

Unjust Rewards

Public opinion on CEO pay

Briefing Note
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Unjust Rewards: Public opinion on CEO pay

Contents

Executive Summary	3
Introduction: Executive pay and inequality in the UK	4
Executive Pay and COVID-19	5
Public Opinion and Executive Pay	7
Findings	7
Discussion	9
Recommendations	11
Appendix I: Full Survey Results	12

Executive Summary

- New polling commissioned by The Equality Trust shows extremely high levels of concern among the public around the issue of executive pay. The Opinium poll of 2,000 UK adults shows that:
 - **73%** of respondents agreed that “the gap in pay between average workers and the highest paid executives in the UK is too wide.”
 - **77%** of respondents agree that “companies that benefited from public support through the COVID-19 pandemic (e.g. the government furlough scheme) should not be increasing the pay of their highest paid executives.”
 - **72%** agreed that “government action and regulation is needed to ensure companies provide a more equitable distribution of pay between chief executives and average workers”, and **64%** agreed that “the government should set a maximum salary for executives relative to workers.”
- The survey results clearly show that the British public is strongly against any pay rise for highly paid executives this year, an insight that companies and investors should take note of this AGM season. It is also clear that public concern about high executive pay is not limited to the context of COVID-19. There is a distinct sense among a majority of people that the distribution of rewards within companies is not equitably balanced, as well as strong support for action from government to address these imbalances.
- Over the past 40 years, the pay of chief executives in the United Kingdom has skyrocketed while the wages of average workers have stagnated. As a consequence, very high executive pay and the structures that underlie it have become major drivers of income inequality in the UK.
- The UK is facing an escalating cost of living crisis driven by rising food and energy prices and tax rises on working people. As the crisis reaches its predicted peak in Spring 2022, many FTSE-100 companies will be holding their AGMs, where they will decide on the pay of their executives. There are fears that this year’s AGM season could see executive pay rebound as executives seek ‘catch up’ pay after two years of restraint.
- The polling shows a clear majority in favour of government action to tackle disparities in pay. The Equality Trust recommends that the government consider measures to target executive pay directly (such as introducing a surcharge to corporation tax based on a ratio of CEO to worker pay), as well as broader measures aimed at rebalancing power in the corporation, such as reforming section 172 of the Companies Act, and introducing mandatory worker representation on boards, sectoral bargaining and profit sharing.

Introduction: Executive pay and inequality in the UK

Over the past 40 years, the United Kingdom has seen a substantial rise in levels of economic inequality, with progressively higher amounts of total income going to those at the top of the income distribution, while the bottom 50% have secured progressively less. These changes do not reflect changes in productivity or effort; in fact, evidence suggests¹ that many workers are working harder than ever. What this rise in inequality represents instead is fundamental changes to the economic ‘rules of the game’ governing how rewards from economic activity are distributed. This briefing focuses on one particular group of workers, executives at large companies, and the structures that govern their pay, presenting new evidence on public opinion around executive pay in the context of the COVID-19 pandemic and the UK’s cost of living crisis.

There is strong rationale for focussing on executive pay as an issue of economic justice. Over the past 40 years, executive pay in the UK has far outstripped that of workers on average or low incomes. In the FTSE-100, for example, the average CEO earned 11 times that of the median UK worker² in 1980. By 2019, this ratio had risen to around 119 times³ the average worker, with the median FTSE-100 CEO being paid around £3.6m and the highest paid CEO taking home £58.73m, or 1,935 times the pay of the average UK worker.

As a result, soaring executive pay has become a major driver of economic inequality in the UK. In an analysis of public use tax return files, Bell and van Reenen⁴ found that the amount of total pre-tax income earned by the top 1% of earners’ had risen by 2.9% from 1998/9

to 2007/8, with almost all of these gains attributable to the rising wages of two groups of workers: chief executives and financial sector employees. Similarly, Brewer and Samano-Robles,⁵ in an analysis of the characteristics of those on top incomes, found that the top 1%, 0.1% and 0.001% overwhelmingly worked in “finance, insurance and real estate” or providing “professional, scientific and technical services.”

