FTSE 100 CEO pay briefing 2013 – Have new rules on top pay had any impact?

Background

- Pay of top executives in the UK has become a controversial political issue, particularly in the aftermath of the 2008-09 recession. The average FTSE 100 Chief Executive was paid £4.3 million in 2012, nearly double the amount they received in 2002. Over the same period, the average UK worker did not experience a real terms pay-rise at all. CEOs are now paid around 160 times the average worker. In 1998 it was about fifty times. In the early 1980s pay packages around 15 or 20 times the average were common-place. *Capital in the Twenty-First Century*, the best-selling book by economist Thomas Piketty, highlights the growth in pay of so-called 'super-managers' as a key contributor to the pay gap between the super-rich and everybody else that has widened since the early 1980s

- *The Business Enterprise and Regulatory Reform Act (2013)* together with the *Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013* introduced new requirements for the setting and reporting of executive pay. Companies must now publish a 'single figure' for the total remuneration awarded to their CEO, and compare it with the figure awarded for the previous year. The increase in pay (excluding so-called Long-Term Incentive Plans) should be compared to the percentage increase awarded to all company employees. Future pay policy is now subject to a binding shareholder vote, to be held at least every three years, while the amount awarded for the current year remains subject to an advisory vote

- This briefing analyses CEO pay from 2012 and 2013 at companies whose most recent financial year end fell between 30 September 2013 and 31 December 2013 – these 67 companies are the first to report pay packages subject to the new regulations. We have also looked at how companies complied with the requirement to compare the increase in pay for their CEO with that experienced by their workforce as a whole.

- A number of caveats apply: The figures we have used are those published by the companies themselves in their annual reports. Some of the figures declared for 2012 differ from those reported by independent analysts and the media. Equally, some companies have declared pay in different currencies (we have calculated the sterling equivalent based on exchange rates in April 2014 when the research was being carried out). Finally, some firms changed CEO over the course of the 2012-13 period analysed – where these changes occurred mid-year, the figure represents aggregate pay received by both CEOs where companies have provided details. Comparisons between incoming CEOs and their predecessors are slightly flawed - one would expect the incoming CEO to receive a lower pay package than their predecessor because the various incentives and share awards handed out by most FTSE 100 companies accumulate over a period of years. Nonetheless, the figures for the index as a whole should provide a useful insight into levels of CEO pay and the effect of the new regulations.

Findings

- Average CEO pay for the companies analysed in 2013 stood at £4.5 million – this represents an increase of around 5% compared to the FTSE 100 average of £4.3 million recorded by Manifest/MM&K in 2012.

- Looking at pay in 2012 for just those firms analysed as part of our research, there is actually a fall in average CEO pay from £4.9 million in 2012 to £4.5 million in 2013. However, this average is skewed by one significant outlier, Melrose Industries, who record a pay package of £31 million in 2012 falling to just £900,000 in 2013 for CEO Simon Peckham. This would have made Peckham comfortably the best-paid CEO in the UK, with more than double the pay of the next best executive (Angela Ahrendts of Burberry). Yet Manifest/MM&K's independent analysis did not put Peckham in the top 5. With Melrose removed from the sample, average CEO pay remains constant, with an average of £4.5 million in both 2012 and 2013.

- Median pay for CEOs stood at £3.9 million in 2013, a small increase from the median of £3.8 million in 2012 (Manifest/MM&K calculated a median figure of around £3.7 million for the whole FTSE 100 in 2012).

- Removing the top five and bottom five for each year to eliminate anomalous outliers does not significantly alter the picture – average pay in 2013 decreased slightly to £4.1 million from £4.2 million using this method.

- The highest paid CEO in 2013 – by some distance – was Martin Sorrell of WPP who was paid just under £30 million last year, compared to £17.5 million in 2012. Sorrell was paid over £78 million between 2009 and 2013. After Sorrell, Peter Long of TUI Travel, paid £10.1 million, was the highest paid in 2013

- Looking at companies' future policy, the average pay expected for 'on target' performance in 2014 was £3.4 million (median, £3.1 million). For maximum performance, the average was £5.8 million (median £4.9 million). The highest pay package awarded for target performance, together with Sir Martin Sorrell, was Stuart Gulliver of HSBC - both around £7.8 million. For maximum performance, Sorrell will be paid £19.3 million, ahead of the next best-paid CEO, Rakesh Kapoor of Reckitt Benckiser, on £18.3 million

- Though companies have complied with the letter of the requirement to compare pay increases for their CEO with that of their workforce, many have not adhered to the spirit of the regulation. The law permits companies to choose a smaller comparator group, if they feel this is more appropriate. TUI Travel exploit this clause to compare CEO pay with a group of just 95 employees out of 55,000 employees, Aggreko's comparator group covers just 99 employees out of 6,000 while International Consolidated Airlines Group chose a group of just 99 employees of out of 60,000. There are a number of other examples of bad practice. The regulations emerged as a response to widespread public concern at the growth of top executives in relation to all workers, so such small comparator groups do not disclose the intended information.

