high pay centre

TOP TO BOTTOM

UNDERSTANDING FAIRER PAY

About the High Pay Centre

The High Pay Centre is an independent non-party think tank established to monitor pay at the top of the income distribution and set out a road map towards better business and economic success. We aim to produce high-quality research and develop a greater understanding of top rewards, company accountability and business performance. We will communicate evidence for change to policymakers, companies and other interested parties to build a consensus for business renewal.

The High Pay Centre is resolutely independent and strictly non-partisan. It is increasingly clear that there has been a policy and market failure in relation to pay at the top of companies and the structures of business over a period of years under all governments. It is now essential to persuade all parties that there is a better way.

The High Pay Centre is grateful to its supporters and to the Barrow Cadbury Trust for funding this work.

@highpaycentre
www.highpaycentre.org

The analysis in this report was carried out by Landman Economics for the High Pay Centre.

Contents

Foreword

" A more equal distribution of income allows for more economic stability, more sustained economic growth and healthier societies with stronger bonds of cohesion and trust." [1]

Christine Lagarde, head of the IMF.

Inequality is the scourge of our modern economy and society. A wide gap has opened up between pay at the very top of the income scale and the bottom in the past 30 years.

Those on middle and low incomes have seen their pay barely keep up with prices in the past decade. While inflation is up 45 per cent, average wages have risen by just 51 per cent during this period. At the same time, pay for top executives has trebled from £1.5 million to a staggering £4.8 million.

Pervasive low pay and the gap between top and bottom demands we ask questions about inequality and the level that can be tolerated in a fair society. Government is forced to subsidise low pay so that those at the bottom of the income scale can make ends meet.

But is it right that taxpayers should support low-paying employers who continue to channel huge rewards to the executives in charge?

Wage stagnation for most of the workforce has also drained spending power out of the economy, making it difficult to return to growth.

Public concern over inequality is expressed in an outcry over bankers' bonuses and widespread criticism of executive pay. But if as a society, we are really concerned about the growing gap between top and bottom pay; between rich and poor, there are things we can do about it.

Redistribution is not a topic that gets much focus. However, without a conscious effort to ameliorate the impact of our extreme form of market capitalism, there will be big winners and losers. Should we as a society help those who lose out?

Many people believe we should have a fairer income distribution that does not channel all of the rewards to those at the very top. But what would this look like and how could it be achieved?

In this report, we are exploring a shift of small amounts between pay bands that would help those on the lowest incomes. Could those in the top 1 per cent forego 10 per cent of their income to help those at the bottom of the income distribution.

While wages have stagnated for the low-paid, they have also seen their bills rise faster than those on higher salaries as inflation for staples and fuel has increased much faster than for other items.

In the UK, one in five workers is paid less than two-thirds the median wage (below £7.49 an hour or £13,600 for full-time work) compared to one in ten in some other European countries. The taxpayer helps support this by transferring about £4 billion in in-work cash transfers, according to the Commission on Living Standards.[2]

When the economy is in such poor shape the fact that that those at the very bottom of the income scale are bearing the brunt of the cutbacks - while those at the top are mostly spared - becomes corrosive.

This report is an attempt to understand how we could create a fairer income distribution. We are talking about shifting a small amount from top pay bands that would make a big impact at the bottom. Could those on the very top incomes give up a month's salary to help those on the bottom? Would they miss it?

[1] http://www.guardian.co.uk/business/2013/jan/23/imf-world-growth-forecast-davos?