The proximate causes of this explosion in executive pay are well established. Starting in the 1980s, models of executive compensation began to reflect the idea that the interests of shareholders should be given primacy over all other stakeholders. In this ‘shareholder primacy’ model, a key goal of executive compensation is to align the interests of management and shareholders, and as such, executive pay packages were restructured to emphasise an ideal of ‘performance’ based to a large degree on capital market measures such as Earnings Per Share (EPS.)

These reforms have opened up a variety of avenues for executives to secure increasingly large pay packages, often without providing any marginal benefit to the companies that employ them. For example, because variable pay is so often based on capital market measures, executives can reap the benefits of any increase to the share price of a company, whether or not it was a result of their actions, especially when the stock market as a whole is buoyant. As recent research⁶ from the High Pay Centre shows, ‘performance related’ annual bonuses and Long Term Incentive Plans (LTIPS) are often structured so that they almost always pay out,

1 Felstead, A, Gallie, D, Green, F and Inanc, H (2013) *Work Intensification in Britain: First Findings from the Skills and Employment Survey 2012*, London: Centre for Learning and Life Chances in Knowledge Economies and Societies, Institute of Education.

2 Bell, B. D., & Van Reenen, J. (2013). Extreme wage inequality: pay at the very top. *American economic review*, 103(3), 153-57.

3 High Pay Centre and CIPD (2019) *HPC/CIPD Annual FTSE 100 CEO Pay Review*, (<https://highpaycentre.org/hpc-cipd-annual-ftse-100-ceo-pay-review-ceo-pay-flat-in-2019/>)

4 Ball & Van Reenen, *Extreme Wage Inequality*

5 Brewer, M. & Samano Robles, C. (2019). *Top incomes in the UK: analysis of the 2015-16 Survey of Personal Incomes*

usually at very close to their maximum values: in the years 2009-2019, LTIPs paid out in 85% of cases, with half of all LTIPs paying out at least two thirds of their maximum value. Meanwhile 94% of annual bonuses paid out, with half of bonus plans paying out at least three quarters of their maximum value.

In response to concerns about soaring CEO pay, the government has introduced a number of reforms, starting with the proposals made in the 1995 Greenbury Report, which then went on to form the basis of Section D of the UK Corporate Governance Code.⁷ However, these

measures have failed to significantly dampen CEO pay, primarily because they have relied on shareholders to act as proactive stewards. In reality, many financial institutions are simply asleep at the wheel: research from the High Pay Centre⁸ shows that, between 2014 and 2018, every pay policy at FTSE-100 companies was approved by shareholders.

Executive Pay and COVID-19

When the COVID-19 pandemic hit the UK in early 2020, many corporate boards took steps to limit CEO pay, either unilaterally or as a result of investor pressure. As a result, median CEO pay fell by 17% in the FTSE-100 and by 12% in the FTSE-30. Annual bonuses in the FTSE-100 were also down, paying out at an average of 38% (compared to an average of around 70% in preceding years). Over half of executives received no salary increase, and around a third of FTSE-100 companies reduced, cancelled or waived annual bonuses according to Deloitte.⁹ Meanwhile, low votes (<80% approval) from investors on remuneration reports in the FTSE-100 reached their highest level in recent years at 13%, with low votes on pay policies hitting 25%.

While this ‘restraint’ might be taken as a sign that the current regime for governing executive pay is working, it is worth reflecting on the wider consequences of the pandemic

for executive pay. Firstly, despite the actions of investors and boards, the overall level of CEO pay remained hugely disproportionate to workers, with the median FTSE-100 CEO taking home £2.69m, or around 86 times that of the average worker. Secondly, these levels of executive pay persisted despite unprecedented levels of taxpayer support for businesses: according to data from the Office for Budget Responsibility, the government provided businesses with £70 billion via the Coronavirus Job Retention Scheme, £31.95bn under the Coronavirus Business Interruption Loan Scheme (CBILS) and Coronavirus Large Business Interruption Loan Scheme (CLBILS) and £18.98bn under the COVID Corporate Financing Facility in 2020/2021. While some of these programmes placed limitations on executive pay, these restrictions were often weak (for example in the CLBILS requirement that the loan could not be used to award pay rises unless the pay rise was agreed in writing

