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CEO pay in the United Kingdom, 1968–2022

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ABSTRACT
This paper contributes to the literature on British business elites by examining the development of pay structures and levels for CEOs of large listed companies in the United Kingdom for the period 1968–2022. It describes two competing theories about executive pay, 'optimal contracting theory' and the 'market failure approach', and considers to what extent they help to explain the historical data. The paper notes how the imitation of American pay structures, especially stock options, in the 1980s, along with the ending of high marginal tax rates which had been prevalent in the UK in the 1960s and 1970s, coincided with steep rises in executive pay. It concludes that isomorphic social comparisons, a prisoner's dilemma at the heart of the work of remuneration committees, a collective action problem faced by institutional investors, and a discount that executives apply to the perceived value of stock options has resulted in top pay inflation.

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1. Introduction

Academic research on executive compensation has traditionally been the domain of economists, economic sociologists, and legal scholars. The geographical focus has primarily been on the United States, where the Standard & Poor's ExecuComp database means pay data is readily available. In the UK, data on individual director's pay was difficult to obtain prior to the publication of the Directors' Remuneration Report Regulations in 2002.[1] Reliable data for other countries in Europe has been equally hard to obtain.

In this paper I examine the remuneration of CEOs of large UK listed companies (defined as those included in the FTSE100 index and its predecessor, the FT30[2]) over the period 1968–2022. I draw on an original dataset, which has been constructed from four separate sources, which I describe. I focus on the UK, which sits between the US and continental Europe in terms of pay structures and pay levels. The UK's mediating role between the US and Europe makes the history of executive pay in the UK of particular interest (Edmans et al., 2023).

While there is an established literature on the history of British business elites—see for example, Fidler (1981), the collection of papers edited by Cassis (1994), and various outputs from the research project on international business elites and elite power led by Maclean;

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for example, Maclean et al. (2006)—until recently business historians have rarely shown much interest in top pay. The literature on business elites has typically focused on issues like the social origins of elites, class, culture, power and networks. Senior executive remuneration has been a topic of public interest in Britain for over forty years, a period which is long enough to be of historical interest (Rosen, 2013). Maclean et al. (2006) cover executive pay in their study of elites in Britain and France, arguing that the twin themes of business elites and corporate governance are inextricably linked. One of the contributions of this paper is to build on this idea, to show how historical research on top pay can be joined up with the literature on business elites. A second contribution of this paper is empirical, viz., the construction of a data set of the pay of CEOs of large listed companies in UK covering the period 1968–2022—further details about this data set are contained in Section 3. A third contribution is in trying to establish 'best fit' between the data and the two main theoretical approaches to executive compensation. I draw some parallels with the work of historically-minded economists Carola Frydman and Raven Saks, whose 2010 paper on US executive compensation for the period 1936–2005 is a notable example of research on pay that does take a long-term perspective (Frydman & Saks, 2010).

The paper proceeds as follows. In Section 2, I summarise two competing academic theories about executive pay—'optimal contracting' and the 'market failure approach'. In Section 3, I discuss materials and methods. Section 4 sets out the history of CEO pay in large UK listed companies for the period 1968–2022. In Section 5, I consider the extent to which the two theoretical approaches outlined in Section 2 help us to understand the historical data. Section 6 concludes.

2. Two competing theories

The traditional approach to corporate governance, after Berle and Means (1932), takes the separation of ownership and control as its point of departure. An alternative approach, which sets corporate governance against the background of the corporate malfeasance seen in the UK in the 1990s (Maxwell, BCCI, Polly Peck, etc.) and in the US in the early 2000s (Worldcom, Enron, Global Crossing, etc.) is predicated on the idea of 'securities against misrule' (Elster, 2013).[3] Within these overarching frameworks two rival theories try to explain the sharp rise in executive compensation over the last fifty years. The first, known as 'optimal contracting theory', is favoured by economists and most closely aligned with the approach to corporate governance based on the separation of ownership and control. Its historical origins lie in both shareholder primacy (Friedman, 1970) and agency theory (Ross, 1973). Agency theory postulates that, in order to motivate senior executives (agents) to carry-out actions and select effort levels that are in the best interests of shareholders (principals), boards of directors, acting on behalf of shareholders, design incentive contracts which make an agent's compensation contingent on measurable performance outcomes (Jensen & Meckling, 1976). The agency model is extended by tournament theory, which proposes that principals structure a company's management hierarchy as a rank-order tournament, and predicts that compensation is an increasing convex function of an agent's position in the hierarchy (Lazear & Rosen, 1981). Hikes in remuneration between levels in the management hierarchy vary inversely in proportion to the probability of being promoted to the next level. As a result, the compensation of the CEO, ranked highest in the tournament, will typically be substantially more than the compensation of executives at the next highest level.