[2] http://livingstandards.org/final-report/gaining-from-growth-a4.pdf

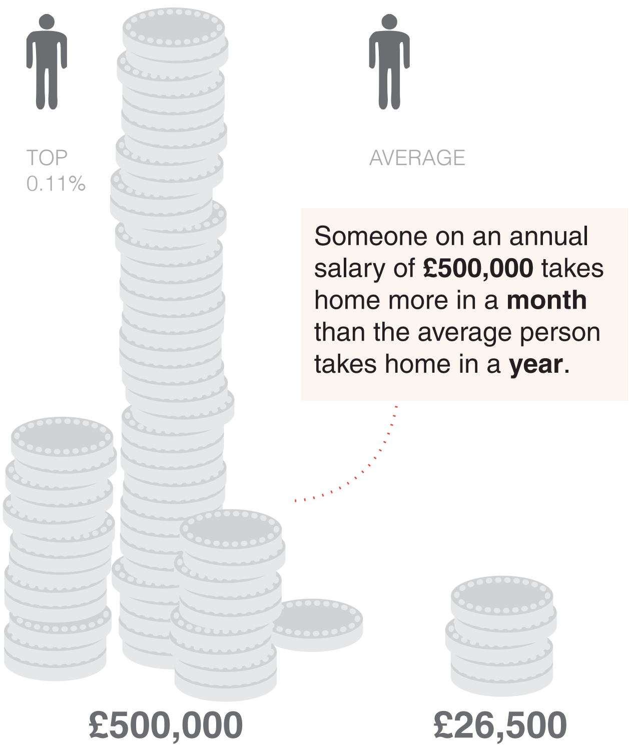
Executive summary

Inequality has risen sharply in Britain in the past 30 years. We have now returned to levels of income inequality last seen in the 1930s. The share of the national income going to the top 1 per cent has more than doubled since 1979 to 14.5 per cent from 6 per cent.[3]

Huge disparities have opened up between pay at the very top of the income scale and pay at the bottom, yet the government is giving a tax break to top earners with the abolition of the 50p top rate of tax. This has infringed any sense of fairness in pay.

[3] High Pay Centre calculation

figure 1 **Top to middle: high earners tower over the average**



Some 26,000 people earning £500,000 or more take home more in a month (£21,500) than those on average salaries earn in a year (£20,500 after tax). Yet our figures show that there are 6.75 million workers earning less than £800 a month.

Taxpayers subsidise low-paying employers to the tune of £4 billion with in-work cash transfers a year.

A fairer distribution of pay could mean looking for a sacrifice on the part of top earners to distribute directly to those on low incomes. A 10 per cent redistribution from those earning more than £300,000 a year (the top 0.25 per cent), for example, would give a pay rise of £40 a month to the lowest paid 25 per cent of the income scale.

The bottom 25 per cent of earners would get a 55p per hour increase in their hourly pay taking it from £6.80 to £7.35, approaching the national living wage of £7.45, if those earning more than £150,000 (the top 0.9 per cent) took a 10 per cent pay cut.

Boosting incomes lower down the pay scale, would inject more spending into the economy. Smaller pay gaps also improve the way businesses function, improving employee engagement and public trust in companies.

Reducing pay inequality, even in this small way can help bring growth back to the economy through increases in spending power at the bottom.

Introduction

Pay at the top continues its meteoric rise, as the rest of the workforce experiences stagnation and decline. Wage increases for those on middle incomes have barely outpaced rising prices over the past 10 years. For those at the bottom, the picture is bleak. Welfare benefits that over the past 10 years have increasingly been used to top-up low wages are being cut and it is hard to see a rise in living standards for most.

Such wage stagnation has a knock-on effect, limiting spending power for those in the middle and bottom of the income distribution, reducing incentives to work and damaging support for businesses.

Income inequality has now returned to the levels experienced before the great depression of the 1930s. The trend towards a more equal society that we saw in the decades after the Second World War has been reversed. CEO pay packets increased by only 0.8 per cent a year between the late 1940s and 1970s, falling behind inflation, as the rest of society caught up, likewise, finance lost much of its wage premium. By the 1970s, our society was the most equal it had ever been.

> In 1979 the top 0.1 per cent took home 1.3 per cent of the national income; by 2007 this had grown to 6.5 per cent.[4]
> The Gini co-efficient, an internationally recognised measure of inequality, was 0.240 in the UK in 1978, since then it has been increasing and in 2010/2011 it was 0.338.[5]

Last year alone, the average FTSE 100 chief executive saw their pay rise by 12 per cent to £4.8m.[6] Meanwhile across the rest of the economy pay stagnated, with a rise of just 2.8 per cent. Indeed only 12 per cent of people experienced a pay rise of 4 per cent or more.[7]

Inequality has different consequences today than it did 40 years ago. But at the bottom of the income spectrum, many live difficult lives in insecure and poorly-paid employment, struggling to make ends meet, as a broken washing machine, or a new school uniform sends monthly expenses off track and can even end in eviction or homelessness.

In 2011, 14 million people were at risk of poverty or social exclusion according to the Office for National Statistics (ONS).[8] The ONS reports that the number of people saying they would be unable to cope with unexpected bills has increased considerably since the start of the financial crisis – up from 26.6 per cent in 2007 to 36.6 per cent. The proportion of people unable to afford one week's annual holiday has also risen from 21.4 per cent to 29.7 per cent.