6 High Pay Centre, (2021) Are bonus payments and Long Term Incentive Plans fair and proportionate rewards and incentives for business leaders? (<https://highpaycentre.org/are-bonus-payments-and-long-term-incentive-plans-fair-and-proportionate-rewards-and-incentives-for-business-leaders>)

7 Financial Reporting Council (2018), The UK Corporate Governance Code (<https://www.frc.org.uk/getattachment/88bd8c45-50ea-4841-95b0-d2f-4f48069a2/2018-UK-Corporate-Governance-Code-FINAL.pdf>)

8 Walsh, A (2020) The myth of shareholder stewardship: How Effectively Do Shareholders oversee FTSE 100 CEO Pay? (https://highpaycentre.org/wp-content/uploads/2020/08/myth_of_shareholder_stewardship.pdf)

9 Deloitte (2021) Directors' remuneration in FTSE 100 companies Your Guide - October 2021, (<https://www2.deloitte.com/uk/en/pages/tax/articles/directors-remuneration-in-ftse-100-companies-oct-2021.html>)

before the loan was taken out), while for others, most notably the CJRS, there were no formal requirements restricting pay rises and bonuses.

Lastly and perhaps most importantly, the underlying structures which enabled soaring executive pay remain in place. This is crucial because, going into 2022's spring AGM season, there is a question as to whether or not boards will once again act with restraint, or if executive pay will rebound, particularly if executives at FTSE-100 companies push for 'catch up' pay or performance based pay awards with soft financial targets to make up for a 'lost year' of bonuses. It is worth noting that, as of January 2022, while most FTSE 100 companies had not yet announced CEO pay for their financial year ending in 2021, 57% of those that have done so have recorded an increase on 2020 levels according to the High Pay Centre.¹⁰ The prospect of a return to pre-pandemic levels of CEO pay is all the more concerning for the fact that the UK is currently in the midst of a cost of living crisis driven by surging food and energy prices and tax rises on workers. Ironically, the cost of living crisis looks set to hit its peak in April 2022, just as many FTSE-100 companies will look to pass votes on their CEOs' pay at their AGMs.

Public Opinion and Executive Pay

Given the role of executive pay in perpetuating economic inequality in the United Kingdom, The Equality Trust believes that it is vital that the public's views on issues of executive pay are heard and taken on by companies, investors and policymakers. This is particularly relevant in the context of high public support for companies in the wake of the pandemic, and concerns about the cost of living crisis. In order to do this The Equality Trust has commissioned polling from Opinium. The polling was conducted on a representative sample of 2000 UK adults in December 2021. Respondents were given the following context:

Over the past few decades, chief executives of British companies have seen their pay packages grow in comparison to the average worker.

In 1980, the average (median) CEO of a UK FTSE 100 company earned 11 times that of the average UK full-time worker. In 2020 the average (median) FTSE* 100 CEO received 86 times the pay of the average UK full-time worker, with the highest paid CEO in the FTSE* 100 receiving 491 times the average UK full-time worker last year.*

**The Financial Times Stock Exchange (FTSE) 100 Index is a list of the 100 largest companies listed on the London Stock Exchange.*

