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PAY RATIOS AND THE FTSE 350

An analysis of the first disclosures

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All opinions expressed in the paper (and any errors) are those of the High Pay Centre only.

Foreword

Extreme income inequality is one of the hallmarks of the UK economy. Out of 40 countries that comprise membership of the OECD group of leading economies, the UK is the 9th most unequal.[1] Other than the United States of America, it is only emerging economies such as South Africa, Turkey and Bulgaria that have a worse record on inequality than the UK amongst the OECD member states.

It is largely pay for what Thomas Piketty termed the 'super managers' – leading executives and business professionals – that has created the vast gap between those at the top and everybody else. Research suggests that the average FTSE 100 CEO is now paid around 126 times the average UK worker, compared to 'only' 58 times in 1999.[2]

Very high levels of inequality have a number of important implications:

- The potential link between higher inequality and greater social problems including higher crime levels; poorer mental and physical health; and lower social mobility with more entrenched social divisions;
- The impact that pay gaps within companies have on business performance through factors such as employee engagement and industrial relations;
- The way in which the distribution of pay by employers affects living standards for low- and middle-earners, and the potential to raise incomes for those who need it most through a more even distribution.

In these respects, the new pay ratio disclosures that have begun to appear in UK-listed companies' annual reports from 2019/20 are of great value.

By showing the scale of pay ratios within companies, and eventually how they change over time, this will enable better, more informed discussion and research into their social and economic impact.

Concrete pay ratio data will also provide stakeholders including investors, trade unions, policymakers and of course the companies themselves with a means of measuring (and targeting) performance in respect of pay distribution – hopefully contributing to a better understanding of both the scale and the basis of prevailing levels of pay inequality.

This report attempts to begin that process, while also being mindful of the fact that this is the first year of the pay ratio disclosures, and that there remains scope for both the calculation and the communication of the figures to be improved. As such, our findings should be treated as the beginning, rather than the end point, of a discussion about pay.

Luke Hildyard
Director, High Pay Centre

[1] OECD, *Income inequality data*, 2020 via https://data.oecd.org/inequality/income-inequality.htm

[2] CIPD and High Pay Centre, *Executive pay in the FTSE 100: 2020 review*, 2020 via https://www.cipd.co.uk/knowledge/strategy/reward/executive-payftse-100-2020

Key findings and recommendations

This executive summary highlights the key findings and recommendations from research into the first round of FTSE 350 companies 'pay ratio' disclosures in 2019/20. More detailed analysis can be found in the main report.

The median CEO/median employee pay ratio across the FTSE 350 is 53:1 and the median CEO/lower quartile employee ratio is 71:1. These ratios are significantly higher for the FTSE 100, where the median CEO/median ratio is 73:1 and the median CEO/lower quartile ratio is 109:1.

Highest pay ratios

The companies with the highest CEO/median and CEO/lower quartile employee ratios are shown in tables 1 and 2. Comparisons between different companies should not be made without fully understanding their respective business models – for example, differing reliance on indirectly employed workers who are not included in the pay ratio calculations, can make the pay ratios of two ostensibly similar companies look very different. Nonetheless, the highest ratios in the sample reveal strikingly wide pay gaps between CEOs and their colleagues. This should prompt serious debate about the causes and consequences of such differences.

Table 1: 10 highest CEO/median employee ratios

Company	Index	Industry	CEO/median employee ratio
Ocado	100	Retail	2,605
JD Sports	100	Retail	310
Tesco	100	Retail	305
Watches of Switzerland	250	Retail	262
GVC Holdings	100	Travel & Leisure	229
Morrisons	100	Retail	217
CRH	100	Construction & Materials	207
WH Smith	250	Retail	207
Astra Zeneca	100	Health Care	190
Serco	250	Industrial Goods & Services	190

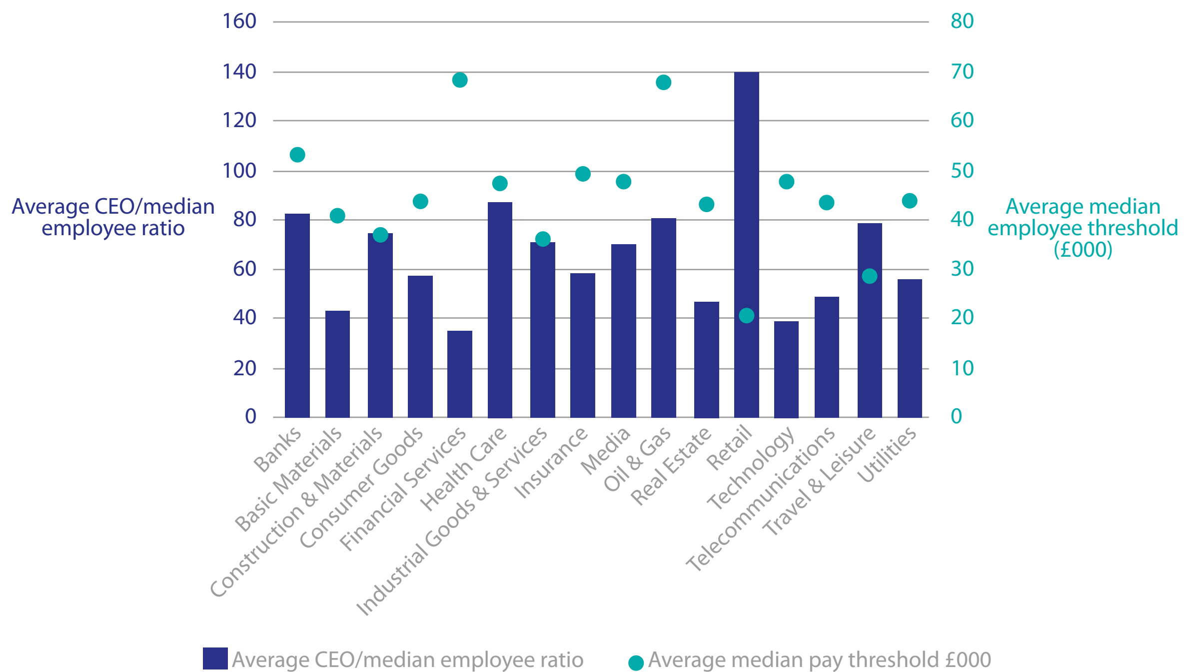
Table 2: 10 highest CEO/lower quartile employee ratios

Company	Index	Industry	CEO/lower quartile employee ratio
Ocado	100	Retail	2,820
BP	100	Oil & Gas	543
Tesco	100	Retail	355
JD Sports	100	Retail	348
Watches of Switzerland	250	Retail	317
CRH	100	Construction & Materials	289
Astra Zeneca	100	Health Care	280
GVC Holdings	100	Travel & Leisure	278
Homeserve	100	Retail	278
Experian	100	Industrial Goods & Services	267

Industry analysis

Even when excluding Ocado (an outlier with a CEO/median employee ratio of 2,605:1), the retail industry has the highest average CEO/median employee ratio of 140:1. The industry with the lowest average CEO/median employee ratio is financial services, with a ratio of 35:1. Overall, more labour intensive industries tend to have higher ratios as they employ a larger number of workers on lower wages. The reverse is true for capital intensive industries.

Figure 1: CEO/median employee pay ratios and median pay thresholds by industry



Trade union influence

The retail industry also provides an interesting case study regarding the influence of trade unions. At companies in the industry where the pay-setting process involves union consultation and/or full collective bargaining agreements, lower quartile thresholds did not fall below £18,000 and the average lower quartile threshold was £18,856, whilst in companies without full collective bargaining coverage, some lower quartile thresholds were below £15,000 and the average lower quartile threshold was £17,661. This is consistent with wider research suggesting a link between collective bargaining agreements and higher pay.[3]

Company characteristics

Net sales, market capitalisation and number of employees (all proxies for the size of the company) all have a positive relationship with pay ratio size.

Table 3: results of univariate test analysing the relationship between pay ratio size and net sales, market capitalisation and number of employees

Firm-level economic determinants	Companies where the CEO/median employee ratio is greater than or equal to the mean for the group	Companies where the CEO/median employee ratio is less than the mean for the group
Average net sales (£bn)	16.5	5.5
Average market capitalisation (£bn)	25.8	7.6
Average number of employees	46,553	19,888

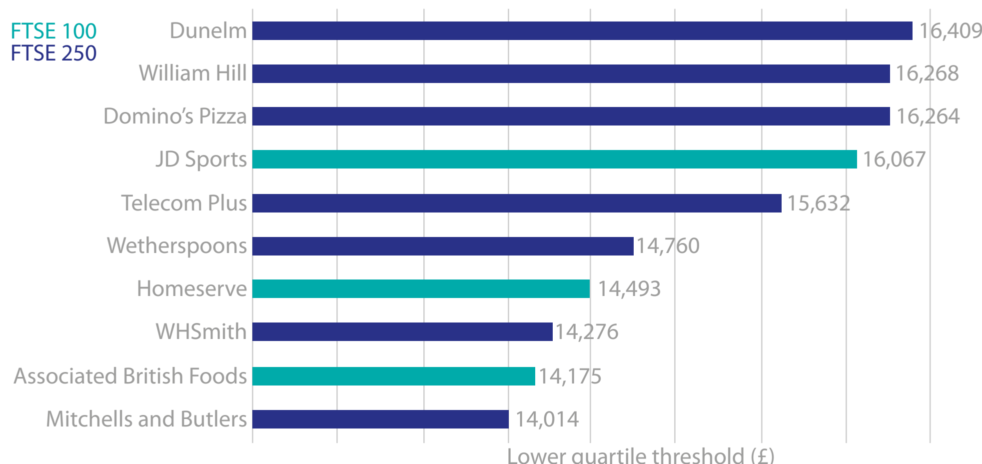
Multivariate regressions also found that the two characteristics which determine pay ratio size were indebtedness and complexity (where complexity is proxied by market-to-book ratio). It might be argued that it is to be expected that a CEO in charge of a larger, more complex organization would expect to be paid more for a more demanding role – equally, it could be said that this makes them more dependent on the support of colleagues and structures than someone running a smaller, more agile organization.

[3] Bryson A and Forth J, The added value of trade unions: New analyses for the TUC of the Workplace Employment Relations Surveys 2004 and 2011, TUC, 2017

Pay for low earners

The pay ratios also provide insights into pay of the lowest earning employees at some of the UK's biggest employers. The 10 companies with the lowest thresholds for pay at the lower quartile of the company's pay distribution were as follows:

Figure 2: 10 lowest lower quartile thresholds



Low pay is widespread across the companies in our sample:

- 36 companies – 18% of the sample – pay at least a quarter of their employees less than £20,000 a year (on an FTE basis).
- Of these, 34 companies pay all lower quartile employees below the annualised equivalent of the London Living Wage (£19,565), while 11 pay below the annualised equivalent of the Real Living Wage (£16,926).[4]

As the pay ratio calculations do not include outsourced workers, who are often low-paid, we estimated the gap between the CEO and a worker earning the living wage or minimum wage, (depending on whether the company is living wage accredited). This results in even more extreme gaps between the lowest earners and the CEO, with several CEOs making 500- or 600-times workers on the minimum or living wage.

Table 4: highest CEO/low-paid worker ratio

Company	Index	Industry	Living/ minimum wage (£)	CEO/low-paid worker ratio
Ocado	100	Retail	14,942	3,930
Astra Zeneca	100	Health Care	16,926	847
BP	100	Oil and Gas	16,926	613
Experian	100	Industrial Goods & Services	16,926	608
Royal Dutch Shell	100	Oil and Gas	14,942	585

[4] Calculations based on a 35-hour week at rates of £10.75 (London Living Wage) and £9.30 (Real Living Wage). The real living wage is a voluntary accreditation set by the Living Wage Foundation, based on their calculation of what is necessary to secure a decent standard of living. It should not be confused with the statutory minimum wage.

The potential to redistribute

The pay ratios also provide useful insights into the potential to raise incomes and living standards by reallocating companies' expenditure on the pay of high earners to those in the middle and at the bottom.