These lives are all around us, yet too often they are hidden from view. Live in London, or the southeast and you see the reality less. For those at the top, disconnection has become a way of life. They have little contact with the people who make their coffee or clean their offices and homes. One chief executive of a large British company spoke to us of the need for all of those lucky

[4] F Alvaredo et al. (n. d.) The World Top Incomes Database, http://g-mond.parisschoolofeconomics.eu/topincomes.
[5] http://www.ifs.org.uk/bns/bn19figs.xls
[6] MM&K/Manifest (2012) Executive Pay Data. Based on year executive pay packages with year end before March 2012.
[7] Incomes Data Services (2012) Pay Survey
[8] http://www.ons.gov.uk/ons/dcp171776_295020.pdf

enough to be at the top of the pile to volunteer in their local community for them to understand what life at the other end of the spectrum is really like.

Indeed, it is the case that luck has more of a role in our lives than we would often care to admit. While many of us like to think our talent, wit and ingenuity got us where we are today, on careful questioning most admit they have enjoyed a lucky break, while an equally deserving colleague or job applicant was turned away. It was Warren Buffett, legendary investor and one or the richest men in the world, who said;

"Most of the rich people in the United States, and probably the UK too, they would not have done quite as well if they'd been in Bangladesh or some place like that, I mean they think they did it all by themselves but the society has done an awful lot for them… When I was born I was wired in a certain way that works wonderfully in a big capitalist society, it wouldn't have worked so well if I'd been somewhere where they valued physical ability or whatever it may be, ***but I get paid off enormously at no great credit to me I was just lucky at birth****, I shouldn't delude myself into thinking I'm some superior individual."* [9]

The decision by the Conservative and Liberal Democrat Coalition to cap nominal benefit increases at 1 per cent annually will hit all of those at the bottom of the pile, in work or out of it. It has been estimated by the IFS that seven million families with a member who is working I will be affected by this cap.[10]

Yet the logic is hard to deny, is it right that the government subsidises low-paying companies, businesses who decline to offer their staff a living wage, who refuse to invest in their employees? But, nor is it right that those who did not contribute to the financial crisis bear the brunt of the pain, nor that those whose lives are most precarious are most badly affected by austerity measures. Fairness is an important issue in pay and yet many people would say that Britain's current wide disparities in income are patently not fair.

For this reason, we ask whether the subsidy for businesses paying low wages could be reduced if we had a more even distribution of wages, and what this would look like. Asking simply this, what would a 10 per cent cut for those in the top 1 per cent mean if it went directly into the pockets of those at the bottom?

It is not a call for an industrial wage policy, employers need to retain flexibility over pay and it is not the place of government to dictate to business how much they should pay their staff. But the current market is rigged, it has been hijacked by those at the top; even as globalisation is blamed for wage suppression at the bottom, so too is it the given reason for wage inflation at the top.

Central to this are bigger questions about how our economy works and how we want it to work. How oligopolies have developed in major areas of our economy. Who does business have a responsibility to? And why ever larger rewards are required to generate performance from individuals at the top of companies whose predecessors but a generation ago, did the job for a 10th of the pay?

We call this project a "numbers exercise" as the difficult reality is that there is no magic button that would bring about this change. Over the medium term it means stronger trade unions or other forms of workplace democracy, it means a new understanding of in whose interests companies serve, and a longer term approach by our business leaders.

So what about right now? Right now it means business leaders taking a pay cut, and refusing their bonuses. It also means shareholders taking a stand, as they did last year and becoming more critical of companies where huge pay gaps exist between top and bottom. For the government it means making the issue of fair pay at the top and the bottom a central pledge in the Budget, and reinstating the 50p tax rate, only in this way can we be seen as "all in it together".

What is the Gini Co-efficient?

It is a measurement of the income distribution in a country. The range is between 0 and 1 and is based on residents' net income, where 0 represents all income distributed exactly equally between all citizens, and 1 represents all income in the hands of one individual.

[9] http://www.youtube.comwatch?v=uZTweMHEFAI
[10] http://www.independent.co.uk/news/uk/politics/benefits-cap-seven-million-families-hit-8441819.html

What does inequality look like now?

We live in an unequal society. Yet it is always surprising to find out how unequal we really are.