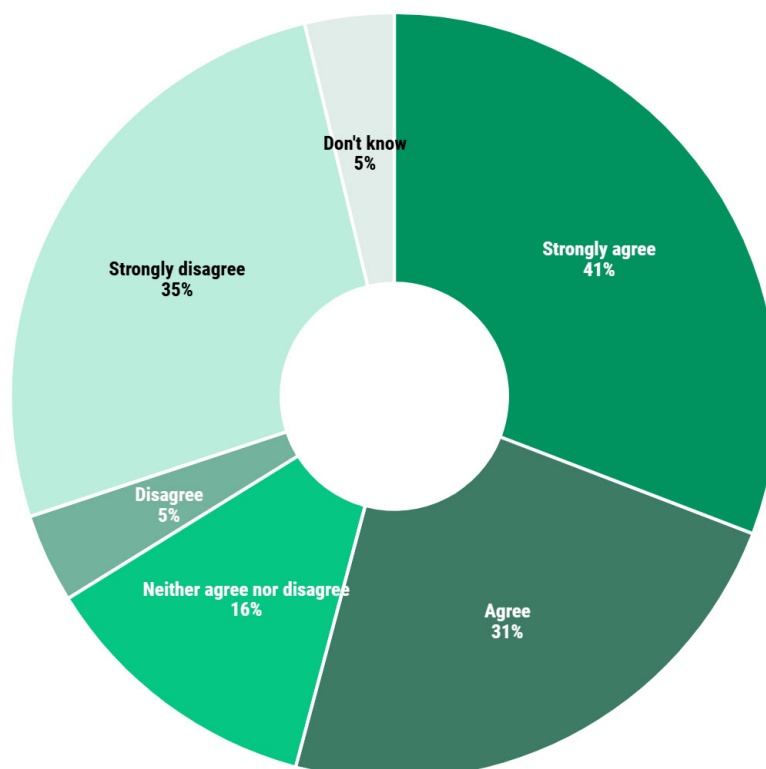
Respondents were then asked to indicate the extent to which they agreed or disagreed with a number of statements on the issue of CEO pay.

The statements were chosen to reflect a range of issues and perspectives around CEO pay and pay disparities.

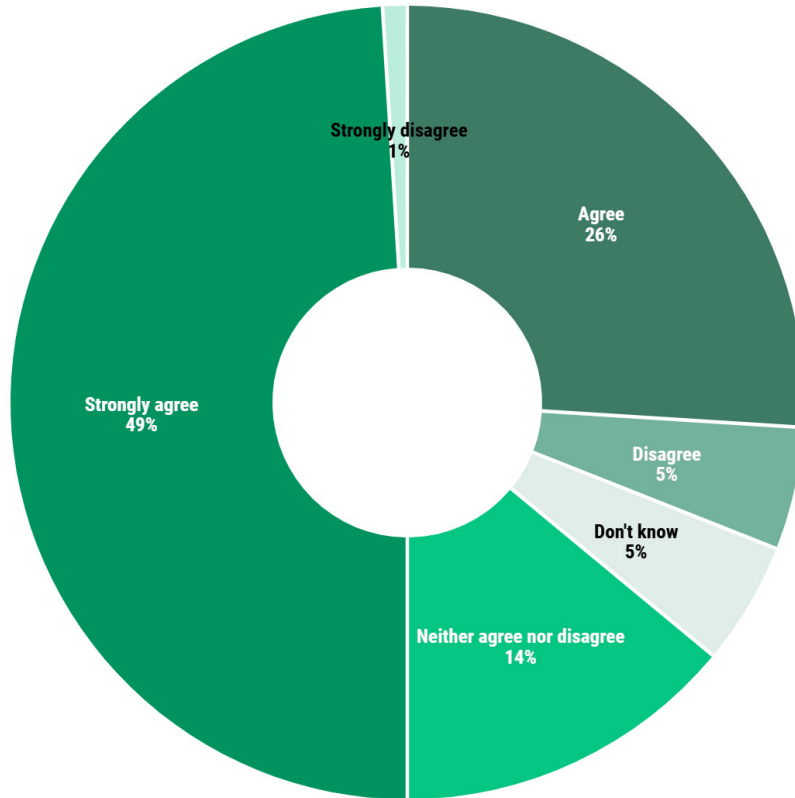
Findings

Full results can be found in Appendix I.

