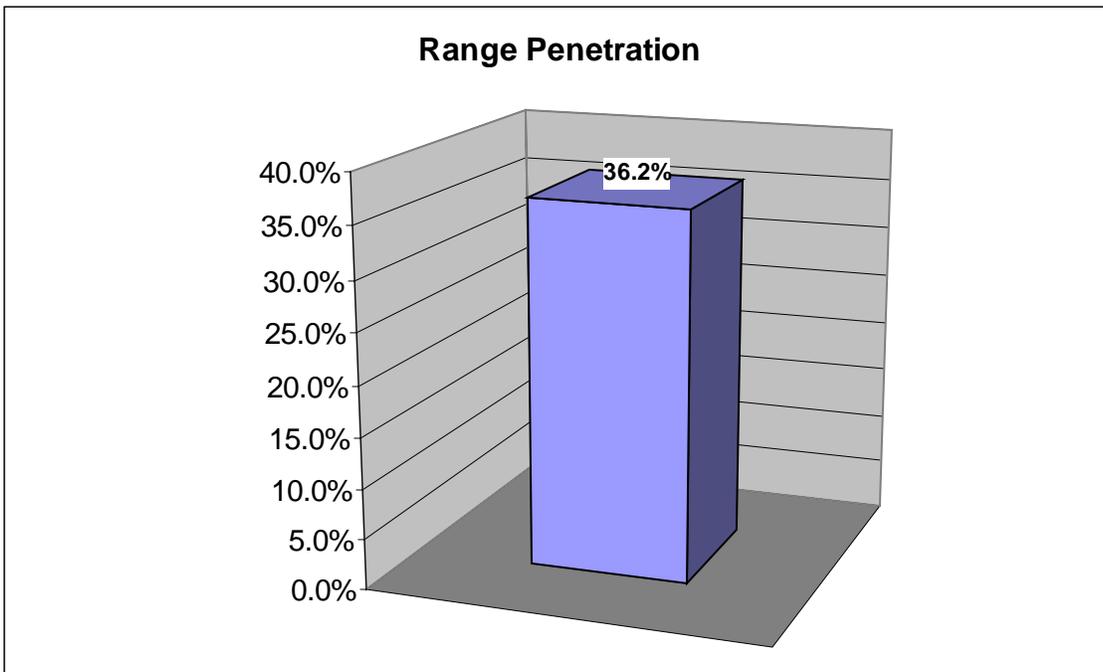
This metric tracks turnover by demographic groups. It is useful in helping to determine if the state is effectively retaining all race-gender segments of the workforce in comparison to the overall turnover rate (11.7% as of 9-30-2006).