For example, a CEO pay award of £5m (there are 23 in our sample who earn at least this amount) equates to the equivalent cost of 295 workers earning the 2019/20 UK real living wage for a year. £5 million could raise the pay of 2,520 minimum wage workers to the real living wage.

On average, a 3% distribution of pay from an earner at the median upper quartile threshold for the companies in our sample (£59,133) would represent £1,774 per lower quartile employee – a significant sum of money for those earning below the median lower quartile threshold of (£28,395). Indeed, as those in the upper quartile earn above the upper quartile threshold, and those in the lower quartile earn below the lower quartile threshold, these figures understate the typical potential to redistribute and benefit low income workers.

However, there is enormous variation by company. At the companies with the lowest-paid lower quartile employees, the upper quartile are also not highly-paid, while at the companies with the highest-earning upper quartile workers, those in the lower quartile are not low-paid.

Table 5: Companies with the 5 lowest lower quartile thresholds and 5 highest upper quartile thresholds

5 companies with lowest lower quartile thresholds	Industry	Lower quartile threshold (£)	Upper quartile threshold (£)
Mitchells and Butlers	Travel & Leisure	14,014	15,881
Associated British Foods	Consumer Goods	14,175	24,026
WHSmith	Retail	14,276	17,034
Homeserve	Retail	14,493	32,232
Wetherspoons	Travel & Leisure	14,760	27,333
5 companies with highest upper quartile thresholds	**Industry**	**Lower quartile threshold (£)**	**Upper quartile threshold (£)**
TP ICAP	Financial Services	57,064	230,554
Man Group	Financial Services	83,084	227,235
Standard Chartered	Banks	83,000	212,000
Tate & Lyle	Consumer Goods	46,064	201,522
British American Tobacco	Consumer Goods	46,216	183,179

There would be considerable interest in understanding the potential to raise pay for low- and middle-income workers by redistributing from those at the very top – the people above the top 1% of the UK earnings distribution, who could afford to give up a significant quantity of their pay and remain well-paid even in comparison to above-average earners. However, data in quartiles does not provide sufficient granularity to do this. For the majority of companies, employees at the upper quartile thresholds are not what most people would consider to be exceptionally rich.

Narrative reporting

Companies are required to provide a narrative accompanying their pay ratio disclosure, however, these were generally insubstantial. Several companies provided minimal or no narrative. Those that did mostly failed to engage with the question of what actions they might take on pay distribution going forward, or how they engaged their workforce in the pay-setting process.

Conclusions and recommendations

It is important to emphasise the value of pay ratio reporting: it can be an important tool for stakeholders, including workers, to hold companies to account - provided it is not used to make sweeping judgements or definitive conclusions, but as a starting point for discussions around pay and employment practices. Indeed, companies themselves can use the process for assessing their corporate culture and the value they deliver for their stakeholders.

The disclosures provide useful benchmarks for pay levels and pay distribution across companies. The scale of the inequality and the extent of low pay at some of the UK's largest employers that they expose is critically important, and needs to be widely debated. However, there are also some limitations to the disclosures, chiefly:

- The exclusion of indirectly employed workers potentially distorts the ratios and renders comparisons more difficult.
- The exclusion of major employers beyond UK-listed companies means the disclosures provide a limited picture of UK employment practices.
- The lack of information on top earners beyond the CEO makes it harder to assess the potential to raise pay for low- and middle- earners by re-balancing pay distributions.

We have made recommendations for how the pay ratios disclosures could be improved: these can be understood both as policy recommendations for when the government next reviews the pay ratio disclosures, and as changes that stakeholders can encourage companies to make voluntarily:

- Companies should provide more granular information on the earnings of those between the upper quartile threshold and the CEO.
- Outsourced workers should be included in the pay ratio calculations.
- There should be higher standards and clearer expectations of narrative reporting.
- Companies should directly provide information on pay ratios to their workers.
- Companies should provide data on their number of UK employees.

We also propose accompanying recommendations that would complement the pay ratio disclosures, and ensure that the information they provide is used to improve low- and middle-income workers' pay and working conditions:

- Allow trade union access to workplaces, to inform workers of the benefits of collective bargaining.
- Establish sectoral governance bodies to monitor fair pay.
- Legislate for worker representation on company boards.
- Require companies to introduce all-employee profit sharing or share ownership schemes.
- Amend company law to give the interests of all stakeholders equal importance, rather than elevating shareholder interests above those of others.
- Make the shareholder vote on directors' remuneration reports legally binding.
- Require companies to include guidance on potential future pay ratio sizes in their remuneration policies so that shareholders can vote on this.
- Apply the pay ratio disclosure requirements to all large employers.

Taken together, these measures would boost transparency, governance and accountability to stakeholders at the UK's biggest businesses, while strengthening the bargaining power of low- and middle-income workers, and significantly improving living standards.

High Pay Centre analysis of 2020 pay ratio disclosures: final report

This introductory section explains the background to the pay ratio disclosures and the parameters for this report. It discusses how the pay ratio disclosures might be used by different stakeholder groups.

Introduction

This report analyses the first set of pay ratio disclosures made by FTSE 350 companies, in order to identify what insights the pay ratios provide and how they might be used by stakeholders.

In addition to examining the ratios between the CEO and their median, upper quartile and lower quartile employees, the analysis reviews data on the lower quartile pay thresholds in order to gain insights into the earnings of the lowest-paid employees at the UK's biggest listed companies. We also look at the pay differences between the upper and lower quartiles (on the basis of pay levels at the 75th and 25th percentiles).

The report is an updated version of an interim study, published in June 2020, analysing the very first pay ratio disclosures from 1 January to 30 April 2020.

The interim report identified initial insights from the disclosures. This final report, covering disclosures by 201 companies (over 90% of the FTSE 350 companies required to report their pay ratio, as of November 30 2020) is able to make more concrete observations on what pay ratio reporting tells us about pay, employment practices and corporate cultures at some of the UK's largest private sector employers. It also makes recommendations for how the disclosures could be improved and how they can best be used.

We intend to repeat the analysis in future years, using the pay ratio disclosures to build a data set that can enhance our understanding of UK corporate pay distribution and its socio-economic impact on an ongoing basis.

Using the analysis

This is only the first year of pay ratio reporting, and given the variable nature of CEO pay awards, more years of data will allow us to build a clearer picture of corporate pay practices.

Nonetheless, this analysis gives an initial snapshot of trends in pay ratio sizes, shows how firms are approaching pay ratio reporting, and provides data that can be used to inform debates about pay and work. It also identifies the limitations of the disclosures and recommends areas for improvement, with regard to both the regulations themselves and their application.

In particular, we hope that the research will be of some value to a number of stakeholders, including the following groups:

- **The workers themselves**, who can potentially benefit from better information about how their pay levels compare to others within their own company or in other similar organisations.
- **Businesses**, particularly the remuneration committees that oversee pay-setting processes and the directors or committees responsible for stakeholder representation in corporate governance structures as mandated by the 2018 Corporate Governance Code. Businesses can use the pay ratio data to inform their thinking on how to achieve the fairest balance of pay distribution across their workforces.
- **Investors** seeking to understand the employment practices and corporate cultures of the companies they invest in, and how their spending on pay – a significant cost for any business – is distributed.
- **Trade unions**, who can use information on pay levels to support the case for fairer wages for the workers they represent.
- **Policymakers** interested in the initial impact of the pay ratio disclosures, and their insights and limitations. Following the outbreak of COVID-19 and the consequent reliance of many businesses on government support, details of the distribution of companies' pay costs may also be relevant to decisions regarding support packages.
- **Academic and commercial researchers** interested in prevailing corporate pay practices, who can use the data to examine how pay distribution relates to issues such as industry type, business performance or societal impact.

We have engaged with businesses, investors, trade unions and policymakers in order to discuss how they can make the best use of the data and the insights it provides. We hope the research will assist these stakeholders in their work shaping the pay and employment practices of the UK's largest private sector employers.

01

Highest and lowest pay ratios

In this section we show the wide range of pay ratio sizes across the companies that have disclosed.

Median pay ratios

The ratio sizes at individual companies vary widely from the median. The pay ratio disclosures mean that we can identify the widest pay differentials across UK-listed companies. Tables 1-4 detail the companies with the highest and lowest CEO/median employee and CEO/lower quartile employee pay ratios. This updated list shows even wider pay gaps than those presented in the interim report.

Table 1: 10 highest CEO/median employee ratios

Company	Index	Industry	CEO/median employee ratio
Ocado	100	Retail	2,605
JD Sports	100	Retail	310
Tesco	100	Retail	305
Watches of Switzerland	250	Retail	262
GVC Holdings	100	Travel & Leisure	229
Morrisons	100	Retail	217
CRH	100	Construction & Materials	207
WH Smith	250	Retail	207
Astra Zeneca	100	Health Care	190
Serco	250	Industrial Goods & Services	190

Ocado is a huge outlier here: its median ratio of 2,605: 1 is due to the unusually large pay package of over £58 million handed to Ocado's CEO. This was a one-off pay award: a growth incentive plan (GIP) worth £54 million constituted the overwhelming majority of the pay package. In the previous year, the Ocado CEO was paid £4 million.

Table 2: 10 highest CEO/lower quartile employee ratios

Company	Index	Industry	CEO/lower quartile employee ratio
Ocado	100	Retail	2,820
BP	100	Oil & Gas	543
Tesco	100	Retail	355
JD Sports	100	Retail	348
Watches of Switzerland	250	Retail	317
CRH	100	Construction & Materials	289
Astra Zeneca	100	Health Care	280
GVC Holdings	100	Travel & Leisure	278
Homeserve	100	Retail	278
Experian	100	Industrial Goods & Services	267

Tables 1 and 2 demonstrate the importance of industry in influencing pay ratio size: the retail industry dominates the companies with the highest ratios. Retail companies employ more low-paid staff than most other industries. There are also several large retailers in the tables whose size is potentially a significant factor driving their high CEO pay.

Table 3: 10 lowest CEO/median employee ratios

Company	Index	Industry	CEO/median employee ratio
Sanne Group	250	Financial Services	8
XP Power	250	Industrial Goods & Services	10
Hiscox	250	Insurance	11
PZ Cussons	250	Consumer Goods	13
Petrofac	250	Oil & Gas	14
Integrafin	250	Financial Services	15
Kainos	250	Technology	15
Victrex	250	Basic Materials	16
Renishaw	250	Industrial Goods & Services	17
CMC	250	Financial Services	17

Comparing tables 1 and 3 shows the huge variation in median pay ratio sizes across the disclosures, with the highest ratios being 200-300: 1 and the lowest being 10-20: 1.

Table 4: 10 lowest CEO/lower quartile employee ratios

Company	Index	Industry	CEO/lower quartile employee ratio
Sanne Group	250	Financial Services	13
XP Power	250	Industrial Goods & Services	16
Victrex	250	Basic Materials	18
Integrafin	250	Financial Services	18
Hiscox	250	Insurance	19
PZ Cussons	250	Consumer Goods	19
Petrofac	250	Oil & Gas	20
Renishaw	250	Industrial Goods & Services	22
Kainos	250	Technology	22
Persimmon	100	Consumer Goods	23

As noted in the interim report, these tables demonstrate the importance of company size in influencing pay gaps: those with higher ratios are mainly from the FTSE 100 index, whilst most of those with the lowest ratios are FTSE 250 companies.

Potential future pay ratio sizes

It is also possible to estimate pay ratios for the coming year, using statements about expected executive remuneration in companies' annual reports.

The reports indicate the level of pay the CEO will receive if they meet (but do not exceed) their targets: this can be used to calculate the company's pay ratio 'target' value for the next financial year, using the workforce pay levels recorded in the pay ratio disclosures for the current financial year as the comparator with the CEO's expected pay.

Analysis of these statements suggests that the ratios disclosed in 2021 will not significantly differ from those in 2020, and that the industry trends we have seen so far will remain consistent, without significant pay increases for the workforce.

The analysis found that for the FTSE 350, the median CEO/median employee pay ratio target value is 55:1, slightly higher than the median CEO/median employee pay ratio for the 53:1 FTSE 350 this year. The industry trends we identify in section 2 are also maintained in the pay ratio target values. For example, in the retail sector, the potential average pay ratio target value for next year remained high at 114:1, whilst the potential average pay ratio target value for financial services remained low at 37:1.