Most of us like to think our society is more equal that it really is, those at the top over-estimate average wages and the pay of those at the bottom, while those in the middle often fail to recognise just what being at the top means and what they really get paid.

What the top thinks:

Research by Ipsos MORI in 2008 among high earners highlighted that they put themselves nearer the middle of the income spectrum than they really were.[11]

As table 1 demonstrates those at the top and the general public experience a significant disconnect when it comes to estimating what being a 'High Earner' really means. Those earning over £200,000 per year estimated that a high earner would be someone on over £100,000, while the general public describes anyone on over £35,000 as a high earner.

In 2011, Ipsos Mori looked at opinions on what being a low earner means, asking how much a person could earn and still be on a low wage: the public said £11,000 while high earners (those on over £100,000) estimated between £12,000-£20,000.[12]

What everyone else thinks:

In polling, the general public consistently underestimates what is earned by top earners. Only 9 per cent of people correctly estimated that the average FTSE 100 CEO would be on more than £4 million per year.[13]

Even with this misperception:
> According to the British Social Attitudes Survey, 59 per cent agree or strongly agree that ordinary working people do not get their fair share of the nation's wealth, with only 14 per cent disagreeing or strongly disagreeing; and
> 73 per cent agree or strongly agree that differences in income in Britain are too large. Only 8 per cent disagree or strongly disagree.

[11] ibid
[12] ibid
[13] Survey conducted for the High Pay Centre by ICM Research Jan 2012

The real picture… What is the current state of inequality?

> Between 1997 and 2007/8 income for the top 0.1 per cent of the income distribution grew by 64.2 per cent, while the income of a person in the 50th percentile (the middle) only increased by 7.2 per cent over the same period.[15]

> The share of national income going to the top 1 per cent of the income scale has more than doubled since 1979 to roughly 14.5 per cent in 2011 from 6 per cent in 1979.[16]

> There are 26,000 people in the UK earning more than £500,000 a year with a take-home pay of £21,500 a month – more than the average annual take-home which is £20,212.[17]

> Britain has some 6.75 million workers who earn less than £800 a month after tax.

> The government is about to give a tax break to the 219,000 people who earn more than £150,000 by abolishing the 50p top rate of tax. At the same time, it is capping benefit rises for those at the bottom of the income scale.

> The cut from 50p to 45p in the top rate of tax will hand a tax break of between £1 billion and £2.7 billion to the highest-paid 0.9 per cent of the pay scale.

> Taxpayers subsidise low-paying employers to the tune of about £4 billion in in-work cash transfers.[18]

table 1 **How Much Does A Single Person Have To Earn To Be A 'High Earner'?** [14]

Wage bracket	What makes a high earner
£200K+ earners 2011	£100,000
£100-£200K+earners 2011	£55,000
General public 2008	£35,000

[14] High Pay Commission (2011) Just Deserts
[15] High Pay Commission (2011) Interim Report
[16] High Pay Centre calculation
[17] High Pay Centre calculation
[18] http://www.living-standards.org/

A step towards a more equal society?

This paper is modelling an example of what a fairer pay scale would look like. It looks at the impact of a modest cut in pay at the very top if it were transferred to those at the bottom. It calculates what would happen if all those at the top of the income scale (the top 1 per cent) took a 10 per cent pay cut and all those at the bottom got the money directly in their pocket.

Health warning!

With any research of this kind, there are holes. No economic model can fill in all the gaps even Treasury modelling is based on estimates and assumptions, but where the gaps are significant we have flagged them up. Equally there are always going to be factors which we think will have an effect but we are unable to anticipate precisely the extent, again when this happens we point it out. It is important to understand that this is based on theoretical ideas and so shouldn't be seen as being possible to recreate in the real world, but it does provide a jumping off point, a discussion piece and an idea of what a more equal society would mean for the top and the bottom.

A re-distribution like this would result in a boost for all of those at the bottom of the income spectrum, which would include second earners in families, bringing much needed relief for increasingly stretched household budgets.

Key findings:

> A **10 per cent pay cut on those earning over £300,000 gross** would mean that all those in the bottom 25 per cent (6.75 million people) of earners, i.e. **those on less than £226 per week would get a £10.13 (before tax) boost each week.**

> Those in the **bottom 25 per cent of earners would get a 55p** increase in their hourly pay taking it f**rom £6.80 to £7.35 on average** if people on over **£150,000 took a 10 per cent pay cut**. This would bring them closer to the national living wage of £7.45 an hour outside London.

