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OFCCP Guidelines — Scientifically Valid But Unclear

Law360, New York (April 08, 2013, 12:29 PM ET) -- The Office of Federal Contract Compliance Programs (OFCCP) has issued new compensation guidelines for federal contractors, effective Feb. 28, 2013.[1] The OFCCP Directive 307 replaces previous compensation guidelines and provides an outline of steps that compliance officers may undertake in conducting a compensation review.

While the new guidelines do not provide a detailed plan as to how the OFCCP will conduct its investigations, they do describe a series of steps that provide enough flexibility to conduct a rigorous analysis. This flexibility is motivated by the complexity of pay practices and the statistical issues arising from analyzing comparator groups of varying sizes.

The lack of specificity may be frustrating to contractors; however, the upside may be that the guidelines suggest that the OFCCP will try to accurately model the contractor's compensation decisions.

Overview of Steps

In the guidelines, the OFCCP outlines a series of steps that a compliance officer will generally conduct. These include conducting a preliminary analysis using affirmative action plan (AAP) job groups followed by an individual level review. Once the individual level data are reviewed, the compliance officers will determine the scope of the investigation and consider all employment practices that may lead to disparities, examining not just base pay but promotions, work assignments and other opportunities as well.

The OFCCP will consider a variety of factors that can potentially explain differences in pay including education, experience, performance ratings and tenure at position and level. If the number of comparable employees is sufficiently large, the compliance officer may develop pay analysis groups, which usually would be evaluated using a multiple regression analysis to control for a variety of factors.

If the number of comparable employees is relatively small, the OFCCP may employ less statistically demanding techniques, such as a cohort analysis. The OFCCP indicates that it will investigate systemic, small group and individual discrimination.

Implications for Reliable Investigations of Compensation Practices

The remainder of the article will discuss the various statistical issues and practical implications of the guidelines. The article examines the consequences of providing flexibility in creating comparator groups, the implication of investigating a smaller subset of employees, the identification of relevant factors and the study of groups of employees that may be too small to analyze using some statistical models.

Flexibility in Creating Pay Analysis Groups

The guidelines indicate that compliance officers will create pay analysis groups to test for statistically significant pay disparities. Pay analysis groups may be "limited to a single job or title, or may include multiple distinct units or categories of workers. A pay analysis group may combine employees in different jobs or groups, with statistical controls to ensure that workers are similarly situated."[2]

While there are various rules of thumb about how large a sample to analyze, a hard and fast rule is probably not realistic as each analysis can present unique facts. There are objective statistical tests that can be used to determine the precision, accuracy and robustness of estimates of discrimination. These tests measure the sensitivity of the model to alternative models and can be used to determine whether the results are robust to other logical interpretations.

There is a variety of reasons why a model may deliver unexpected results. Among the potential reasons are that a model may include irrelevant factors or may exclude important factors, the pay analysis groups may include individuals who are compensated very differently, or outcomes are determined by a few outliers. A larger sample size may not compensate for a poorly specified model.

The guidelines do not specify how to group similar jobs. The quote in the previous paragraph describes the use of statistical controls to ensure that workers are similarly situated. This raises the important statistical issue of whether to analyze different job groups separately or to analyze them together while controlling for the different job groups.

Controlling for a job group within a larger pay analysis group may be more appropriate when one particular job group offers slightly higher or lower compensation than comparable job groups but other factors such as experience and performance are similarly rewarded. Conversely, if other factors are rewarded differently, it may be more appropriate to analyze each group differently.

For example, butchers in a supermarket may earn a bit more than bakers (possibly because of the risk of injury associated with cutting meat) but are similarly rewarded for experience, tenure with the company and performance. In this example, it may make sense to group these two jobs and to statistically control for butchers.

However, if a company has two sets of sales teams, one that earns a small base salary and a large incentive component, while another earns a large base salary and a small incentive component, grouping these two sets of employees may not be correct. Individual performance is probably rewarded differently for these two sets of sales teams, so the two sets of jobs should potentially be analyzed separately. Each job in a firm may have different characteristics and responsibilities so flexible guidelines are warranted.