It will be interesting to compare the actual pay ratios reported in 2021 to these projections. The impact of the Covid-19 pandemic may mean that CEO performance targets are not met and that pay awards are lower. Several CEOs have made salary cuts or have forgone bonuses in response to the economic shutdown, and Long-Term Incentive Plans may also vest at lower levels if company performance has suffered.[1] On the other hand, many companies have furloughed workers on reduced pay, which could potentially widen ratios.

[1] High Pay Centre, *Corporate Response to the Economic Shutdown*, 2020 via https://highpaycentre.org/wp-content/uploads/2020/08/report_copy.pdf

Limitations of the disclosures

It is important that sweeping judgements are not made on the basis of the pay ratio disclosures alone, and that they are used as the starting point rather than the last word of a debate about corporate employment practices and pay distributions.

There is a temptation to assume that those companies with low ratios are necessarily examples of 'better practice'. However, it is important to also examine factors behind the ratios. In section 2 we discuss the complexities of the characteristics that influence the ratio sizes.

The one-off nature of some CEO awards, such as Ocado's £58m pay package, means that the snapshot of individual companies pay ratios may be misleading. We will get a more consistent picture when we have a few years of disclosures to analyse and can compare both pay ratios in a particular year, as well as company averages over a multi-year period.

Different employment models and the use of outsourced workers also complicate inter-company comparisons.

The extent to which many UK companies rely on indirectly employed workers and the implications of their exclusion from pay ratio calculations is discussed further in section 4 of the report. The oil industry provides one of the most obvious examples of how this can distort comparisons between ostensibly similar companies, if undertaken without contextual understanding of their wider employment models.

BP and Shell, two major FTSE 100 oil companies with similarly high CEO pay levels, have very different ratio sizes: BP has a CEO/lower quartile employee ratio of 543:1 whereas Shell's is 147:1. This is because Shell franchises its petrol stations, meaning that low-paid retail staff working at petrol stations are not included in its pay ratio calculations, whereas BP retail workers are directly employed and included in the calculation. As such, Shell's lower quartile threshold is £59,419 whilst BP's is £19,108.

Table 5: A comparison of BP's and Shell's pay ratios

Company	Index	CEO pay (£m)	Lower quartile ratio	Median ratio	Lower quartile pay threshold (£)	Median threshold (£)
BP	100	10.4	543	188	19,108	55,071
Royal Dutch Shell	100	8.7	147	87	59,419	100,755

Pay ratios and inequality

However, even accounting for these issues, the ratios identified in this section convey useful information and raise important questions.

The widest ratios show individuals making 100, 200 or even 500 times many of their colleagues. These are stark findings, regardless of whether or not the ratios identified really are the widest in the UK. Indeed, if different employment models obscure a higher number of companies with ratios of this size then the issue becomes even more important.

From a business perspective, there is an extensive academic and commercial research literature over how much of the variance in firm performance can be attributed to an individual CEO.[2] By highlighting the scale of the gap between CEOs and their colleagues, research can inform discussion of whether or not this fairly reflects their economic value.

Similarly, there are also important moral questions around the scale of inequality cited in this section, and concerns about the impact that it might have on social cohesion, and on employee morale and workplace relationships.[3]

Again, by highlighting the most extreme intra-company pay differences, the pay ratio disclosures will raise the profile of these issues and inform and encourage discussion of pay inequality.

[2] See e.g. Fitza M A, How much do CEOs really matter? Reaffirming that the CEO effect is mostly due to chance, 2017, Strategic Management Journal, 38(3), 802-811.

[3] Notably, voters in San Francisco recently approved a ballot measure to impose an extra tax on companies that pay their CEO over 100 times more than their median employee.

02

Pay ratios by industry

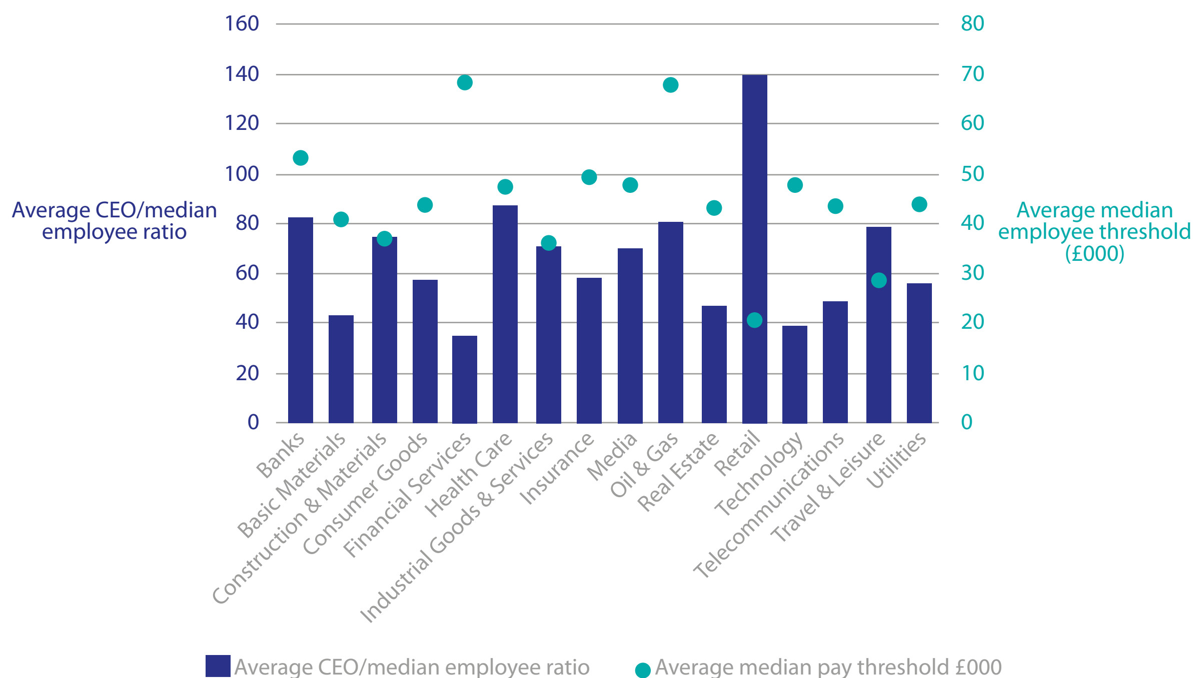
This section looks at average pay ratios across industries and sectors, discussing factors that potentially shape the ratios within different industries.

Pay ratios across industries

A company's industry or sector is likely to have a significant impact on the size of its pay ratio. Analysing the pay ratios across different industries and sectors can help to identify certain trends. However, it should again be reiterated that companies should not be judged solely on the basis of comparisons between their pay ratio and the industry average - and that it is important for stakeholders to understand the company's individual context before making a judgement on whether its balance of pay is fair or proportionate.

Figure 1 shows the average CEO/median employee pay ratio and the average pay threshold for median earners across different industries (Ocado has been excluded from the data given that it is such an outlier).[4]

Figure 1: CEO/median employee pay ratios and median pay thresholds by industry



To date, the **retail industry** has the highest average CEO/median ratio: excluding Ocado, this is 140:1, and including Ocado it is 276:1.

Table 5 shows Ocado and the 5 other retail companies with the highest median ratios. Note that the lower quartile thresholds are full-time equivalent.

[4] We have used the Industry Classification Benchmark Rules which can be found here: https://research.ftserussell.com/products/downloads/ICB_Rules.pdf. A mixture of industries and supersectors have been used, depending on the number of companies in each classification

Table 6: highest CEO/median pay ratios in the retail industry

Company	Index	CEO pay (£m)	Lower quartile ratio	Median ratio	Lower quartile pay threshold (£)	Median threshold (£)
Ocado	100	58.7	2,820	2,605	20,800	22,500
JD Sports	100	5.6	348	310	16,067	18,299
Tesco	100	6.4	355	305	18,086	21,057
Watches of Switzerland	250	6.5	317	262	20,500	24,900
Morrisons	100	4.2	230	217	18,202	19,340
WH Smith	250	3.4	239	207	14,276	16,502

Pay ratios are, of course, determined both by levels of pay for the company's UK employees and levels of pay for their CEO. As we noted in the previous section, high CEO pay is a big factor in the size of the ratios at certain major retail companies. However, what is really distinctive about the retail industry is that it has by far the lowest median employee pay of all industries, averaging £20,574. As Table 5 shows, some of the lower quartile thresholds in the retail industry are extremely low: for example, WH Smith's lower quartile threshold is £14,276. Low pay is discussed further in section 4 of the report.

The **financial services industry** has the lowest average CEO/median ratio. This is a capital-intensive industry with relatively few employees who are often in highly-paid analytical or specialist roles. Thus, the low ratios are predominantly due to the type of work involved in the sector and the type of employees recruited - though as shown in Table 6, some of the lowest ratios are also due to low CEO pay.

Table 7: lowest CEO/median employee ratios in the financial services industry

Company	Index	CEO pay (£m)	Lower quartile ratio	Median ratio	Lower quartile pay threshold (£)	Median threshold (£)
Sanne Group	250	0.3	13	8	33,128	53,614
Integrafin	250	0.8	18	15	41,722	50,067
Man Group	250	2.2	26	17	83,084	126,740
CMC	250	1.0	26	17	40,300	62,600
Investec	250	1.3	34	18	38,784	72,337

The effect of union influence on pay ratio size

Trade union presence within a company is a potential influence on the size of pay ratios.

The retail industry provides an example of the differences between companies with and without collective bargaining. For 5 of the 18 retail companies in our sample, pay across the workforce is determined by collective bargaining agreement or by significant consultation with unions: these are Greggs, Morrisons, Ocado, Sainsbury's and Tesco.[5] All of these companies have lower quartile thresholds above £18,000, and the average lower quartile threshold for these five companies is £18,856.

For the remaining 13 companies, the lowest lower quartile thresholds are below £15,000, and the average lower quartile threshold is £17,661.[6] An average difference of over £1,000 is substantial at these low levels of pay, and this suggests that when unions have collective bargaining rights at a particular company, this makes a significant difference to the pay of lower paid workers.

5 Information provided by the USDAW trade union.
6 Two of these companies, B&M European Retail and Next, have collective bargaining but only for their distribution sides.

This analysis is consistent with wider research showing the relationship between collective bargaining and higher workforce pay across the UK as a whole. A 2017 study found that 'staff at workplaces where unions were recognised for collective bargaining were paid 5.3% more than staff at comparable workplaces without collective bargaining'.[7]

However, collective bargaining does not seem to have contained CEO pay at the retail companies examined. Ocado, Morrisons and Tesco are all in our list of the companies with the top 10 CEO/median employee ratios shown in Table 1. This is understandable given that pay across the workforce tends to be set by different mechanisms to executive pay.[8]

Nonetheless, addressing this question from a sectoral perspective suggests that there may be some relationship between lower CEO pay and collective bargaining. The Aerospace and Defence sector tends to have high levels of union membership, with the majority of companies negotiating with unions on pay. The table below shows that ratios in the sector are relatively low, though not consistently low across the board: the two FTSE 100 companies in the group have higher CEO pay and higher ratios.

Table 8: pay ratios in the aerospace and defence industry

Company	Index	CEO pay (£m)	Lower quartile ratio	Median ratio	Lower quartile pay threshold (£)	Median threshold (£)
Babcock	250	1.4	47	37	29,200	37,600
Ultra Electronics	250	1.6	54	37	29,549	43,151
Meggitt	250	2.5	76	58	32,879	42,861
Qinetic	250	2.0	56	41	35,732	48,965
BAE Systems	100	3.9	90	72	43,873	54,833
Rolls Royce	100	3.2	66	56	48,000	56,000

The possibility of a relationship between lower pay ratios and higher trade union membership is supported by the fact that at the national level, there is a strong link between lower economic inequality and higher trade union membership or collective bargaining coverage – the richest 1% tend to take a much higher share of total incomes in countries with lower union membership and/or collective bargaining coverage.[9] In the UK, the share of incomes going to the top 1% has risen over the past forty years in tandem with the fall in trade union membership.[10]

It is also the case that unions are well placed to use these disclosures to push for fairer pay distribution, so it is possible that industries in which unions are influential might see ratios getting smaller now that this information is available.