Statewide Percent of Employees Eligible for Retirement as of 9-30-2006

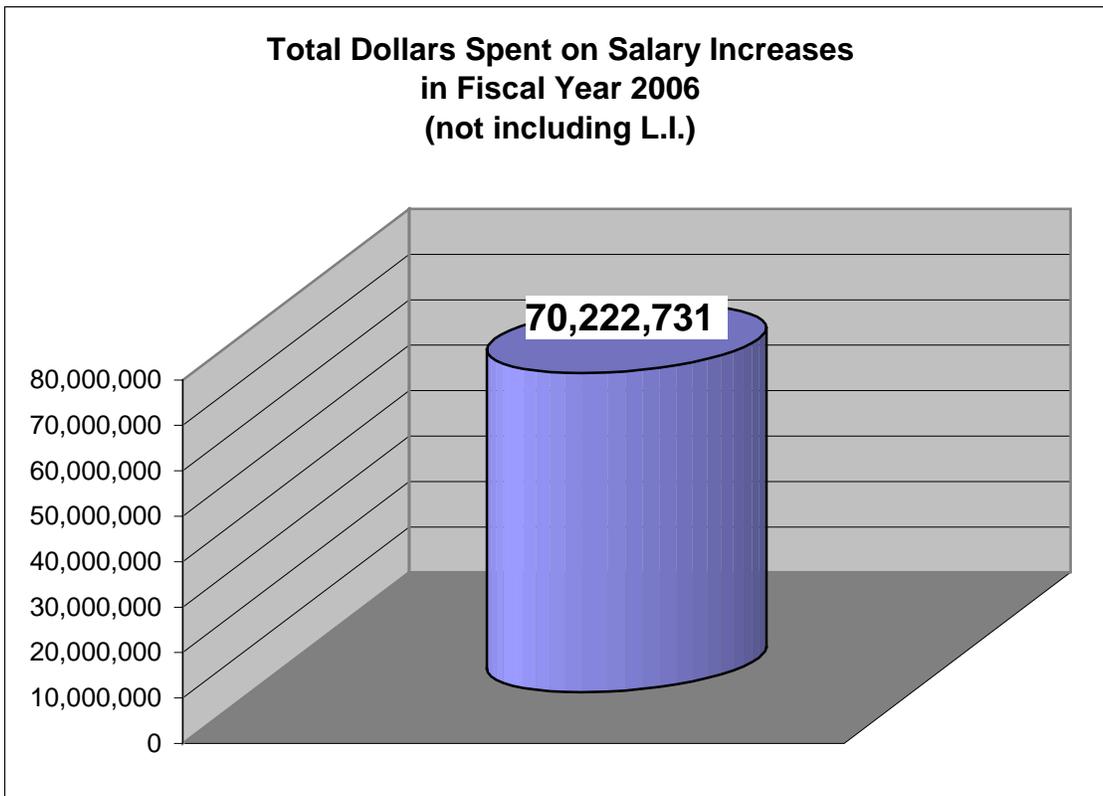


This graphic depicts the proportion of the state's workforce that may exit the organization for retirement. It is critical that planning take place to transfer these employees' institutional knowledge.

III. STATEWIDE COMPENSATION DATA

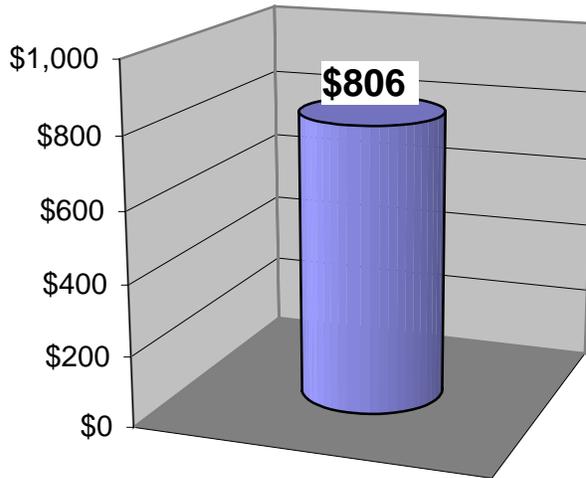


Range penetration is the average percent employees are paid above pay range minimums. The number may be indicative of how well the state is employing mechanisms for setting salaries, or making funds available to do so.



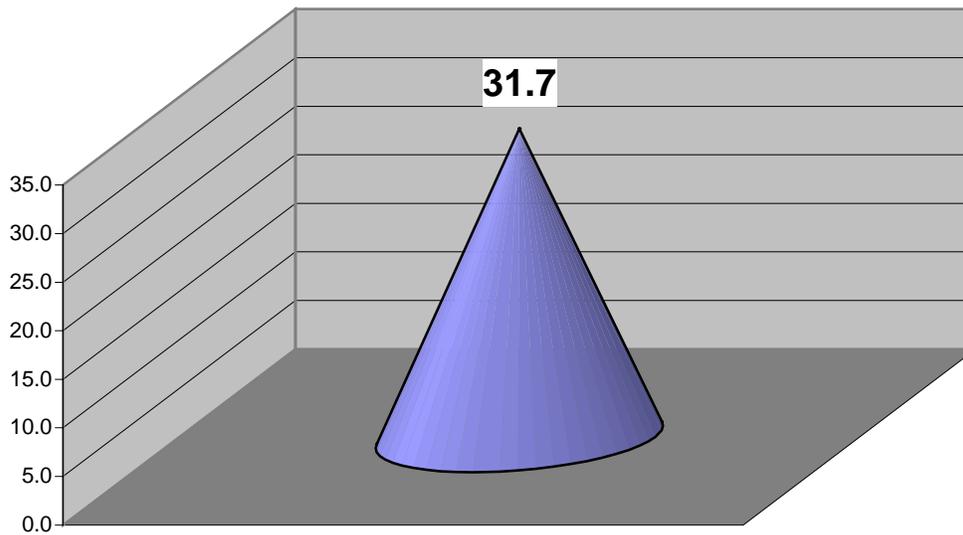
This information can be used for planning purposes as salary improvement needs are considered.

2007 Statewide Per Capita Dollars Spent on Salary Increases (not including COLA)



This graphic represents the average amount spent on salary increases per employee. As above, this information can be used for planning purposes as salary improvement needs are considered.

Percent of Employees Receiving Salary Increases



This graphic represents the percentage of state employees receiving salary increases (other than COLA). It gives some indication as to the distribution of salary reserves.