Excessive executive pay

Explore the CIPD's point of view on excessive executive pay packages, including actions for Government and recommendations for employers

Excessive executive pay packages and a poor link to company performance undermine trust in business and are a symptom of poor corporate governance. There's a need to reform executive reward practices to ensure fairer alignment with the pay of the wider workforce, and a closer link between the contribution of business leaders and organisational performance.

Executive pay is out of kilter. Since the 2008 financial crisis, pay for FTSE 100 CEOs has risen while that of the average worker has failed to keep pace with increases in living costs. Between 2009 and 2019, median pay for CEOs rose from £2.27 million to £3.79 million in 2011 before oscillating around this mark for the rest of the decade. By contrast, between 2009 and 2019 median pay among full-time workers increased from £25,806 to £30,353. Yet remuneration committees (RemCos), which govern executive pay, can struggle to demonstrate (in their annual reports) a clear link between CEO pay and performance.

Excessive CEO pay packages and a poor or non-existent link to performance undermine trust in business. According to the 2019 annual Edelmans Trust Index, 62% of the public said that addressing the high pay and bonuses given to senior management and business leaders was either 'important' or 'very important' when it came to rebuilding trust in business.

FTSE 100 executive pay is often used as a benchmark by smaller companies to set the pay of their CEOs, and it can influence pay for other top earners and key decision makers within firms, so excessive remuneration in the UK's largest companies has a ripple effect across the whole economy.

Disproportionate rewards for top executives are a visible sign that corporate governance is failing, damaging trust in business among the workforce and wider society. Excessive executive pay can also damage employee morale and motivation – CIPD research finds that 60% of workers agree that CEO pay levels in the UK demotivate employees, with just 13% disagreeing.

To address this, an organisation's RemCo should ensure that executive remuneration is aligned to company purpose, culture and values, and be clearly linked to the successful delivery of the company's long-term strategy.

There should be a clear rationale and explanation of why executive remuneration levels are fair and appropriate using internal and external measures, including pay ratios and pay gaps.

Organisations should engage with the workforce to explain how executive remuneration aligns with wider company pay policy.

Pay for senior executives should be based on smaller and more immediate incentives rather than complex Long-Term Incentive Plans, and linked to both financial and non-financial measures of performance, including, for example, the level of investment in workforce training and development, or environmental impact.

- Review how employers are complying with the requirement to publish CEO pay ratios.

- Extend single-figure reporting requirements and guidance to cover key management personnel and the disclosure of pay for the top 1% of earners, to further improve transparency and ensure this area of reporting practice improves.

- The Financial Reporting Council should publish guidance for employers on extending the remit of remuneration committees to cover wider workforce issues, including culture, as recommended in the UK Corporate Governance Code.

- The Corporate Governance Code should be amended to also require publicly limited companies to report on the ethnicity of their senior management teams and their direct reports.

- Remuneration committees should broaden their remit beyond CEO reward (as recommended by the UK Corporate Governance Code). Instead of RemCos, firms should establish a formal committee to provide oversight on factors such as diversity, skills, stability and morale that influence pay levels and are, in turn, shaped by them.

- Demonstrate in annual reports how executive remuneration and pay practices more widely relate to their strategy for people management and corporate culture as well as how they relate to broader environmental, social and governance requirements.

- Invest in the company's HR analytics capability so that people, pay and organisational committees can use meaningful data to evaluate how effectively people throughout the organisation are managed, developed and rewarded. This data, as well as financial data, should be used to assess executive and company performance.

- Explore whether long-term incentive plans are a suitable way to remunerate CEOs and whether a less complex system based on basic salary (with a much smaller restricted share award as an incentive to deliver sustainable long-term performance) is more appropriate.

Reports

- Executive pay in the FTSE 100: 2020 review
- RemCo reform: governing successful organisations that benefit everyone
- Show me the money: the behavioural science of reward
- The power and pitfalls of executive reward: a behavioural perspective

Podcasts

- Executive pay and the psychology of motivation

Commentary

- The truth about executive pay