As more pay ratio disclosures are published in the coming years, the potential evidence base for research into the role that unions play in counteracting pay inequality will grow.

7 Bryson A and Forth J, The added value of trade unions: New analyses for the TUC of the Workplace Employment Relations Surveys 2004 and 2011, TUC, 2017 via https://www.tuc.org.uk/sites/default/files/1%20WERS%20lit%20review%20new%20format%20%20RS_0.pdf

8 This has been the case since the early 1980s, prior to which pay for both employees and executives was set with reference to internal pay grades. This is discussed in Willman P & Pepper A, The role played by large firms in generating income inequality: UK FTSE 100 pay practices in the late twentieth and early twenty-first centuries, Economy and Society, 2020

9 IPPR, Fall in trade union membership linked to rising share of income going to top 1%, 2018 via https://www.ippr.org/news-and-media/press-releases/fall-in-trade-union-membership-linked-to-rising-share-of-income-going-to-top-1

10 Social Europe, Collective bargaining and rising inequalities: do the IMF and OECD get it?, 2016 via https://www.socialeurope.eu/collective-bargaining-rising-inequalities-oecd-imf-get

03 Company characteristics

This section details external research commissioned by the High Pay Centre aimed at understanding which company characteristics are drivers and/or predictors of pay ratio size.

Which company characteristics drive pay ratios?

In order to supplement our own analysis of the pay ratio disclosures, The High Pay Centre carried out research in partnership with Dr Aditi Gupta at Kings' Business School, Kings' College London, and Steve Glenn, Head of Executive Remuneration Research at E-Reward, to analyse the impact of specific company characteristics on pay ratio size.[11]

Pay ratios and company size

Dr Gupta's analysis found that market capitalisation, net sales and employee numbers all had a very significant positive correlation with pay ratio size (see Table 9). These characteristics are all proxies for company size.

Table 9: results of univariate test analysing the relationship between pay ratio size and net sales, market capitalisation and number of employees

Firm-level economic determinants	Companies where the CEO/median employee ratio is greater than or equal to the mean for the group	Companies where the CEO/median employee ratio is less than the mean for the group
Average net sales (£bn)	16.5	5.5
Average market capitalisation (£bn)	25.8	7.6
Average number of employees	46,553	19,888

Pay ratios and company complexity

More sophisticated tests controlling for multiple variables found that only two characteristics were highly significant in determining pay ratios: these were firm risk (proxied by firm debt) and firm complexity (proxied by market-to-book ratio). Higher debt and a higher market-to-book ratio were related to higher ratios[12]. This indicates that CEOs are being paid more in companies that are more indebted and more complex.

[11] Details of the methodologies used for this research can be found in Appendix A.

[12] The market-to-book ratio evaluates a company's market value relative to its book value. The 'market' value is the current price of all shares, whilst the book value is the current cost of the company's assets minus the cost of its liabilities.

It is not immediately clear why indebtedness might bring about a higher ratio. However, there is evidence to suggest that firms use indebtedness in order to claim that they are unable to pay workers more. One US study finds that firms under threat of unionisation tend to take on more debt in order to reduce the funds that are available on its balance sheet.[13] The potential connection between lower workforce pay and greater company indebtedness is one possible explanation for the connection between higher leverage and higher pay ratios.

Pay ratios and performance

One might expect that CEO pay, and therefore pay ratio size, would correlate with firm performance, since most CEO pay packages have a substantial performance-related element that is pegged to financial metrics. However, this was not borne out by the results.

Our analysis examined the relationship between pay ratio size and 3-year share price change data (since Long-Term Incentive Plans for CEO pay packages are commonly set with reference to a 3-year time period), finding a weak relationship between the two variables for the FTSE 350 with an R-Squared value of 0.0071. There was a slightly stronger correlation between the two variables for the FTSE 100, with an R-Squared value of 0.1134.

Further research on the relationship between performance and pay ratios found that neither 1-year share returns nor 5-year return on assets had a significant positive relationship with pay ratios. A separate univariate test looking at the relationship between proxies for performance and CEO pay also failed to find a significant positive correlation. This suggests that good performance does not necessarily result in higher pay for the CEO and therefore in larger ratios, and likewise that bad performance does not necessarily result in lower pay for the CEO.

There are two important caveats with this analysis. Firstly, most of the company characteristics being examined affect predominantly the CEO pay aspect of the ratio and not the workforce pay aspect. Market capitalisation, net sales and firm performance fall under this category. Potential exceptions to this are indebtedness, as discussed, and employee numbers: research on pay ratios in the US has found that a higher employee count is correlated with lower median pay.[14] Nonetheless, most of these results are telling us about what drives CEO pay levels rather than the ratio sizes themselves.

Secondly, our sample size of just under 200 companies is small, and regressions are usually done with a much bigger sample, so these findings should be interpreted with some caution. We are planning to continue research on this, and the results will become more reliable once we have several years of data to work with. It is worth noting, however, that research analysing the pay ratio disclosures in the US, which came into force in 2018, has found similar results: in this US analysis, pay ratio size correlated closely with both market capitalisation and employee numbers, and there was no correlation between pay ratio size and firm performance.[15]

[13] Bronars S and Deere D, The Threat of Unionization, the Use of Debt, and the Preservation of Shareholder Wealth, The Quarterly Journal of Economics, 106: 1, 1991, via http://www.jstor.org/stable/2937914

[14] Burney B, What does the CEO pay ratio data say about pay? 2018 via https://corpgov.law.harvard.edu/2018/09/04/what-does-the-ceo-pay-ratio-data-say-about-pay/

[15] See Lifshey D, The CEO Pay Ratio: Data and Perspectives from the 2018 Proxy Season, 2018 via https://corpgov.law.harvard.edu/2018/10/14/the-ceo-pay-ratio-data-and-perspectives-from-the-2018-proxy-season/

Are pay ratio sizes justified?

Beyond simply looking at which factors determine or correlate with pay ratio size, we need to ask whether it is justifiable for pay ratio size to be affected by certain factors.

For example, it appears to be standard practice that larger companies reward their CEOs more highly and have larger pay ratios as a result. It is true that at companies that have a higher market capitalisation, decisions taken by the CEO will have a greater financial value. However as we have previously noted, the economic importance and impact of executives on company performance, and whether or not this justifies such vast pay gaps, continues to be extensively debated by researchers.[16]

In the case of companies with a larger number of employees (with more levels between the CEO and the median worker), there will be more extensive supply chains, and involvement in a wider range of markets, all adding to the complexity of the CEO's role.

At the same time, however, a larger company also makes the CEO more dependent on their colleagues. It is arguably impossible for a single individual or executive team to maintain oversight of an organisation with extensive operations and supply chains spanning multiple continents, time zones and regulatory regimes. As Sir Philip Hampton, former Chair of GSK and RBS, said in a research interview for a previous High Pay Centre publication,

"the bigger the system,the more it's the system that counts rather than the person on top of it".[17]

[16] See e.g. Li W & Young S, An analysis of CEO pay arrangements and value creation for FTSE-350 companies, 2016, CFA Society of the United Kingdom, 2.

[17] High Pay Centre, Made to measure: How opinion about performance becomes fact, 2015 via http://highpaycentre.org/files/FINAL_MADE_TO_MEASURE.pdf

04 Pay for low earners

This section examines absolute pay levels at the lower quartile threshold, highlighting the companies with the lowest paid lower quartile employees in the sample and discussing the implications. It also looks at the possible impact of outsourcing on pay ratios, and calculates ratios that show the gap between CEO pay and the annualised national minimum or real living wage (dependent on whether the company in question is an accredited living wage employer).

Though the pay ratio reporting requirements were driven by concern about CEO pay levels relative to the wider workforce, it is arguably the disclosure of absolute pay at the lower quartile of their pay distribution that is the most interesting aspect of the disclosures. Ensuring everyone has a decent standard of living should be one of the foremost priorities for any society. In this respect, what the lowest-paid employees at some of the UK's largest employers earn is of considerable importance.

The median lower quartile threshold for the companies in our sample is £28,395. This figure seems high, and is not far below the median gross annual earnings for full-time workers in the UK of £30,353.[18] However, it is worth noting that the figure refers to total employee remuneration, rather than just wages or salaries: it includes taxable benefits, pensions and any share-based pay or cash bonuses. Furthermore, as the figures below show, it masks considerable variation across different companies.

It is also very important to emphasise that this is the lower quartile threshold. That means that 25% of employees at these companies are earning less than this. Accordingly, the disclosures do not show what the lowest-paid employees are earning. Furthermore, indirectly employed workers, who very often carry out low-paid roles (security guards or cleaners maintaining a firm's offices, for example) are not included in the sample.

Lowest-paying companies

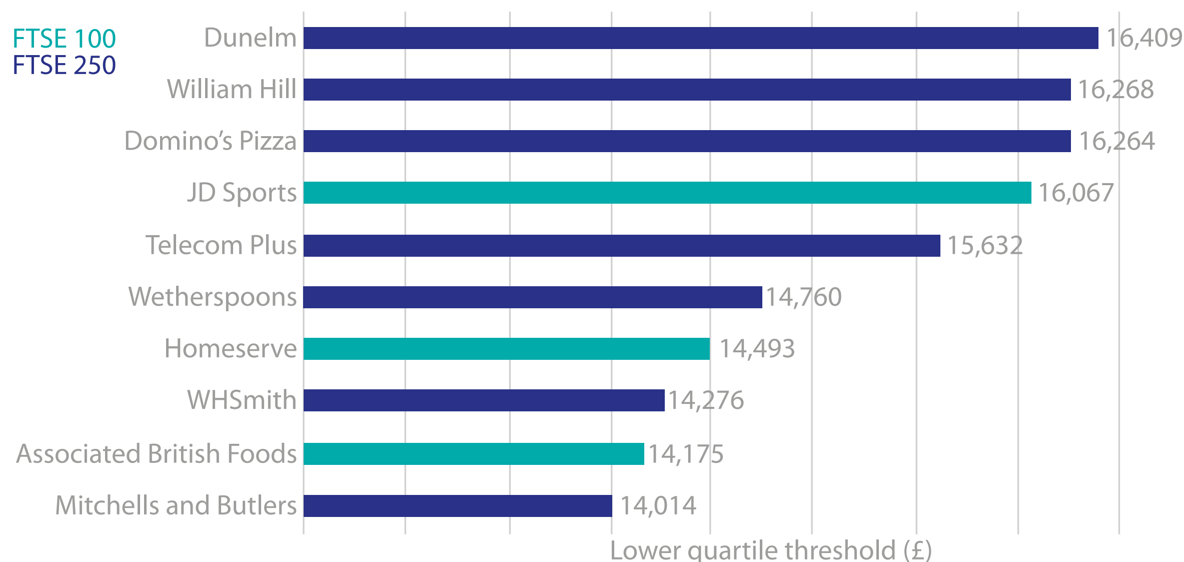
Figure 2 shows the companies with the lowest levels for the lower quartile pay threshold.

As might be expected, the companies in this table are mostly from sectors such as retail and travel and leisure, which are labour-intensive companies with a large proportion of low-paid roles. They are also both sectors that employ large proportions of under-25s, to whom the national living wage rate does not apply.

In our interim report, the lowest levels for the lower quartile threshold were around £16-17,000. With this extended set of disclosures, the picture has worsened considerably. The lowest thresholds for lower quartile earners at FTSE 350 companies are strikingly low, with the lowest-paying five companies all paying at least a quarter of their employees below £15,000, while 36 companies – 18% of the total sample – pay the lower quartile less than £20,000.

[18] Office for National Statistics, Annual Survey of Hours and Earnings, 20 October 2019

Figure 2: 10 lowest lower quartile thresholds



The UK real living wage, calculated by the Living Wage Foundation, as the minimum hourly rate on which the recipient is able to cover their living expenses and live a healthy lifestyle, was £9.30 an hour across the UK and £10.75 in London up until November 2020. Based on a 35-hour week, the 2019/20 UK rate equated to £16,926 per annum and the London rate to £19,565 per annum.