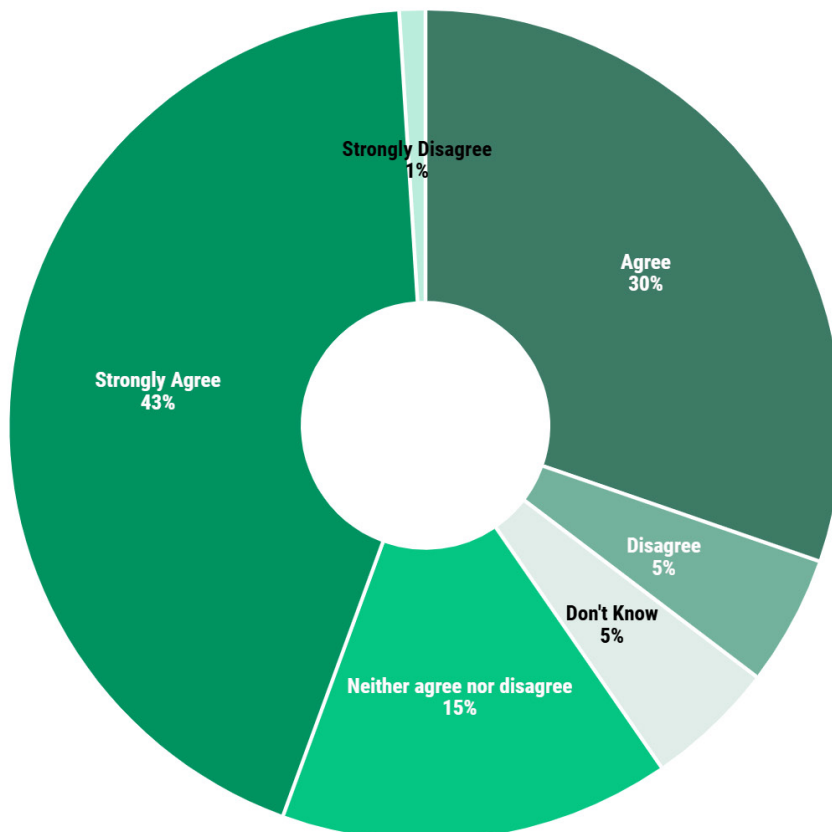
The government should do more to ensure British companies provide a more equitable distribution of pay packages between Chief Executives and average workers.



The gap in pay between average workers and the highest paid executives in the UK is too wide.



Companies should not be increasing the pay of their highest paid executives while the economy is still recovering from the impacts of the pandemic.



Discussion

Overall, the survey revealed a strong and distinct level of dissatisfaction with the status quo on CEO pay. Respondents indicated a high level of concern around pay disparities (Q1), with three quarters (75%) of respondents agreeing that the gap between average workers and the highest paid executives in the UK was too wide, with almost half (49%) saying that they strongly agreed with this statement. There was also a high level of net agreement with statement, “companies that employ large amounts of low paid workers or have employees living in poverty should not be providing excessive pay packages to their highest paid executives” (77% net agreement), and the statement “Government should ensure that companies in receipt of taxpayer money through government contracts do not pay their highest paid executives excessively and should consider withdrawing contracts from companies that pay executives unreasonable amounts” (78% net agreement.)

These results imply that receipt of taxpayer money and the employment of workers on low pay might influence how the public feel about high executive pay in a given company. It is notable that there also seems to be a high level of public concern about disparities in pay more generally, and that concerns around the level of executive pay are not necessarily dependent on these factors. It should be noted that this survey did not seek to establish what the public deem to be ‘excessive’ or ‘unreasonable’ amounts to earn, although previous polling¹¹ conducted by Autonomy and the High Pay Centre found a majority of support for a maximum wage in absolute terms (i.e. not directly pegged to the wages of the lowest paid workers), with 69% of the public supporting maximum wages of either £100,000, £200,00 or £300,000.

With regard to the pandemic, the survey revealed a similar theme. There was a high

level of agreement (77%) with the statement, “companies that have benefited from public support through the COVID-19 pandemic (e.g., the government furlough scheme) should not be increasing the pay of their highest paid executives.” There was a similar (73%) level of agreement with the following, more general, statement, “companies should not be increasing the pay of their highest paid executives while the economy is still recovering from the impacts of the pandemic.”

Again this implies that concern around CEO pay is not conditional on the receipt of public funds. Instead there is a more general concern with fairness and a view that both the economic costs of the pandemic should be distributed fairly, regardless of whether or not a company was directly supported by the taxpayer.

The survey also revealed a high level of support for government action. This included support for the government to generally do more to ensure that the distribution of pay is more equitable (72% net agreement, 41% strongly agree) as well as support for specific action on executive pay, with 61% net agreement with the statement, “If companies will not limit how much they pay their highest paid executives, the government should take action against them.”