The main problem for agency theorists is that empirical evidence has failed to establish a strong link between executive pay and the financial performance of firms, which agency theory predicts should be the case.[4] Most economists now appear to accept that the strongest empirical correlation is between executive pay and firm size, not financial performance (Baker et al. 1988; Gabaix & Landier, 2008). Optimal contracting theorists contend that this is not necessarily inefficient. They argue that big companies must attract the best management talent to run efficiently, because they are more complex and difficult to manage than smaller companies. They also argue that CEOs can have a multiplier effect on growth in firm value because their actions are scalable. A CEO whose strategic decisions double the size of a $10 billion company creates proportionately much more shareholder value than a CEO whose actions double the size of a $5 billion company. Therefore, big companies must provide the largest pay packets, which increase as a power relationship of the growth in company size (Edmans & Gabaix, 2016). It should be noted in passing that one obvious weakness of this approach is in accepting ex post that a correlation between CEO pay and company size is an acceptable outcome when aiming ex ante for a causal connection between CEO pay and firm performance.

The main alternative to optimal contracting theory is the 'market failure approach', favoured by economic sociologists and some legal scholars and aligned with the 'securities against misrule' perspective on corporate governance. It argues that top managers use managerial power to extract economic rents—payments in excess of the amounts which are economically or socially necessary (Bebchuk et al., 2002). Efficient markets require many buyers and sellers, free market entry and exit, plentiful information and little economic friction. The trouble with the market for top executives is that practically none of these conditions holds good. In the absence of accurate price signals, high pay is replicated across companies as remuneration committees benchmark the pay practices of other companies (DiPrete et al., 2010), and as they follow the recommendations of remuneration consultants (Bender, 2011). Regulatory constraints also cause pay structures and levels to replicate. Sociologists call this process 'isomorphism' (Di Maggio & Powell, 1983). Di Maggio and Powell identify three different types of isomorphism: mimetic isomorphism (imitation), which is a standard response to uncertainty; coercive isomorphism, which is the result of political pressure and the search for legitimacy; and normative isomorphism, which is associated with professional standards and the search for 'best practice'.

Mimetic isomorphism leads to a continuous ratcheting-up of top pay. This has been described both as a result of a 'Lake Wobegon Effect' (Hayes & Schaefer, 2009) and as the 'Remuneration Committee's Dilemma' (Pepper, 2022). Most companies believe that their CEOs are better than average—a mathematical impossibility. Paying over the odds becomes a dominant strategy in a prisoner's dilemma. Companies will generally be no better off by offering higher pay than if they all paid more modestly. However, paying over the odds might increase the probability of recruiting a top performer, and is better than running the risk of attracting an inferior CEO by paying less than the competitors. So everyone pays high.

3. Materials and methods

The historical data utilised in this paper is based on archival material and an original dataset of top pay in the UK which has been constructed from four different sources. Data for the period 1968–1979 has been extrapolated from a series of reports produced by the National Board for Prices and Incomes, as well as the Review Body on Top Salaries, between 1968 and 1980 (National Board for Prices and Incomes, 1968, 1969), in particular Report No. 107 on