> A 1**0 per cent pay cut for those on £500,000** and more could mean a 22p an hour increase for the bottom **25 per cent on average this would mean an increase from £6.80 to £7.02 gross.**

What about cost?

It is right at this point to note that our analysis has demonstrated that this sort of redistribution would not come without a fiscal cost, it would in the short term have an impact on the government's tax revenue. This is because the money saved in reduced benefits, and increased through higher tax revenues at the bottom, does not quite equal the tax revenues lost by the cut in pay at the top: it is not fiscally neutral.

Depending on the type of redistribution, the shortfall varies from just over £2bn, to £0.22bn (as can be seen in tables 6 and 7). With any estimate or calculation of this kind there are holes, this analysis does not cover everything. For example, this analysis on cost does not include the increased economic boost that might occur if those at the bottom increased their spending, nor does it include the increased tax revenues from that spending from VAT receipts, nor indeed does it include the savings the government might make in reduced tax relief on lower pensions savings by those at the very top.

It is also arguable that this short term fiscal cost would be made up both through greater labour market participation, encouraged by higher wages and higher spending at the bottom of the income spectrum.[19] Indeed the economic boost of higher spending power at the bottom on the productive economy could mitigate any loss to the Treasury over the short to medium term. But it is not built into the model so it is not possible to be certain.

Alternatively, it is arguable that any immediate shortfall would be covered if the government did not scrap the 50p tax rate on those earning over £150,000. How much exactly this would raise is deeply contentious. Original estimates from the Treasury put it at £2.7bn, and while that has now been revised down, the new calculations have been extensively critiqued.

Fairness is often bandied around as a desirable thing, something no-one can really object to like motherhood and apple pie, but in reality a fairer pay economy will not be achieved without political risks, and bold business decisions.

Main breadwinner or second earner?

When we look at the breakdown of the figures it is very clear that this change would in large part positively affect dual earner families, over 30 per cent of each low income earner measurement are second earners, ie they are in a dual income household and are the lowest earner. Any change in their pay will not just affect the very lowest household in terms of income, but would have a positive impact on second earner families.[20]

Is the Gini back in the bottle?

These figures show that while this shift would have a positive impact on nearly 6.5m (for the bottom 25 per cent) people or 2.5 million (for the bottom 10 per cent) its impact on the Gini-coefficent would be small.

Even the maximum reduction in the Gini coefficient resulting from any of the redistributions modelled here – a reduction of around 0.004 – would take the Gini coefficient down to about 0.348. The data on Households Below Average Income for the most recent available year (2010-11) show that the Gini coefficient declined from 0.357 to 0.338 (a level well below 0.348) but this was mainly to do with falling net incomes in the aftermath of the 2008-09 recession. Prior to this, a Gini below 0.35 was last achieved in 2005-06.

[19] K Dynan, J Skinner and S Zeldes (2004) "Do the rich save more?" Journal of Political Economy, vol 112 no 2, pp397-444;
[20] We have not included the analysis on second earners in this report to assist with clarity. If you are interested we can provide it as a separate document.

The Analysis

What is a high earner?

In this analysis, we explore five different definitions of "top earners". These are based on HMRC statistics on the number of individual employees with incomes from employment [21] over the cut off points listed:

a) £150,000 per year;
b) £200,000 per year;
c) £300,000 per year;
d) £500,000 per year;
e) £1,000,000 per year.

Defining the 'low paid'

To define those on "low pay" we use the most recent data available namely the 2010-11 Family Resources Survey (FRS). Creating four different definitions:

1. The lowest paid quartile (25%) by hourly wage – less than £6.80 per hour in the 2010-11 FRS;
2. The lowest paid quartile (25%) by weekly wage – less than £226 per week in the 2010-11 FRS;
3. The lowest paid decile (10%) by hourly wage – less than £5.07 per hour in the 2010-11 FRS; [23]
4. The lowest paid decile (10%) by weekly wage – less than £106 per week in the 2010-11 FRS.

table 2 **The number of taxpayers above each of the top cut off points, total earnings and average earnings.[22]**