Analysis

- The new rules on pay do not appear to have had a significant effect in terms of reducing executive pay packages from around the £4 million mark, a level more than 150 times that of the average UK worker.

- The requirement contained in the *Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013* forcing companies to compare pay increases for workers and CEOs has been next to useless.

- Firstly, the requirement is flawed, because it does not include so-called 'Long-Term Incentive Plans' – the largest element of CEO pay – and it only refers to pay increases, rather than absolute pay differences. This means that, for example, a tiny bonus pool, shared only amongst a few senior managers beneath board level, increased in proportion to the CEO's annual bonus, would show up as a similar percentage increase in bonuses for the CEO and for all workers.

- Secondly, the clause permitting companies to use a smaller comparator group means that many companies are excluding the overwhelming majority of their workers from the comparison anyway. A pay ratio between the pay received by the CEO and the lowest-paid worker would be a much more sensible measure.

- Thus far, there have not been dramatic pay increases for FTSE 100 CEOs across the board, while just over half the 67 companies we examined actually cut CEO pay. This may be down to the new regulations and fear over a shareholder revolt, together with public anger over excessive executive pay. However, the evidence suggests that this will not trigger a move towards lower levels of CEO pay more closely related to incomes across the economy.

- 32 out of the 67 increased their CEO's pay. While shareholder votes against pay packages at companies like Astra Zeneca and Barclays attracted considerable media attention, these were advisory votes on pay awards rather than binding votes on pay policy. In any case, there was no majority opposition to a pay package at a FTSE 100 company even in an advisory vote.

- Binding votes on future pay policy were generally approved by a large margin of over 90%. The banking group, Standard Chartered, however, did attract a vote of 41% against its three-year policy because bonus targets could be met after a year rather than over the longer-term as investors prefer for banks.

- At some of the companies with the biggest reductions in CEO pay, there were either particular one-off circumstances to explain the move– these included major reputational challenges (Barclays); or a change in CEO (Pearson or ARM Holdings). At many others, the reduction involved a decrease from a very high level of pay to a level that was still well above the FTSE 100 average (Old Mutual, Prudential, Reckitt Benckiser and Royal Dutch Shell, for example).

- Furthermore, pay policy suggests that average pay at the companies analysed will be £3.4 million in 2014, even if the CEOs in question only achieve target performance. However, one would expect a great number of FTSE 100 CEOs to exceed this threshold (though it is debateable to what extent that is attributable to their individual performance, as opposed to the collective efforts of their employees and the wider economic context). Certainly, they have done so in the past. Pay could be as high as £5.8 million, and it may be sensible to estimate an average closer to this figure.

- As such, it is impossible to see any evidence of a decline in CEO pay or a narrowing of the gap between top bosses and ordinary workers. After just one year, it would be too optimistic, even, to suggest that we are witnessing an end to rising top pay after three decades of increases (over that period there have been occasional instances of year-on-year declines or small rises, within a general upward trend in CEO pay).

- Even if that were the case, it would be impossible to ignore the shift that has taken place, not just since the Thatcher era, but since the late 1990s and early 2000s. In 1998, the average pay for a FTSE 100 CEO was just over £1 million, around 60 times the pay of the average UK worker (so still a sum of money that afforded a life of unparalleled opulence, far beyond the reaches of most people). It is now clear that, however one measures pay for a leading CEO, they can expect to make about £4 million a year, roughly 160 times the national average.

- This matters because FTSE 100 CEO pay reflects and encourages pay increases for other top earners – bankers, city lawyers, partners at accountancy firms. Even senior civil servants have justified six-figure pay packages on the basis that they still earn far less than a FTSE 100 CEO for jobs requiring a similar skillset. Given that wages excluding bonuses continue to increase at below the rate of inflation, there is no likely prospect of pay for ordinary workers catching up with those at the top, even if CEO pay did remain flat for years to come. There has been a permanent increase in the gap between those at the very top and the rest of the population, and the Government's new measures will not do enough to address it.