Top Salaries in the Private Sector and Nationalised Industries (Cmnd.3970) published by the National Board for Prices and Incomes in March 1969, Report No. 6 on Top Salaries (Cmnd.5846) by the Review Body on Top Salaries in 1974 (Review Body on Top Salaries 1974), and Report No. 14, the Fourth Report on Top Salaries, (Cmnd.7952) by the Review Body on Top Salaries in July 1980 (Review Body on Top Salaries, 1980). While these reports primarily focused on pay in the public sector, they included survey data on the pay of senior executives in large private sector companies. For 1980–1998, data have been hand collected from companies' annual reports and accounts available online at Companies House. Estimates have been made of the value of pension contributions and stock awards. For 1999–2014, data have been extracted from Income Data Services Executive Pay Reports for the relevant years. For 2015–2022, data is drawn from annual summaries of FTSE100 'single figure' directors pay produced by the Chartered Institute of Personnel and Development and the High Pay Centre.

Although the FTSE100 index only came into existence in January 1984, the data collected for 1980 onwards also broadly relates to the 100 largest listed companies in the UK in those years. For years prior to 1980 data is drawn from the FT30. In all around 3200 data points (CEOs or highest paid executives) are included in the sample. Non-cash pay is evaluated, using estimates where necessary, in accordance with the 'single figure' principle contained in The Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013. Where appropriate, data is shown in real terms, adjusted to 2022 rates using the Bank of England inflation calculator. FTSE100 index data was obtained from the London Stock Exchange, and UK average national earnings data from the Office for National Statistics. Supplementary information has been drawn from a number of historical sources, including statutory materials, newspaper articles, official reports, company accounts, interviews, correspondence, and other publications and records.

4. CEO pay in large UK listed companies, 1968–2022

This section sets out the history of executive pay structures and levels in the largest listed public companies in the UK during the period 1968–2022. Table 1 provides total reward figures (not inflation adjusted), split between salary and benefits, pensions, annual bonuses and long-term incentives (share options and LTIPs) at five year intervals for the period under review. Figure 1 charts the growth of CEO pay over the period, inflation-adjusted to 2022 rates.

The data shows that the pay of large company CEO's began to rise steeply in the mid-1980s, with a further significant inflection point in the late 1990s. While salaries increased

Table 1. UK large company CEO pay, 1968–2022 (not inflation adjusted).

	1968 £000	1970 £000	1975 £000	1980 £000	1985 £000	1990 £000	1995 £000	2000 £000	2005 £000	2010 £000	2015 £000	2020 £000	2022 £000
Salary and benefits	23	27	36	64	113	327	421	495	734	855	889	738	978
Pension	1	2	6	10	17	49	63	74	184	214	212	123	117
Annual bonus	0	1	2	2	9	52	106	277	646	888	1,065	590	125
Share options/ LTIPs	0	0	1	1	14	30	55	112	221	564	1,900	1,009	1,564
Total remuneration	£24	£30	£45	£77	£153	£458	£645	£958	£1,785	£2,521	£4,066	£2,460	£3,910

quite significantly in the late 1980s, the biggest rises were in annual bonuses, which by 2000 were equivalent to 56% of salary and represented 29% of total reward. From the year 2000 onwards, salaries and pension contributions have remained relatively stable in real terms, while the steepest increases are in long-term incentives (stock options and LTIPs), which by 2015 represented 47% of total reward. After peaking in 2016 at £4,542,000 (£5,483,000 adjusted for inflation) top pay appears to flatten-off, with a steep decline in 2020 because of the economic impact of the COVID-19 pandemic. By 2022 FTSE100 CEO pay had returned to the levels seen in 2018.

The data shown in Figure 1 and Table 1 is shown before deduction of income tax. Post-tax earnings are hard to calculate accurately, as they depend on the tax base (what is brought into the charge to tax), income tax rates (which in the early years under review included a basic rate, higher rates, an additional rate, and in some cases a surcharge called surtax), as well as the executive's personal circumstances. Nevertheless, Table 2, which tabulates the marginal rate of income tax applicable to the top slice of income, gives an important indication of how top tax rates have declined significantly over the period.