(£/year)	Number of taxpayers above cut-off (1000s	As % of all taxpayers	Total earnings above cut-off (£m)	Average earnings above cut-off (£m)
150,000	219	0.91%	59,900	271,795
200,000	124	0.52%	46,900	375,065
300,000	61	0.25%	34,800	564,131
500,000	26	0.11%	24,000	906,231
1,000,000	8	0.03%	14,200	1,710,000

[21] This analysis does not include income from investments.
[22] HMRC Income Tax Statistics for 2010-11, Table 3.6 (published December 2012)
[23] Note: hourly wage figure seems low given that it is below the 2010-11 National Minimum Wage level. As the 'weekly earnings' variable and the 'total hours worked' variable in= the FRS do not always refer to the same week, weekly earnings tend to have a wider variance in the FRS than in other datasets. However it is used here as in general, the weekly earnings measure in FRS is more reliable than the hourly earnings measure.

How many people?

The total estimated number of employees in the 2010-11 FRS is equivalent to nearly 25 million people across the UK as a whole. This means that:

> for low-paid measures (1) and (2), around 6.75 million workers are receiving a gross wage increase as a result of this redistribution, (around 5 million of these are full-time workers) and

> for low-paid measures (3) and (4), around 2.5 million workers are receiving a gross wage increase.

table 2b

Group	Average weekly wage, 2010-11 FRS
Whole sample	£474.88
Low paid group 1: lowest paid quartile by hourly wage	£154.63
Low paid group 2: lowest paid quartile by weekly wage	£120.30
Low paid group 3: lowest paid decile by hourly wage	£97.21
Low paid group 4: lowest paid decile by weekly wage	£55.07
Lowest paid quartile by weekly wage: full-time workers only	£220.17
Lowest paid decile by weekly wage: full-time workers only	£148.28

table 3 **Increase in wages for each low-paid employee, based on the six different high-income cut-off points above.[24]**

Those earning over (£/year)	Increases in gross wages for low earners that can be financed by 10% reduction in gross earnings for high earners above cut-off point			
	Increase in hourly wage for lowest 25% of hourly wage earners	Increase in weekly wage for lowest 25% of weekly wage earners	Increase in hourly wage for lowest 10% of hourly wage earners	Increase in weekly wage for lowest 10% of weekly wage earners
150,000	£0.55	£17.44	£1.39	£43.53
200,000	£0.43	£13.65	£1.09	£34.08
300,000	£0.32	£10.13	£0.81	£25.29
500,000	£0.22	£6.99	£0.56	£17.44
1,000,000	£0.13	£4.13	£0.33	£10.32

[24] For the low pay definitions based on the hourly wage (1 and 3 above) the reduction in gross pay for high earners is reallocated to low earners by increasing the hourly wage of each low-paid employee by a set amount, while for the low pay definitions based on the weekly wage (2 and 4 above) the reduction in gross pay for high earners is reallocated to low earners by increasing the weekly wage of each low-paid employee by a fixed amount.
The 2008-09 FRS is used rather than the 2010-11 FRS (which is the most recent data at the time of writing) because the ippr tax-benefit model (which is used to calculate the increase in net incomes for low-paid workers arising from the redistribution.

Understanding the results [25]

The tables below show

1. The total amount redistributed from high-paid to low-paid workers in £billion;
2. The total increase in net, after tax/benefit, incomes for low-paid workers in £billion;
3. The average marginal deduction rate (MDR) for low-paid employees who benefit from the redistribution. For example, if this figure is 39% then for each extra pound of gross earnings, the low-paid employees get (100-39) = 61 pence of take-home pay;
4. The total amount of increased tax/reduced benefits payments for low-paid workers (this is equal to the total amount of redistribution minus the total increase in net incomes;) [26]
5. The total amount of reduced tax on high-paid workers whose gross earnings have been reduced by 10 per cent;
6. The overall fiscal impact of the redistribution on the public finances (a negative number here indicates that the Exchequer loses money overall;
7. The new Gini coefficient on household net incomes after redistribution;
8. The change in the Gini coefficient compared with the actual Gini coefficient for the 2008-09 HBAI data (which was 0.3515).