There was also strong support for the government to set specific limits on the maximum salary of executives based on how much they are paid in relation to the lowest paid workers (65% net agreement, 38% strongly agree, 12% net disagreement). Perhaps unsurprisingly, this support for government action was matched by a low level of faith in the market to self-regulate. Just under a quarter of respondents (24%) agreed with the statement, “If the pay packages of chief executives are too high then the market will correct itself, governments should not intervene”, compared

11 Autonomy and High Pay Centre (2020) Paying for Covid: capping excessive salaries to save industries, (<https://highpaycentre.org/paying-for-covid-capping-excessive-salaries-to-save-industries/>)

with 44% disagreeing. Respondents' views on the statement, "Businesses should be free to decide the pay of their highest paid executives" were more ambivalent, with 31% net agreement, 35% net disagreement and 28% neither agreeing or disagreeing.

However, there was a higher level of support for the statement, "It's important that businesses offer competitive salaries to chief executives to attract the best talent", with 43% net agreement compared to 20% net disagreement, and 31% neither agreeing or disagreeing.

This implies some level of sympathy with the idea that companies must compete for the best CEOs. Another possible explanation here is the way the issue is framed: when the issue of high pay was framed in terms of competitiveness, respondents seemed more supportive (albeit in a limited way) of the need for it. On the other hand, when the issue of high pay was framed in terms of abstract market mechanisms or the government acting to prevent greater disparities in pay, support for the status quo was generally less pronounced.

Recommendations

- **Companies and investors must exercise restraint this AGM season:** In the short term, it is clear that companies do not have public support to increase the pay of their highest paid executives while the UK is still recovering from the economic shock of the pandemic.
- **Companies need to be aware of the broader economic context in which they operate:** after two years where many have faced huge personal and financial loss, and with rapidly rising inflation already squeezing the incomes of workers across the country, remuneration committees need to exercise an even greater degree of discretion on CEO pay this year, and avoid any suggestion that pay packages this year should ‘make up’ for the last two years. Investors too need to be proactive and work collaboratively to force low votes (<80% approval) on say on pay resolutions at problematic companies.
- **Companies should move to reform their pay practices:** The survey results presented in this briefing demonstrate that concern around executive pay is not limited to the pandemic, or issues of low pay or receipt of taxpayer money. Instead there is a clear sense that the public is concerned with large disparities in pay between executives and average workers. Ultimately, the culture and mechanisms underpinning CEO pay need to change, beginning with a move away from the fallacy of alignment between shareholders and directors. Some of these steps can be taken unilaterally by companies. These actions should be guided by the principles set out by PIRC in its Pay for a New World¹² consultation, which include: a going true market salary, director service contracts approved by vote, a single profit pool to be distributed company-wide, exceptional bonuses only, and the ending of LTIPs.
- **The government should consider regulation on executive pay, but it must not repeat the mistakes of the past:** Regulatory action will be needed to truly address the issue of executive pay, and it is clear that the public is in favour of action that targets executive pay as well as pay disparities generally. The government should learn from previous attempts at regulating executive pay, which have been predicated on the idea that investors would take active stewardship roles. One option would be to follow the example of “Excessive CEO Pay Taxes” at the city level in the United States by penalising excessive executive compensation through a surcharge on corporation tax linked to the ratio between chief executive pay and the pay of the lowest or average worker.
- **In the long term, deeper structural change by companies is needed:** It is unlikely that this kind of reform on its own will be enough to rein in executive pay. Instead, action should be taken to end the era of ‘shareholder primacy’, which has transformed the corporation from an institution focussed on production to an engine of wealth extraction and inequality which has occurred over the past 40 years. Rewriting s172 of the Companies Act, which acts as the legal underpinning of shareholder primacy in UK law, would be a first step towards this. More broadly, moves should be made to democratise companies, such as having substantial portions of corporate boards elected by the workforce, the introduction of sectoral collective bargaining, extending the economic franchise to workers by allowing them to become members of their companies and mandatory profit sharing.

Appendix I: Full Survey Results

To what extent do you agree or disagree with the following statements?

Strongly Agree Agree Neither agree nor disagree Disagree Strongly Disagree Don't Know



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