All of the companies in this figure are below the annualised Living Wage, and certainly well below the London Living Wage. This is despite the fact that the disclosures include pensions whilst the Living Wage does not. Amongst the disclosures as a whole, 34 companies lower quartile thresholds below the annualised equivalent of the Real Living Wage for London, including 11 below the national Real Living Wage.[19]

It is worth re-stating that a quarter of employees at each company earn less than the lower quartile threshold while, as we discuss in the next section, the exclusion of indirectly employed workers from the pay ratio calculations means that the thresholds may be artificially high in many cases. So even these stark findings potentially understate the extent of low pay at some of the UK's biggest companies.

[19] On the same basis that we have annualised the real living wage, an annualised equivalent of the statutory minimum wage for over 25s would be £14,492 - however there is no suggestion that any companies in our sample, including the three with lower quartile thresholds below this amount, have breached the minimum wage requirements. Factors that could potentially drive pay levels below an annualised minimum wage equivalent include the employment of large numbers of workers below the age of 25, and the use of the Coronavirus Job Retention Scheme, whereby workers receive only 80% of their pay.

Box 1: Compliance with the pay ratio reporting

The Companies (Miscellaneous Reporting) Regulations 2018 state that companies must disclose the total remuneration of employees at the lower quartile, median and upper quartile mark, as well as the salary component of this remuneration.[20]

Not all companies have complied: Biffa, Centrica, Electrcomponents, Homeserve, Ibstock, Imperial Brands, Pets at Home, Rentokil, TalkTalk, Telecom Plus and Wetherspoons all failed to disclose the pay levels of employees at the three required points of the pay distribution, publishing only the ratio to CEO pay. Just Eat did not disclose workforce remuneration levels or the pay ratios.

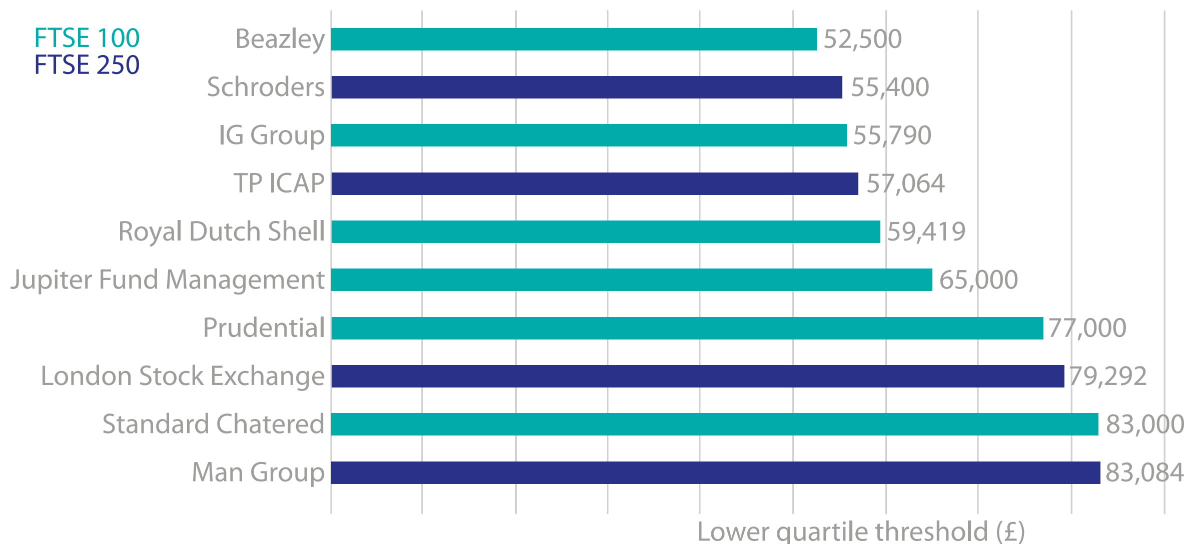
Homeserve, Telecom Plus and Wetherspoons are all amongst the ten companies with the lowest lower quartile thresholds. Biffa, Ibstock and Pets at Home also have lower quartile thresholds under £20,000. It may be the case that the companies in question did not disclose their absolute pay thresholds in order to avoid attention being drawn to their high proportion of low-paid employees.

For the purposes of our analysis, companies' failure to disclose thresholds is not a problem as we can calculate the thresholds by dividing the declared figure for CEO pay by the declared ratio. However, the principle of companies with potentially noteworthy pay practices disregarding reporting requirements on the subject is concerning.

Highest lower quartile thresholds

However, just as there are a strikingly large number of companies with very high numbers of low paid employees, the median lower quartile pay threshold of £28,395 reflects the fact that there are a number of companies in the sample where even those employees at the lower quartile are well paid by the standards of the wider UK economy.

Figure 3: 10 highest lower quartile thresholds



[20] The Companies (Miscellaneous Reporting) Regulations 2018, Paragraph 19F, via https://www.legislation.gov.uk/ukdsi/2018/9780111170298/pdfs/ukdsi_9780111170298_en.pdf

Almost all of the companies highlighted in figure 3 are financial services or insurance companies which employ a small number of very highly-paid staff. However, the disclosures do not include outsourced workers. It is probable that many of these companies have low-paid workers such as cleaners or caterers who have permanent employment on the company in question's premises, doing work commissioned by the company, but are indirectly employed and are not included in the pay ratio calculations. This means that their lower quartile thresholds appear much higher than they would be were these workers included.

Highest to lowest paid workers

The exclusion of indirectly employed workers - coupled with the lack of data on pay for employees below the lower quartile threshold - is a weakness of the disclosures.

Many commonly outsourced roles are in low-paid occupations, so their omission will have a significant impact on the recorded pay ratio in many cases. Box 2 highlights their prevalence and the extent to which many leading companies rely on them.

Box 2: Workers excluded from the pay ratio calculation

As we have noted throughout the report, the pay ratio calculations do not include certain types of worker who many people would understand to be working for a particular company. We have highlighted how Shell, for example, uses a franchise model for its petrol stations, meaning that their staff are employed by the franchisee rather than Shell, even though they work in Shell-branded outlets. Other companies such as Intercontinental Hotels and Dominos also use a franchise model.

In the construction sector, many self-employed workers are engaged on building sites on behalf of major building and construction firms without being counted amongst their employees. It is noticeable that Morgan Sindall (£50,249) Persimmon (£33,409) and Taylor Wimpey (£41,483) in our sample have median pay levels much higher than the £24,964 suggested by Unite the Union as a typical rate for a construction worker within the National Vocational Qualification level 2 band covering the largest number of workers in the sector.

Insights from Unite, who represent many outsourced workers across the companies in our sample, provide further indication of the extent of outsourcing of low-paid work. In the financials industry, Aviva, Barclays, HSBC, Lloyds, M&G, Phoenix, Prudential, RBS and RSA amongst others have outsourced roles in areas including facilities management, post-room, scanning, cleaning, catering, maintenance and pensions administration.

However, it is possible to make a crude estimation of the pay ratios between the CEO and their very lowest paid workers by using annualised equivalents of the Real Living Wage and the statutory minimum wage (also now branded as the 'National Living Wage').

The Living Wage Foundation accredits employers that pay a 'real Living Wage' (to all workers, including indirectly employed staff if they work for 2 or more hours a week, for 8 or more consecutive weeks a year) that independent experts calculate is the minimum needed to support a decent standard of living.

For those companies accredited by the Living Wage Foundation, we have assumed their lowest paid workers are paid £16,926, the annualised 2019/2020 hourly Living Wage rate of £9.30, based on a 35-hour week. For non-accredited companies, we have assumed that they are paid the annual equivalent of the statutory national minimum wage 2019/2020 rate for those aged 25 and over, based on a 35-hour week, which is £14,942.

Using this calculation, the median CEO/low paid worker (i.e. national minimum or real living wage earner) ratio is 130:1, significantly higher than the median CEO/lower quartile employee ratio of 71:1.

For FTSE 100 companies, the ratio is 214:1 compared to the median CEO/lower quartile employee ratio of 109:1. Table 10 shows the ten largest gaps between companies' CEOs and the annualised equivalent of either the real living wage (if the company is an accredited living wage employer) or the national minimum wage.

Table 10: 10 highest CEO/low paid worker ratio

Company	Index	Industry	Living/ minimum wage (£)	CEO/low paid worker ratio
Ocado	100	Retail	14,942	3,930
Astra Zeneca	100	Health Care	16,926	847
BP	100	Oil & Gas	16,926	613
Experian	100	Industrial Goods & Services	16,926	608
Royal Dutch Shell	100	Oil & Gas	14,942	585
CRH	100	Construction & Materials	14,942	550
Berkeley	100	Consumer Goods	14,942	537
RELX	100	Media	16,926	513
GSK	100	Health Care	16,926	495
Prudential	100	Insurance	14,942	450

This table suggests potential extreme pay differences within UK companies, with several CEOs making 500- or 600-times workers on the minimum or living wage. As with the very high ratios identified in section 1 of this report, it will be important for stakeholders to establish how accurate these estimates reflect highest to lowest earner pay gaps at UK companies and their impact on factors such as employee well-being, morale and commitment to the company.

05 The potential to redistribute

This section examines pay ratios between the upper and lower quartiles, highlighting the companies with the highest ratios. It also discusses hypothetical redistributions from the upper to the lower quartile, examining what difference various levels of redistribution would make to the lower earners and at what cost to the higher earners.

The 'opportunity cost' of high pay

Our analysis of pay ratio disclosures so far has provided insights on intra-firm inequality at some of the UK's biggest employers. This can inform the understandable moral concerns about whether the prevailing CEO pay levels and CEO worker pay gaps can be justified, and also the rich academic, business and policy debate around the impact on issues such as democracy, health and wellbeing, social cohesion and economic productivity.

However, in practical terms it is important to examine the 'opportunity costs' associated with top pay - particularly in terms of the cost to low earners. We can use the pay ratios to help understand the degree of potential redistribution that might be possible within firms, if they reallocated some of their expenditure on the pay of high earners to those in the middle and at the bottom.

Redistributing CEO pay

Some of the largest CEO pay awards on their own could make a substantial difference to the incomes of lower earners if shared more evenly. Most obviously, if £57m of Ocado's CEO award of £58m was shared amongst all of the company's 15,000 employees, each employee would receive a bonus of £3,800; a very significant amount compared to Ocado's median pay of £22,500. This would still leave Tim Steiner, Ocado's CEO, with an award of £1m.

Of course, Ocado is something of an outlier. However, there are other examples of companies where redistributing from the CEO to low and middle earners would also result in a substantial pay rise for the low and middle earners. At Watches of Switzerland, redistributing £5.5m of the CEO's £6.5m award would result in a bonus of over £5,000 for roughly 1,000 employees earning less the median pay of £24,900. At IWG, redistributing £3.5m of the CEO's £4.5m award would result in an award of £1,400 for the 2,400 employees earning below the lower quartile threshold of £19,400.