To provide a wider societal context, Figure 2 plots the ratio of median CEO pay to average annual national earnings over the period under review. Average annual national earnings increased from £788 in 1968 to £31,616 in 2022, compared with the increase in median CEO remuneration over the same period from £23,000 to £3,910,000. The ratio of CEO pay to average annual national earnings increased from 30:1 in 1968 to a peak of 178:1 in 2016. It fell during the COVID years to 87:1 in 2020, before rising again to 124:1 by 2022. While there are many reasons for the rise in inequality in the UK in the second half of the twentieth century, as described inter alia by the French economist, Thomas Piketty, and the English economist Tony Atkinson, (Atkinson, 2014; Piketty, 2014), nevertheless the shape of the graph in Figure 2 is consistent with Piketty's thesis that a major reason for the rise in income inequality in English-speaking countries is the rise of the 'supermanager' (Piketty, 2014 p. 315).

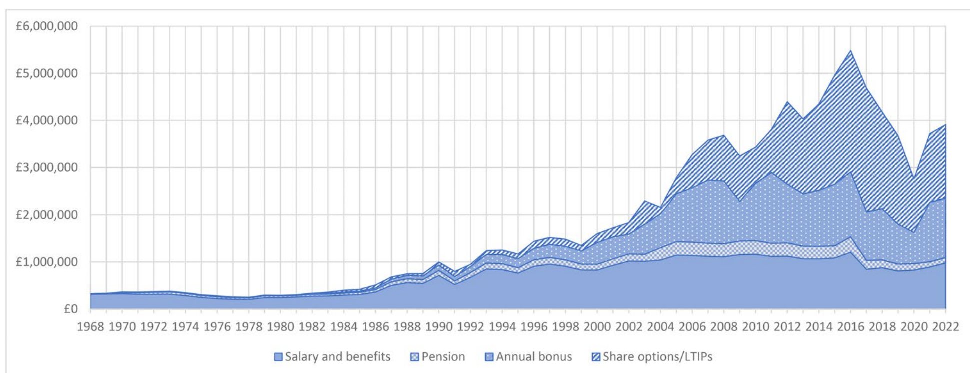

Figure 1. UK large company CEO pay 1968–2022 (inflation adjusted to 2022 rates).

Table 2. Marginal UK income tax rates for top earners, 1968–2022.

	1968	1970	1975	1980	1985	1990	1995	2000	2005	2010	2015	2020	2022
Marginal rate (%)	91.25.	83.0.	83.0.	60.0.	60.0.	40.0.	40.0.	40.0.	40.0.	50.0.	45.0.	45.0.	45.0.

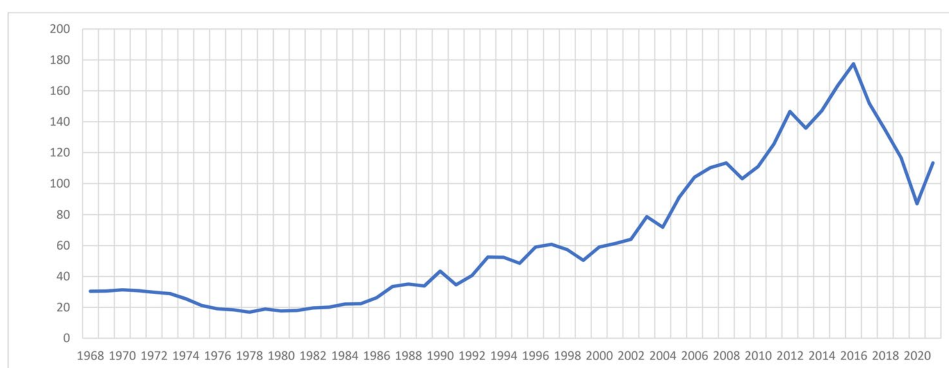

Figure 2. Ratio of CEO pay to annual average national earnings.