Investigating Smaller Subsets of Employees

Compliance officers may drill down into greater detail after an initial test of a larger group. The guidelines state that as "the results of the initial analysis and facts warrant, OFCCP refines the analysis, based on pre- or post-onsite information, and OFCCP may conduct subsequent statistical and/or non-statistical tests of smaller groups or individuals."[3]

While an expansion of an analysis into smaller groups could impose additional demands, a more detailed analysis of smaller groups may benefit contractors.

In particular, issues affecting a subset of employees can taint a larger sample. If there is a statistically significant adverse impact on a small subset of employees, aggregating these employees with other employee groups into a larger pay analysis group can cause the larger group to appear to be adversely impacted. Disaggregation can identify the precise problem area, potentially reducing exposure and damages.

Additionally, excessive aggregation of small groups for which there is individually no adverse impact can cause the appearance of adverse impact for the aggregated group. This can happen if members of a protected group are more likely to be represented in certain smaller groups.

For instance, if there are more female marketing managers but fewer female finance managers, and if finance managers are, on average, paid more than marketing managers, an aggregated analysis that does not control for the type of manager may find that men are paid more. Disaggregating the analysis by manager type could indicate that women were not paid less than men. Employers may want to maintain data on market compensation to demonstrate that the salaries of finance managers, in this example, were higher due to market factors and not discrimination.

Identification of Relevant Factors

The guidelines present factors that compliance officers may consider in modeling compensation. The OFCCP could consider individual-specific factors such as education, experience, tenure in position and performance ratings or job-specific factors such as position, level and function.

However, a factor cannot be used if it is potentially tainted by discrimination. Objective measures of performance may be used as valid explanatory factors, but more subjective measures of performance can be more problematic.

For instance, a measure of future potential could be perceived as discriminatory against older employees. Before using a specific factor, the compliance officer would determine whether the data are complete and whether the factor is relevant and consistently applied to all employees.

On several occasions, the guidelines mention the use of regression analysis in modeling compensation. A regression analysis is a very useful tool for examining an outcome when a variety of factors may impact that outcome. In practice, comparing means is limited to just a few explanatory factors.

If an economist or statistician is comparing compensation between men and women and has information only on whether an employee had extensive or limited experience, she could compare salaries of experienced men and women and separately compare salaries of inexperienced men and women. It would become more difficult to compare means if experience were measured continuously (if there is a distinction among one, five, 10 and 15 years of experience) or if additional factors such as education were available.

So while a regression analysis — a widely accepted statistical tool that is frequently used in litigation — may appear as a bit of a black box to someone with limited statistical experience, it is very useful in analyzing outcomes when a variety of explanatory factors are present.

Analysis of Smaller Groups

As the number of comparable employees becomes smaller, a statistical analysis can become less effective. If idiosyncratic, individual-specific characteristics explain compensation outcomes, it may be more appropriate to use a different methodology. This could be the case if an employee has a unique function within company (which is usually the case for senior-level employees) or if the company has few employees.

In these circumstances, it may be more challenging to conduct a standard statistical analysis. The guidelines recognize this complexity and discuss the use of a comparative or cohort analysis to examine the treatment of employees.

Comparative analysis is less statistically complex but may require a much more detailed and possibly anecdotal review of the employment circumstances of each employee being analyzed. Because such employees would probably have to be analyzed differently than employees with many relevant comparators, a uniform methodology could probably not be applied.

Conclusions

Given the scope of employment practices, it is probably not feasible to provide a detailed, consistently applied, replicable step-by-step process to be followed in all investigations. While contractors may find the lack of a specific methodology frustrating, the flexibility of the approaches does provide both the contractor and the OFCCP an opportunity to correctly model compensation practices.

The description of the potential analyses suggests that the OFCCP has considered various statistical and econometric complications when drafting these guidelines and intends to conduct more scientifically rigorous investigations. Accordingly, employers and their legal counsel are likely to be well-served by having the capability to evaluate and, if necessary, challenge the statistical findings of the OFCCP.

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