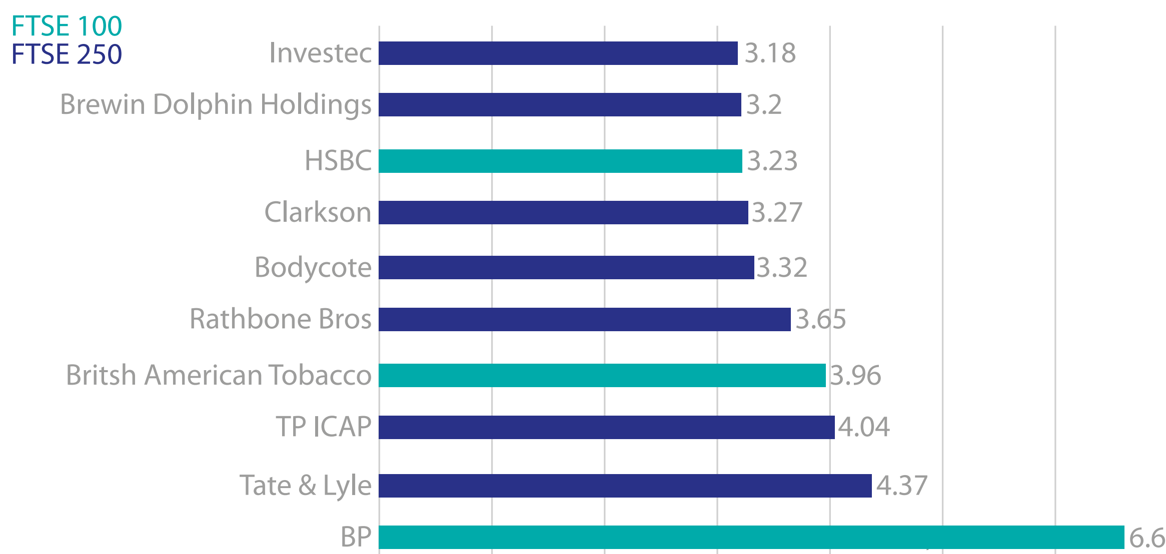
More generally, a CEO pay award of £5m (there are 23 in our sample who earn at least this amount) equates to the equivalent cost of 295 workers earning the 2019/20 UK real living wage for a year. £5 million could raise the pay of 2,520 minimum wage workers to the real living wage.[21]

[21] This calculation uses the annualised statutory national minimum wage at the 2019/2020 rate for those aged 25 and over, based on a 35-hour week, which is £14,942, and the annualised 2019/2020 Living Wage hourly rate of £9.30, based on a 35-hour week, which is £16,926.

Upper quartile to lower quartile pay gaps

However, even in the case of CEOs paid millions, the pay of one individual may not be enough to enable major pay increases if shared across hundreds or thousands of their colleagues. But redistributing from top earners more broadly could potentially result in much bigger gains for those in the middle and at the bottom. Looking at gaps between upper and lower quartile earners as detailed in the pay ratio disclosures offers some insight into the scale and limitations of this potential at different companies.

Figure 4: 10 highest upper quartile/lower quartile ratios



Perhaps the most striking aspect of the upper quartile to lower quartile ratios is that even the widest gaps shown in figure 4 are small compared to those between CEOs and the median. In this respect, the disclosures mirror income distributions across society as a whole.

Research by the Autonomy think-tank (based on the Annual Survey of Hours and Earnings 2019) as part of a project with the High Pay Centre estimated that the threshold for the top 1% of UK full-time workers was just over £150,000 while the threshold for the top 0.1% was around £388,000.[22] That same year, the thresholds for the median and the 75th percentile of UK full time workers were respectively just over £30,000 and £43,000.

In other words, the ratio of the 75th percentile to the median is significantly smaller than the 99th percentile to the 75th, which in turn is only slightly larger than the ratio of the 99.9th to the 99th points.

Similarly, the median upper quartile pay threshold for the companies that have disclosed is £59,133. This is a substantial sum of money that would put someone earning a full-time salary of this amount close to the top 10% of the highest-paid full-time UK workers. However, it is not what most people would consider to be seriously rich.

[22] Autonomy, Paying for Covid: capping excessive salaries to save industries, 2020 via https://autonomy.work/portfolio/payratios/

Upper quartile to lower quartile redistribution

As the pay ratio disclosures provide no further breakdown of pay between the 75th percentile and the CEO, we can only confidently estimate hypothetical redistributions from the top quarter of earners to the lower quarter on the basis of the top quarter employees earning the amount disclosed for earnings at the 75th percentile (in reality, they all earn at least this amount, with many making vast amounts more).

On that basis, redistributions from the median upper quartile threshold to workers in the lower quartile would have the following value per worker:

Table 11: hypothetical redistributions from median upper quartile threshold to lower quartile earners

% redistribution from median upper quartile threshold to lower quartile earners	Median increase in pay for lower quartile earners
1%	£591
3%	£1,774
5%	£2,957
10%	£5,913

This table conceals the fact that there is huge variation between companies in terms of the scope for redistribution. At many companies with the lowest-paid workers, even those in the upper quartile are also paid very little: these are often companies in the retail or travel and leisure industries where pay distribution tends to be fairly flat.

Conversely, at those companies with the highest upper quartile thresholds, the lower quartile thresholds are still well above the median threshold of gross earnings for the UK as a whole.

To illustrate this, the table below shows the five companies with the lowest lower quartile thresholds and the upper quartile thresholds at those companies, and the five companies with the highest upper quartile thresholds and their lower quartile thresholds.

Table 12: Companies with the 5 lowest lower quartile thresholds and 5 highest upper quartile thresholds

5 companies with lowest lower quartile thresholds	Industry	Lower quartile threshold (£)	Upper quartile threshold (£)
Mitchells and Butlers	Travel & Leisure	14,014	15,881
Associated British Foods	Consumer Goods	14,175	24,026
WHSmith	Retail	14,276	17,034
Homeserve	Retail	14,493	32,232
Wetherspoons	Travel & Leisure	14,760	27,333
5 companies with highest upper quartile thresholds	**Industry**	**Lower quartile threshold (£)**	**Upper quartile threshold (£)**
TP ICAP	Financial Services	57,064	230,554
Man Group	Financial Services	83,084	227,235
Standard Chartered	Banks	83,000	212,000
Tate & Lyle	Consumer Goods	46,064	201,522
British American Tobacco	Consumer Goods	46,216	183,179

In the case of the companies with the five lowest lower quartile pay thresholds, the upper quartile earners are also not especially well-paid, suggesting that there would be little case to redistribute to the bottom quarter by reducing pay of employees at the upper quartile threshold.

Conversely, at the companies with the five highest upper quartile thresholds, even those at the lower quartile earn comfortably above the amount that Autonomy estimate to be an upper quartile salary across the UK economy as a whole.

Of course, this could still mean there is scope to redistribute from top earners above the upper quartile threshold in the former group of companies. Similarly, there may be a pressing need to raise the pay of low-paid employees below the lower quartile in the latter group. It is just that we cannot gain any insights to this effect from the pay ratio disclosures.

There is, however, greater scope for substantial pay redistribution from the upper quartile to the lower quartile at other companies in the sample. Table 13 highlights ten companies where the upper quartile workers earn at least £50,000 and the lower quartile earn under £25,000. In each case, a redistribution of 3% from upper to lower quartile makes only a small difference to the earnings of the latter group while increasing the pay of the latter group much more substantially.

Table 13: redistribution from upper quartile to lower quartile earners

Company	Lower quartile threshold (£)	Upper quartile threshold (£)	3% of upper quartile threshold (£)	Lower quartile threshold following redistribution (£)	Upper quartile threshold following redistribution (£)
BP	19,108	126,085	3,783	22,891	122,312
Bodycote	22,379	74,341	2,230	24,609	72,111
Capita	19,147	57,049	1,711	20,858	55,338
Intercontinental Hotels	18,786	57,383	1,721	20,507	55,662
RSA	23,152	59,663	1,790	24,942	57,873
Paragon Banking	24,000	54,000	1,620	25,620	52,380
Inchcape	24,000	52,000	1,560	25,560	50,440
Burberry	24,000	52,000	1,560	25,560	50,440
Dechra Pharmaceuticals	24,000	57,000	1,710	25,710	55,290
One Savings	24,600	61,500	1,845	26,445	59,655

It is worth re-emphasising that top quartile earners at these companies earn **above** the upper quartile threshold, and lower quartile earners earn **below** the lower quartile threshold: there is, therefore, potential to raise pay for lower earners significantly with even more minimal redistribution from those in higher earning brackets.

The treatment of indirectly employed workers by the pay ratios is very relevant to calculations of the potential to re-balance pay distribution. Including large numbers of low-paid workers may alter the balance between the upper and lower quartiles of the workforce, meaning redistributions from top earners would have to be shared amongst a much larger group of lower earners, leading to smaller increases.

This would not necessarily affect potential redistributions at all the companies in our sample, but looking at Table 13, for example, Intercontinental Hotels employs a franchising model which means that many lower-earning hotel workers are not included in the ratio calculation. Therefore, there is perhaps less potential to raise incomes for lower earners significantly through a re-balancing of pay than the pay ratio disclosures suggest.

It is important to be clear that this report is not necessarily calling for the enactment of the potential pay redistributions we outline. Even in the cases where hypothetical redistributions from high to low earners would yield real benefits to the latter group while costing the former little, it might be challenging to ask upper quartile earners to accept pay reductions, even by the small amounts suggested.

However, the hypothetical redistributions would not have to take the form of an immediate subtraction from the pay of high earners and addition to that of those in the middle and at the bottom. They could instead serve as a guide or target for companies seeking to improve the pay of those that need it most for a more equal pay distribution over the longer term, and could be enacted not by pay cuts but by reducing pay increases for those at the top whilst raising pay more substantially for those at the bottom over several years.

Given the context of pay stagnation and pay inequality in the UK, the possibility of rebalancing pay in this way should be of considerable interest to stakeholders including businesses, investors, trade unions and policymakers.[23]

Top pay between the upper quartile threshold and the CEO

In order to understand the potential for changes to corporate pay distributions to boost lower and middle income workers by redistributing only from the very rich - those in the top 1% of the UK earnings distribution or higher, rather than those in the top 10% or 25% (where many of the upper quartile thresholds across our sample are located) - we need better information on what those at the very top beyond the CEO are paid relative to their colleagues. Data in quartiles does not provide sufficient granularity to do this.

[23] See for example, data showing the UK has the 9th highest income inequality of 40 members of the OECD group of advanced economies - OECD, Income inequality data, 2020 via https://data.oecd.org/inequality/ income-inequality.htm and figures showing that the UK has just endured its worst decade for pay growth for a century - Resolution Foundation, The economic history of the 2010s, 3 January 2020 via https://www.resolutionfoundation.org/comment/the-economic-history-of-the-2010s/

Box 3: Excessive incomes and a maximum wage?

Research by Autonomy cited in the previous section suggests a worker at the 99th percentile of the UK-wide earnings distribution (earning around £150,0000) makes roughly three and a half times as much as a counterpart at the 75th percentile.

In other words, their income enables a lifestyle far beyond the means of even those with above average pay, raising the question of whether earnings beyond this level represent an excessive reward or incentive for taking on more demanding roles.

Autonomy have used the research to support the argument for a 'maximum wage' with incomes capped in the low hundreds of thousands.[24] They argue that - across the UK as a whole - this could free up resources for those whose need is greater, and would represent a more efficient distribution of the prosperity generated by our economy.

This is perhaps a subject that merits wider discussion, including of how it might apply at the level of individual companies. Certainly, workers or their trade union representatives would be interested in their employers' expenditure on pay packages over a certain limit, and whether this could enable meaningful pay rises for lower earners if redistributed.

Similarly, information on a company's expenditure on very highly-paid employees could be relevant to investors, particularly if they felt that this money could be used more productively elsewhere (including in pay for the wider workforce) or simply returned to shareholders.

The UK-listed banks, which do provide more detailed disclosures, are an interesting case study in this respect. For example, the RBS 2019 annual report produced a table, replicated in figure 5, which shows the number of employees falling into particular pay bands.

Figure 5: RBS earners by pay band

Summary of remuneration levels for employees in 2019
46,152 employees earned a total remuneration of up to £50,000
12,117 employees earned a total remuneration of between £50,000 and £100,000
5,218 employees earned a total remuneration of between £100,000 and £250,000
910 employees earned a total remuneration of over £250,000

The banks also detail their total expenditure on 'material risk takers' (staff in the most strategically significant positions that would include most if not all of their highest-paid employees). At the 4 major UK-listed banks these individuals account for between 0.4% and 2% of the (global) employee population, and are currently paid on average between £400k and £900k.

A hypothetical redistribution from these high earners to lower-paid employees would significantly boost the wages of the latter group while the former would retain pay packages worth hundreds of thousands of pounds even after the redistributions had taken place.