Appendix – pay across all companies analysed:

Company Name	Pay 2013	Pay 2012	2014 Target	2014 Maximum
WPP	29,846	17,543	7,802	19,264
TUI TRAVEL	10,122	6,737	2,364	5,339
PRUDENTIAL	8,656	9,533	5,163	7,815
SCHRODERS	8,414	4,870	5,689	7,673
ITV	8,365	2,914	2,522	4,790
HSBC	8,033	7,532	7,808	11,383
BP	7,982	5,563	6,835	11,810
GLAXOSMITHKLINE	7,207	4,386	5,477	11,647
IMI	7,118	7,954	2,151	4,084
ROYAL DUTCH SHELL	6,933	14,961	7,298	12,300
ANGLO AMERICAN	6,764	3,203	6,200	8,600
RECKITT BENCKISER GROUP	6,692	8,411	4,870	18,250
LLOYDS BANKING GROUP	6,571	3,398	4,917	7,787
BRITISH AMERICAN TOBACCO	6,492	6,340	3,699	8,550
EASYJET	6,435	3,694	1,936	4,042
UNILEVER	6,349	6,441	5,680	9,600
ROLLS-ROYCE HOLDINGS	6,228	4,557	4,250	2,600
RIO TINTO	5,596	4,040	5,381	8,490
COMPASS GROUP	5,532	4,811	3,100	4,700
PERSIMMON	5,492	4,989	1,400	2,000
ARM HOLDINGS	5,481	6,710	1,534	2,221
REED ELSEVIER	5,425	11,145	5,325	8,090
SHIRE	5,391	7,904	3,126	5,230
ABERDEEN ASSET MAN.	5,102	4,501	n/a	n/a
WILLIAM HILL	4,974	1,914	1,753	3,280

INTERNATIONAL CONSOLIDATED AIRLINES	4,971	1,083	2,729	4,379
OLD MUTUAL	4,789	7,881	3,257	4,941
MONDI	4,656	5,184	3,250	4,750
RANDGOLD RESOURCES	4,335	3,192	4,120	7,650
LEGAL & GENERAL	4,072	4,178	2,742	4,279
STANDARD LIFE	4,049	5,564	2,490	4,110
STANDARD CHARTERED	4,026	6,482	4,386	7,268
BUNZL	4,019	3,502	2,437	3,746
GKN	3,853	3,206	1,847	3,264
ANTOFAGASTA	3,615	3,598	3,615	3,615
MEGGITT	3,488	3,812	2,119	3,474
REXAM	3,472	4,731	2,740	4,308
CRH	3,418	2,082	2,817	5,404
ASTRAZENECA	3,344	7,840	5,500	8,600
INTERTEK GROUP	3,241	5,298	2,625	4,265
INTERCONTINENTAL HOTELS	3,149	4,881	2,709	4,143
TRAVIS PERKINS	2,993	3,506	2,500	3,800
ST.JAMES'S PLACE	2,921	2,410	1,561	2,324
SMITH & NEPHEW	2,774	2,934	3,459	4,906
TULLOW OIL	2,750	2,623	4,000	6,250
AVIVA	2,615	1,330	3,517	5,722
BG GROUP	2,518	5,411	3,800	9,100
BAE SYSTEMS	2,499	2,574	3,513	6,643
CENTRICA	2,235	5,709	4,480	6,969
CAPITA	2,209	2,038	1,791	3,041
HAMMERSON	2,069	2,451	2,563	1,519
IMPERIAL TOBACCO	2,011	2,793	2,830	5,820
G4S	1,973	1,186	2,551	4,754

AGGREKO	1,788	2,686	1,522	2,910
PEARSON	1,727	5,330	3,664	5,536
SAGE GROUP	1,670	1,196	2,070	4,020
WEIR GROUP	1,670	3,364	2,500	3,800
RESOLUTION	1,627	1,234	1,709	3,387
ROYAL BANK OF SCOTLAND	1,613	1,646	3,726	5,376
BARCLAYS	1,602	2,421	4,964	7,378
COCA-COLA HBC	1,594	1,202	n/a	n/a
PETROFAC	1,532	2,744	1,671	3,107
RSA INSURANCE	1,032	2,164	3,808	5,637
GLENCORE XSTRATA	964	964	n/a	n/a
MELROSE INDUSTRIES	928	31,201	1,089	1,658
FRESNILLO	697	1,142	721	852
ADMIRAL GROUP	387	374	393	393
Average	**4,509**	**4,913**	**3,439**	**5,823**
Average (minus Melrose 2012)	**4,509**	**4,515**		
Median	**3,853**	**3,812**		
Average (not inc top/bottom 5)	**4,082**	**4,212**		