[25] For further explanation of the results see annex 1.
[26] Note that this figure includes additional employer NICs accruing to the government from higher pay for the low paid workers, whereas the MDR figure above does not

table 4 **Results: redistribution to lowest 25% of employees by hourly earnings.**

Those earning over (£/year)	Total gross redistribution high-paid to low-paid (£bn)	Increase in net incomes for low paid (£bn)	Average MDR for low-paid	Increased tax/reduced benefits from low paid (£bn)	Reduced taxes on high-paid (£bn)	Overall fiscal impact (£bn)	New Gini coefficient	Reduction in Gini
150,000	5.99	3.71	38.1%	3.14	3.94	-0.80	0.3492	-0.0023
200,000	4.69	2.19	37.1%	2.42	3.09	-0.67	0.3497	-0.0018
300,000	3.48	2.03	37.1%	1.79	2.29	-0.50	0.3503	-0.0012
500,000	2.40	1.48	38.3%	1.25	1.58	-0.33	0.3509	-0.0006
1,000,000	1.42	0.91	36.1%	0.71	0.93	-0.22	0.3511	-0.0004

table 5 **Results: redistribution to lowest 25% of employees by weekly earnings.**

Those earning over (£/year)	Total gross redistribution high-paid to low-paid (£bn)	Increase in net incomes for low paid (£bn)	Average MDR for low-paid	Increased tax/reduced benefits from low paid (£bn)	Reduced taxes on high-paid (£bn)	Overall fiscal impact (£bn)	New Gini coefficient	Reduction in Gini
150,000	5.99	3.83	36.1%	2.82	3.94	-1.12	0.3490	-0.0025
200,000	4.69	3.01	35.8%	2.19	3.09	-0.90	0.3495	-0.0020
300,000	3.48	2.24	35.6%	1.61	2.29	-0.68	0.3502	-0.0013
500,000	2.40	1.55	35.4%	1.10	1.58	-0.48	0.3508	-0.0007
1,000,000	1.42	0.92	34.9%	0.64	0.93	-0.29	0.3512	-0.0003

table 6 **Results: redistribution to lowest 10% of employees by hourly earnings.**

Those earning over (£/year)	Total gross redistribution high-paid to low-paid (£bn)	Increase in net incomes for low paid (£bn)	Average MDR for low-paid	Increased tax/reduced benefits from low paid (£bn)	Reduced taxes on high-paid (£bn)	Overall fiscal impact (£bn)	New Gini coefficient	Reduction in Gini
150,000	5.99	3.97	33.7%	2.69	3.94	-1.25	0.3488	-0.0027
200,000	4.69	3.12	33.5%	2.07	3.09	-1.02	0.3495	-0.0020
300,000	3.48	2.36	32.2%	1.48	2.29	-0.81	0.3500	-0.0015
500,000	2.40	1.66	30.8%	0.98	1.58	-0.60	0.3507	-0.0008
1,000,000	1.42	1.00	29.6%	0.55	0.93	-0.38	0.3510	-0.0005

table 7 **Results: redistribution to lowest 10% of employees by weekly earnings8**

Those earning over (£/year)	Total gross redistribution high-paid to low-paid (£bn)	Increase in net incomes for low paid (£bn)	Average MDR for low-paid	Increased tax/reduced benefits from low paid (£bn)	Reduced taxes on high-paid (£bn)	Overall fiscal impact (£bn)	New Gini coefficient	Reduction in Gini
150,000	5.99	4.35	27.4%	1.76	3.94	-2.18	0.3485	-0.0030
200,000	4.69	3.43	26.9%	1.31	3.09	-1.78	0.3491	-0.0024
300,000	3.48	2.56	26.4%	0.93	2.29	-1.36	0.3499	-0.0016
500,000	2.40	1.77	26.3%	0.63	1.58	-0.95	0.3505	-0.0010
1,000,000	1.42	1.06	25.4%	0.36	0.93	-0.57	0.3509	-0.0006

Why make the change?

There is a well-recognised business and economic case for a fairer pay system.

1. The government could stop subsidising low wage employers

The welfare system was always intended for those who fell upon hard times, to act as a safety net. Now too often it is just a safety net for businesses, subsidising the low wage economy. The changes in the welfare system that included Working Family Tax Credits are part of a range of policies that attempt to "make work pay". A redistribution in terms of pay could see an end to the need for government to provide so much subsidy for pay at the bottom.[27]

2. Those at the bottom spend and those at the top save

Spending patterns vary across the income spectrum. Those at the bottom of the income spectrum spend a larger percentage of their income in the so-called productive economy, namely buying food, goods, and other products along with services including health, utilities and education services.[28]

Those at the top save a larger percentage of their income investing it often in safe assets like pension wealth and most notably the housing market. Higher income earners, who are more likely to own their own homes, spend a larger percentage of their money on mortgage interest, and property than lower income earners.[29]

Redistributing incomes could result in a higher percentage spend on the productive economy.