[24] Autonomy/High Pay Centre, Paying for Covid: capping excessive salaries to save industries, 2020 via https://autonomy.work/wp-content/uploads/2020/10/2020OCT_SalaryCap_Ameneded.pdf

Table 14: Hypothetical redistribution at UK-listed banks (all figures for the year 2019)

Company	Total employees	Number of high earners (MRTs)	Spend on high earners (£m)	Value of 50% of high earners earnings per below-median employee (£)	Average high earner pay post hypothetical redistribution (£000)
Barclays	86,931	1,704	1,405	16,162	412
HSBC	247,055	1,159	1,048	4,241	452
Lloyds	70,083	292	157.8	2,252	270
RBS	64,200	751	327.21	5,097	218

Engaging on top pay

Banks are unusual in terms of their number of very high earning employees, so it is not necessarily the case that there is the same hypothetical potential to rebalance pay at companies in other industries.

At Lloyds, for example - a domestically-focused bank with the majority of staff based in the UK - the MRTs account for about 0.4% of the employee population, but consume around 4.6% of total expenditure on pay.

More detailed data is needed to understand how typical this is of corporate Britain - one would expect pay inequality within firms and expenditure on high earners to vary substantially by industry. However, there does appear to be considerable potential to significantly boost the pay of low earners by redistributing pay from those at the very top, with the latter group still remaining very well-paid by the standards of the wider economy, at some companies at least.

Given that the UK has just endured its weakest decade of pay growth for a century, this presents a strong case for more granular disclosure requirements relating to pay for high earners between the upper quartile threshold and the CEO.

In the meantime, the pay ratio disclosures may serve as a useful starting point for more detailed discussions between stakeholders - such as trade unions or investors - and companies on pay for top earners and the value and opportunity costs that result for the business.

06 Narrative reporting

This section examines the narrative reports that companies are required to provide to contextualise their pay ratio data, and examines how useful the initial reports have been for stakeholders.

Lack of narrative

As well as publishing the pay ratio data itself, companies are also required to provide a 'narrative' to explain the size of the pay ratios. This is an important requirement, given that, as discussed, the data on its own does not explain a company's pay structure or its employment model. A qualitative explanation of the pay ratio data can add useful context for stakeholders in this respect.

We found that a large number of companies provided little or no narrative. This is particularly concerning in the case of companies with low workforce pay and/or high pay ratios, where we would want to see companies providing an explanation of pay levels and ideally what actions might be taken to distribute pay more fairly. For example, Homeserve, Dunelm and Wetherspoons, all of which have lower quartile thresholds of under £17,000, provided no accompanying narrative to their disclosures.

Engaging with stakeholder concerns

Whilst some companies provided a more detailed narrative, explaining, for example, the workforce profile or the company's employment model, there has been very little engagement with any of the criticisms of pay gaps regarding fairness or proportionality, or discussion of how the board are planning to use the pay ratio data in the future in order to address these criticisms.[25] The statements also do not engage with the gaps between the upper quartile, median and lower quartile thresholds. As we have shown in the previous section, these are potentially material to employees' absolute pay levels and will be of as much interest to them as the gap between them and the CEO.

As we discussed in the interim report, in the cases where low pay is accompanied by a narrative, justifications of this tend either to stress the 'diversity' of roles within the workforce or to point out that most staff are in roles which are not highly valued by the market. For example, BP's annual report states that the pay ratio includes workers 'who are employed in roles which attract relatively lower market rates of pay'. Similarly, JD Sports, which has a lower quartile threshold of £16,067, says that its pay is 'in line with typical practice in the retail sector'. The responsibility for low pay is thus shifted away from the company and onto 'the market'. Companies are not forbidden from paying higher than the market. Indeed, for some larger employers, market rates in their sector are a consequence of their decisions on pay as well as vice versa.

[25] One of the better examples of narrative reporting is Experian's 2020 Annual Report, which explains that they have a Sharesave scheme available to all employees, that eligibility for Long-Term Incentive Plans has been expanded to more employees this year, and that they have been paying the Living Wage since 2015.

Box 4: Corporate purpose

Directors' responsibilities as outlined in section 172 of the 2006 Companies Act are to 'have regard' for the interests of all stakeholders, including their workers when carrying out their duties as Directors.[26] Concepts such as 'purposeful business' or 'stakeholder capitalism', which argue that businesses should prioritise good outcomes for workers and wider society at least as highly as financial returns, are being discussed increasingly seriously by academics, business leaders and commentators.[27]

In this context, how boards sustainably marry their objectives in terms of pay for their workers and returns for their shareholders, and how this is borne out in their pay distribution, is an important aspect of their business philosophy that might be discussed in pay ratio narrative reporting, or elsewhere in annual reports. However, this is currently very rarely the case. Research by Grant Thornton found that just 6% of FTSE 350 companies provided meaningful statements of corporate purpose beyond profit backed by measurable performance indicators.[28]

'Copy and paste' reporting

We also noted in the interim report that a large number of companies use very similar wording in their narratives. For example, Rentokil's annual report states that:

> 'The median pay ratio is consistent with the pay, reward and progression policies for the Company's UK employees taken as a whole.'

ITV uses almost exactly the same phrase:

> 'The median pay ratio for 2019 is considered to be consistent with the pay, reward and progression policies for the Company's UK employees taken as a whole.'

HSBC, Tesco, IMI, Spectris, WHSmith and Drax also use very similar variants of this in their annual reports. This phrase is taken from the reporting regulations, which state that the company should explain:

> 'whether, and if so why, the company believes the median pay ratio for the relevant financial year is consistent with the pay, reward and progression policies for the company's UK employees taken as a whole.'[29]

Several companies have provided explanations of why they believe this statement to be true, though in some cases they provide minimal explanations of their employee pay policies, only saying that employee's packages are set with reference to the external market. More concerningly, others have simply stated that their median pay ratio is consistent with their pay, reward and progression policies for employees, and have not explained why this is the case.

[26] UK Government, Companies Act 2006 via https://www.legislation.gov.uk/ukpga/2006/46/section/172

[27] For examples, see Financial Times, Capitalism: Time for a Reset, 16 September 2019 via https://aboutus.ft.com/en-gb/announcements/ft-sets-the-agenda-with-new-brand-platform/ or British Academy, Principles for Purposeful Business, 2019 via https://www.thebritishacademy.ac.uk/publications/future-of-the-corporation-principles-for-purposeful-business/

[28] Grant Thornton, Corporate Governance Review:2020 via https://www2.grantthornton.co.uk/corporate-governance-review-2020.html?_ga=2.55819883.1335805288.1606923606-433553438.1606923606

[29] UK Government, Companies (Miscellaneous Reporting) Regulations 2018, via https://www.legislation.gov.uk/ukdsi/2018/9780111170298

Engaging on narrative

It is important to note that companies may be sensitive to criticism that annual reports, and the remuneration report sections in particular, have become overly long (with remuneration reports in excess of 20 pages now commonplace). However, statements such as the above, which tell us little about the company's pay practices, could easily be replaced with something more insightful.

The pay ratio disclosures have been complemented by a number of other recent corporate governance and stewardship reforms. These include the 2019 update to the Stewardship Code, setting expectations of the investment industry in terms of their engagement with investee companies. The 2018 Corporate Governance Code requires companies to report on their engagement with their stakeholders, and to introduce one of three mechanisms to promote worker voice in strategic decision-making: worker directors on boards, non-executive directors with specific responsibility for stakeholder issues, or stakeholder committees.

Narrative pay ratio reporting is very relevant to both of these initiatives. Executive pay practices have historically been a key area of engagement between investors and companies, while other stakeholders – particularly the company's workforce - have an obvious interest in pay ratios and pay distribution. Therefore, we would expect both investors' stewardship activities and stakeholder representation mechanisms in corporate governance structures to encourage useful narrative reporting on these topics in future.

Conclusions and recommendations

This section summarises the key insights from our research and highlights the debates we hope that it will prompt. It also discusses some of the limitations we have identified in the pay ratio disclosures. Finally, it makes recommendations for how the pay ratio disclosures could be improved in both policy and practice going forward.

Insights from pay ratio reporting

The initial disclosures under the pay ratio reporting requirements yield a number of insights and suggest several potential avenues for further research as well as action.

Specific insights include:

- The median pay ratios and the typical thresholds for upper, median and lower quartile pay for particular industries and sectors. Provided they are not used to make sweeping or instant judgements, this data provides useful evidence to inform vital discussions between companies and their investors, workers, trade unions and other stakeholders about their employment models and the link to their wider strategy. Data on Environmental, Social and Governance (ESG) issues is becoming increasingly important to investors, and pay distribution relates closely to the 'S' in ESG, which has become even more relevant given the interest in how companies are treating their workers in the aftermath of the coronavirus outbreak.
- The scale and variation in pay gaps within the UK's largest listed companies, ranging from between 10:1 and 20:1 at the companies with the lowest CEO/median employee ratios to between 200:1 and 300:1 at those with the highest, with Ocado as an outlier at 2,605:1. These gaps become even larger when we look at the gap between the CEO and a worker earning the minimum or living wage.
- Even though we know that the pay ratio disclosures understate the extent of low pay in the UK, they nonetheless show a concerningly high prevalence of low pay amongst the FTSE 350. There are 11 companies where the threshold for lower quartile earnings is lower than the annualised equivalent of the Real Living Wage for a 35-hour week, and 34 where the lower quartile threshold is lower than the annualised London Living Wage.[30] This suggests that there are a number of employees at these large, high value companies struggling with the cost of living – even before indirectly employed workers are taken into account.
- The distribution of pay across the workforce varies widely between companies. In some companies, there is scope for a hypothetical re-balancing of pay distribution: a small proportion of top pay redistributed from the top quartile to the bottom would make a huge difference to the incomes of lower quartile earners, without drastically reducing the incomes of those in the top quartile. It is also the case for some companies that redistributing some of the CEO's pay would make a substantial difference to those on low incomes. In other companies, however, we would need more granular information on pay in order to identify opportunities for meaningful redistribution.

[30] The Real Living Wage and the London Living Wage are both calculated by the Living Wage Foundation and are minimum standards that companies can adopt on a voluntary basis.

The research also suggests a number of factors which could be relevant to the size of pay ratios, and which could inform debate around why CEOs and different types of workers at different points of the organisational pay distribution are paid what they are:

- Industry
- Trade union influence
- Employment model
- Company size, in terms of both market capitalisation and employee numbers
- Company debt
- Company complexity

Questions for stakeholder engagement

Given that policymakers, business leaders, trade unions and many other stakeholder groups all have an interest in raising the incomes and living standards of UK workers - particularly the lowest paid workers - the pay ratios are a critically important issue to debate. We hope that these insights can lead to further discussion, research and ultimately improvements to policy and practice in relation to pay. Questions that might begin this discussion could include:

- How can we value low-paid but essential jobs more highly, and what measures can we take to raise the pay of these workers?
- How can we expand trade union membership across more companies, and what would be the implications of this?
- How will investors and the directors and committees responsible for workforce representation in corporate governance structures engage with pay ratio disclosures – particularly in terms of explanations of pay structures and their link to the company's broader strategy and business model?
- Should increased company size necessarily result in higher CEO pay and why/why not?
- How should pay ratio reporting and pay ratios within companies relate to concepts of corporate purpose, and the responsibilities of businesses to stakeholders beyond their shareholders?

Limitations of the pay ratio disclosures

Whilst acknowledging the vital and informative resource that the first year of pay ratio disclosures provide, it is also important to identify their limitations. These include:

- The exclusion of outsourced workers. Given the prevalence of outsourcing in the UK economy, this likely affects a large proportion of the companies that have disclosed, meaning that the pay ratios do not give an accurate picture of pay levels in these companies. This makes it difficult to compare companies, especially those with different employment models. This should prompt a discussion about the use of outsourced or franchised employment and business models and their implications for stakeholders including the business, their investors, the workers themselves and wider society.
- The exclusion of privately-owned UK companies or foreign-owned firms operating in the UK. Only UK-listed companies are required to disclose their pay ratios, and many of these base the majority of their operations overseas - it is striking that over a third of the FTSE 350 will not provide pay ratio figures because they do have enough employees in the UK to obligate disclosures. Conversely, many organisations that are major employers are not subject to the requirements because they are not listed. Given that we are interested in the pay and working conditions of all UK workers, this is a major shortcoming. This challenge is compounded by the fact that the majority of companies in the sample do not disclose their number of UK employees.

- The lack of information on the pay of those between the top quartile and the CEO. The top quartile covers everyone from CEOs typically earning millions of pounds to those at the 75th percentile, some of whom are undoubtedly comfortable, but not what most people would consider excessively rich.

Recommendations for better reporting

Given that this is the first year of pay ratio disclosures, it's unlikely that the government will review or change the requirements until they have been in place for at least two or three years.

However, investors, unions, employees and other stakeholders can still push individual companies to change their practices with immediate effect. The recommendations below can therefore be understood both as policy recommendations for the future and as changes that stakeholders should encourage companies to make voluntarily.

- **Companies should provide more granular information on the earnings of those between the upper quartile threshold and the CEO**. The disproportionate share of incomes captured by those at the very top is one of the biggest issues relating to economic inequality in the UK, and more information on how this occurs at particular employers would contribute to our understanding of how to achieve a fairer share of incomes accruing to those in the middle and at the bottom. Possible models for granular reporting could include reporting on those with pay awards of over £150k, or on the pay of the top 1% of the company's employees.
- **Outsourced UK workers should be included in the pay ratio calculations,** since these workers are vital to the companies' operations and often make up a large proportion of workers. Their inclusion would provide a more accurate picture of companies' pay practices and would also make it easier to compare companies. An important question here is which indirectly employed workers should be included in the calculation. We suggest using the Living Wage Foundation's standard for 'regularly contracted staff' which covers 'contracted staff who work 2 or more hours a week, for 8 or more consecutive weeks a year'.[31]
- **Higher standards and clearer expectations of narrative reporting** around the ratios could enable better understanding of the link between pay distribution and business strategy. We would suggest that companies should explain 1) how boards plan to use the pay ratio disclosures going forward, 2) whether and to what extent workers and investors feed into the pay-setting process, and 3) to what extent raising pay for low- to middle-income workers and reducing inequality is a priority for the company. However, we are aware that many remuneration reports are already overly long, making it difficult for stakeholders to find the information they need, so we suggest that rather than simply adding this information, companies should reshape remuneration reporting to put more emphasis on pay across the workforce.
- **Companies should directly provide information on pay ratios to their workers.** The objective of pay ratio disclosures is to empower low- and middle-income workers to achieve better pay and working conditions - if individuals have more information about pay levels across their workforce, this can strengthen their bargaining position in relation to their own pay. However, company annual reports are long and confusing, and it is unrealistic to expect a critical mass of workers to read through them in order to access pay distribution data. Companies that are confident that their pay practices are fair ought not to be afraid of discussing them - therefore, CEO pay levels and pay ratio data should be circulated to all employees in an individual letter, as well being published in annual reports.

[31] Living Wage Foundation website, 'FAQs', via https://www.livingwage.org.uk/faqs#t136n1755

- **Companies should provide data on their number of UK employees.** One of the major gaps in the pay ratio data is that, while it shows the gaps between the CEO and the different quartiles of the workforce, it does not include the number of employees covered (even though this information needs to be calculated in order to provide the ratios). As such, it becomes challenging to assess the wider importance of the different companies' pay practices, to prioritise analysis of individual companies or to accurately calculate the number of workers that would benefit or lose out from more even pay distribution. External scrutiny is undoubtedly one of the factors shaping corporate pay practices, so if this scrutiny is more informed/accurate that ought to result in fairer pay.
- **Apply the pay ratio disclosure requirements to all large employers**, giving a more complete picture of the pay inequality, governance, workplace culture and potential for redistribution that the disclosures provide across the UK. How large employers distribute their pay has socio-economic implications for the UK regardless of whether or not they are listed on the stock market. Therefore, all those companies that are expected to comply with the Wates Principles for Corporate Governance of private companies, as well as institutions that are large employers such as universities, hospitals and local authorities, should be subject to the same pay ratio disclosure requirements as those with a premium listing.[32]

Recommendations for wider policy change

Whilst the purpose of this report is to analyse the pay ratio disclosures and identify ways in which they can be improved, the High Pay Centre's ultimate aim is to raise pay for low and middle earners in the UK. We therefore propose a number of accompanying recommendations that would complement the pay ratio disclosures, and ensure that the information they provide is used to support efforts to improve low- and middle-income workers' pay and working conditions:

- **Allow trade union access to workplaces, to inform workers of the benefits of collective bargaining:** Companies which negotiate with trade unions deliver higher rates of pay for low and middle earners, as suggested by examples in this report and by wider research.[33] Union representatives can use the pay ratio disclosures to build arguments in support of improved pay and working conditions, and highlight unfair pay gaps in a way that may be more challenging for unrepresented individual workers.
- **Establish sectoral governance bodies to monitor fair pay.** These bodies could be made up of stakeholders including representatives from business, unions, workers and government in a similar fashion to the Wages Councils, which were in place in the UK until the 1990s. Their remit could include setting guidelines for minimum wages and pay ratio limits across the sector, using pay ratio disclosures to inform recommendations.
- **Legislate for worker representation on company boards.** This would allow workers to play a meaningful part in the governance process, and would provide a voice at the highest level of the company making the argument for more even pay distribution. The UK Corporate Governance Code gives companies the option to appoint/elect worker directors as one of three options for introducing stakeholders into their corporate governance structures, but this option has only been taken up in a tiny number of instances.

[32] Those with over 2,000 employees and/or turnover of £200 million and a balance sheet of £2 billion.

[33] See e.g. Bryson A and Forth J, The added value of trade unions: New analyses for the TUC of the Workplace Employment Relations Surveys 2004 and 2011, TUC, 2017 via https://www.tuc.org.uk/sites/default/files/1%20WERS%20lit%20review%20new%20format%20%20RS_0.pdf

- **Require companies to introduce all-employee profit sharing or share ownership schemes.**[34] One of the reasons why some of the pay ratios between workers and CEOs are so wide is that CEOs receive large share-based payments in addition to their regular salary while workers do not, even though workers also deserve to be rewarded for good company performance. It is essential that these schemes cover all, not just part, of the workforce. In France all companies are required to share an element of profits exceeding a set amount calculated using factors including taxable profits, net equity, wages and added value with their workforce. A similar requirement could be replicated in the UK.
- **Amend company law to give the interests of all stakeholders equal importance, rather than elevating shareholder interests above those of others**. The 2018 Companies (Miscellaneous Reporting) Regulations introduced a requirement for directors to report on how they have complied with their section 172 responsibilities to have regard for stakeholders beyond shareholders. This is a welcome development, but does not go far enough. A duty to run the company using a balanced judgement of the long-term interest of all stakeholders would encourage boards to think more deeply about pay distribution at their company and how to improve pay and conditions for the majority of their workforce.
- **Give shareholders binding votes on directors' remuneration reports**. Whilst shareholders have a binding vote on a company's remuneration policy, their vote on the remuneration report - i.e. the executive pay packages - is only advisory. This can result in instances where a majority of shareholders oppose the remuneration report - including the pay ratio - but it remains unchanged. This was the case with Tesco in 2020, when two thirds of the shareholders opposed the remuneration report.[35] The CEO's remuneration was not altered, however, and as a result Tesco has the 3rd highest median pay ratio this year at 305:1.
- **Require companies to include guidance on potential future pay ratio sizes in their remuneration reports.** The 'Large and Medium Size Companies Regulations 2013' requires companies outline maximum, minimum and 'target' values for executive pay awards in the forthcoming year.[36] These disclosures should also include guidance on maximum, minimum and target pay ratio sizes over the next three years. This would enable shareholders to take future pay ratio size into account when considering their votes at company AGMs, thereby encouraging better stewardship of pay practices on a company-wide basis, rather than just at board level.

Taken together, these measures would boost transparency, governance and accountability to stakeholders at the UK's biggest businesses, while strengthening the bargaining power of low- and middle-income workers, and significantly improving living standards.

[34] For more detail on the design of these schemes see Social Market Foundation, Strengthening employee share ownership in the UK, February 2020 via https://www.smf.co.uk/wp-content/uploads/2020/02/ Employee-Share-Ownership-February-2020.pdf

[35] Guardian, Tesco hit by shareholder revolt over executive pay, 26 June 2020 via https://www.theguardian.com/business/2020/jun/26/tesco-sales-soar-as-customers-turn-to-deliveries-in-pandemic-coronavirus

[36] UK Government, The Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013 via https://www.legislation.gov.uk/ukdsi/2013/9780111100318/schedule

Appendix A: Methodology

This report is based on analysis of all the FTSE 350 companies to provide pay ratio disclosures prior to 30 November 2020.

Over the time period covered, a total of 186 FTSE 350 companies covered by the pay ratio reporting requirements (78 from the FTSE 100 and 108 from the FTSE 250) published annual reports in which pay ratios were disclosed. This excludes closed-end investment funds and companies with under 250 UK employees.

In addition to these mandatory disclosures, we have included some voluntary disclosures. 15 companies which have not yet published their annual reports made voluntary disclosures in 2019. This brings the total number of disclosures up to 201, which represents over 90% of companies that are required to disclose.

For the analysis detailed in Section 3, we commissioned Dr Aditi Gupta at Kings' Business School, Kings' College London, and data analyst Steve Glenn of E-Reward to analyse the impact of specific company characteristics on pay ratio size.

Dr Gupta carried out statistical tests using the High Pay Centre's pay ratio data and Kings' College London's databases to analyse the relationship between pay ratios and a range of company characteristics. She undertook a series of univariate tests looking at the relationship between pay ratio size and other individual variables, including proxies for company size and company performance. She also carried multivariate tests controlling for multiple different company characteristics such as firm age, productivity, market-to-book ratio and firm assets.

Steve Glenn of E-Reward supplemented this analysis with a study of the correlation between companies' three-year share price change, and their pay ratio.

Steve Glenn used the same sample of companies as the High Pay Centre, but excluded Ocado for the share price change analysis as Ocado is an outlier. Dr Gupta's sample consisted of the mandatory disclosures only and excluded the voluntary disclosures.

Appendix B: Pay ratio disclosure requirements

The *Companies (Miscellaneous Reporting) Regulations,* introduced by Theresa May's Conservative government as part of a broader programme of corporate governance reform, require all UK-incorporated companies with a premium stock market listing and over 250 UK employees to publish 'pay ratios', showing the relationship of their CEO's pay to other employees in the company.

The regulations stipulate that companies must publish a table in their annual remuneration report showing CEO pay relative to pay at the 75th, median and 25th percentile of the company's UK employees. That is to say, if all the company's UK employees were ranked from highest to lowest in terms of their total pay (on a full time equivalent basis) how would the CEO's pay compare to the thresholds for the upper quartile (i.e. the 75th percentile, earning more than 75% of employees), the median (exactly in the middle of the ranking) and the lower quartile (the 25th percentile, earning more than 25% of UK employees).

UK employees include everyone employed by the company under a contract of service, excluding those who work wholly or mainly outside the UK. Indirectly employed workers also excluded.

CEO pay must be calculated using the existing formula for the so-called 'single figure' of total remuneration, encompassing salary and all forms of pay and benefit including pensions, bonuses and share awards. The employee total remuneration figure, provided at the 75th, median and 25th percentile, includes salary, taxable benefits, cash bonuses, share-based pay and pensions. It should be calculated 'wherever possible' by determining pay for all UK employees (on an FTE basis), ranking them on a low-to-high basis and identifying the employees whose remuneration places them at the upper, median and lower percentile points (option A).

Alternatively, companies may calculate the 25th, 50th and 75th percentile points based on their gender pay reporting disclosures, which require them to identify the gender breakdown of employees in each pay quartile, and thus to calculate the thresholds for each quartile (option B), or they may use other existing pay data, provided it has been calculated no earlier than the previous financial year (option C).

The disclosure requirements apply to pay awarded for financial years beginning from 1 January 2019. Therefore, the first mandatory disclosures appeared in annual reports published in 2020 for financial years ending on or after 31 December 2019.

Standard Life
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Standard Life Foundation funds research, policy work and campaigning activities to tackle financial problems and improve living standards for people on low-to-middle incomes in the UK. It is an independent charitable foundation registered in Scotland.

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