3. Reduce social fallout of inequality

Inequality has social as well as economic effects. It has a big impact on community cohesion, and when it reaches extreme levels it creates social unrest, when those at the bottom no longer feel like they have a stake in society they are encouraged to pursue their economic objectives outside of the mainstream.[30] As such reducing inequality has positive social effects.

4. Improved employee engagement

Lower pay gaps within businesses contribute to greater employee engagement. Employee engagement is associated with:
> High levels of productivity;
> Lower levels of employee absenteeism;

In a global survey of executives, 84 per cent said that 'disengaged employees' are one of the three biggest threats facing their business.[31]

5. Greater public support for business

Trust in business is considered by most business leaders to be central to reputation and company longevity. Studies show that wage inequality within companies has a negative effect on public opinions of business and excessive executive rewards are seen as a significant factor in determining attitudes towards business.

[27] Reamonn Lydon & Ian Walker (2004) Welfare-to-Work, Wages and Wage Growth, IFS
[28] Peter Levell & Zoe Oldfield (2011)The spending patterns and inflation experience of low-income households over the past decade
[29] Catherine Ruetschlin (2012) Retail's Hidden Potential: How Raising Wages Would Benefit Workers, the Industry and the Overall Economy; The Psychology Of Poverty http://www.investopedia.com/financial-edge/1012/the-psychology-of-poverty.aspx#ixzz2J4UA01DQ
[30] High Pay Commission (2012) Cheques with Balances
[31] Economist Intelligence Unit (2010) Re-engaging With Engagement: views from the boardroom on employee engagement, www.businessresearch.eiu.com/sites/business-research.eiu.com/files/LON%20-%20PL%20-%20Hay%20report_WEB.pdf.

In the UK, the number of people who trust in businesses to do the right thing fell to 38 per cent in 2012 – fifth lowest level among 25 countries polled.[32]

Equally, when rewards for company bosses go beyond their apparent contribution to the success or welfare of the company, it damages trust and adds to a growing public attitude that business leaders are 'in it for themselves'.[33]

Conclusion

A fairer pay economy should be a priority for any government.
It is good for the economy and for business.

Even a small pay cut to those at the very top of the income scale of just 10 per cent can make a difference. It would not only boost those on the very margins of the working economy, but would also help second earners in families boosting household incomes when it is needed most.

[32] Edelman Trust Barometer
[33] R. Thompson (2009) 'Excessive executive pay – what's the solution?', Harvard Business School; K O'Hanson, 'Public trust in business', Santa Clara University.

Annex 1

The key points are as follows:

> Depending on the particular measure of low pay used, low-paid workers get between 62 pence and 75 pence of any increase in gross earnings as net income. It is important to bear in mind that this is an average figure, and for some low-paid workers (e.g. those on the taper for tax credits, Housing Benefit/Council Tax Benefit etc.) the marginal deduction rate will be much higher than this. Conversely, for other low-paid workers (e.g. low-paid second earners in families with a high-paid primary earner) the MDR will be zero up to the income tax personal allowance level in many cases.

> The overall marginal tax rate for high-paid workers (above £150,000 per year) is currently 52% - this means that a redistribution for high-paid to low-paid workers costs the Exchequer because the MDR on additional income for low-paid workers is lower than the MDR on the reduced income for high-paid workers. On top of this, the Exchequer also loses a further 13.8% in reduced employer NICs for high-paid workers which it does not fully recoup on low-paid workers (because some of them are below the weekly pay threshold for employer NICs). This is reflected in the "Overall fiscal impact" column of each Table.

> The reduction in the Gini coefficient is relatively small – a maximum of 0.0037 (just over a third of a percentage point) in the top row of Table 5. This is partly because we are only reducing top earnings by 10% - we would expect a proportionately bigger result if top earnings were reduced by a larger percentage (e.g. 30%). Also, the amount of gross income being redistributed (amounts ranging from £1.4bn to £8.5 bn depending on which high earner cut-off point is used) is relatively small compared with total gross income from employment of around £640bn. Thus, it is not surprising that the effect of the Gini coefficient for net incomes is relatively small.