In 1968, the start of the period under review, many of the UK's major industries, utilities, and transport networks were monopolies run by state-owned enterprises. These included the National Coal Board, British Steel, the Electricity Council and Area Electricity Boards, the Gas Council and Area Gas Boards, British Rail, and British Airways (organised at the time as two separate companies, British Overseas Airways Corporation and British European Airways). A Government White Paper on productivity, prices and incomes policy published in April 1968 (Cmnd.3590) affirmed the principle that incomes policy should apply to all forms of remuneration, including that of company directors and executives, and that a $3^1/_2$% ceiling on wages, salary, and dividend increases would apply until further notice. The only exceptions to this rule were for wages which were fixed by collective bargaining. In July 1968 the Government instructed the National Board for Prices and Incomes to carry out a detailed examination of the remuneration of the most senior executives in the private and public sectors, and to make recommendations about the appropriate range of remuneration at senior manager and board level in the nationalised industries. Ongoing responsibility for reporting on top pay was subsequently passed to the Review Body on Top Salaries. While the pay of chairmen and board directors of nationalised industries was ultimately determined by the Government, and structured like the pay of senior civil servants, judges, and senior officers in the armed forces, it was benchmarked against the pay of directors of private companies, thus providing a valuable source of pay data.

Between 1968 and 1979, standard practice was for executive directors to be provided with a salary, benefits, and a final-salary defined-benefit pension. A small number of companies also provided share options, though these were relatively unusual. Report No. 107 by the National Board for Prices and Incomes noted that 'an option to take up shares in the company employing the executive in question is taxable as income at the moment the option is taken up, and the difference between the take-up price and the price on realisation can subsequently be taxed as a capital gain. This means that the practice of granting 'stock-options' is almost non-existent in this country'. The 1972 Finance Act simplified the tax treatment of share options, so that there was not normally a tax charge at the date of grant—instead, gains were subject to income tax when options were exercised. However, it was not until the introduction of tax relief for so-called 'discretionary share options schemes' in 1984 that the UK tax code was adjusted in such a way as to encourage the use of share options as an incentive mechanism for top managers.

Frydman and Saks (2010) have described how from 1936 until the mid 1950s executive compensation in the United States comprised mainly salaries and annual bonuses (also pension contributions, although these are not included in the Frydman and Saks data set). From 1936 to 1950 the value of compensation was broadly flat, actually declining in real terms from $0.9 million to $0.75 million. Between 1950 and 1975, executive compensation grew slowly at an average annual rate of 0.8% in the United States, and it was only in the mid 1970s that executive pay began to rise at a rapidly increasing rate. Stock option grants did not materially contribute to the median level of executive pay until the late 1970s. Yet by the mid 1990s the value of stock options and long-term incentives comprised nearly 50% of total compensation.

In the 1980s, American executive compensation practices began to be copied in the UK. An early example can be found at BOC Group, which was part of the FTSE100 index from its foundation in January 1984 until September 2006 when the company was acquired by Linde Group. In 1978, BOC acquired an American company, Airco. Richard Giordano, president of Airco, moved to the UK and was appointed group managing director and chief executive of BOC group in October 1979.[5] From 1985 to December 1990 he combined his position as Chief Executive with that of Chairman. In 1991 he stood down as Chief Executive, but remained as Chairman until January 1992. Giordano was the highest paid executive in the FTSE100 until superseded by Ralph Halpern, the flamboyant chief executive of the Burton Group, who became the first £1 m per year UK CEO in 1986. He went on to have a long career as a non-executive director of various other large companies.[6]

Mr. Giordano's remuneration in 1980 was £277,400 (not adjusted for inflation), increasing to £477,000 in 1981. This compares with FTSE100 CEO median earnings of £77,000 (not adjusted for inflation) in 1980 and £89,000 in 1981. In 1982, Mr. Giordano was paid £579,000—£118,700 of which was a deferred bonus paid under an earnings performance unit plan, which had been awarded by Airco in 1978 before the BOC takeover. On 30th July 1982 shareholders approved the BOC Group Senior Executives' Share Option Scheme, to which they allocated over eight million shares. Under the scheme, options were granted at the market price of the company's ordinary shares at the time of grant, exercisable after three years. Mr. Giordano was awarded a stock option over 400,000 shares in 1982. At the time of grant this option would have had a fair value of around £45,000, estimated using the Black and Scholes methodology. By the time the option vested in 1985 the gain would have amounted to some £395,000.

The 1984 Finance Act introduced tax-favoured discretionary share options, generally known as 'approved executive share options schemes'. Under these schemes the appreciation in share value was liable to capital gains tax when shares were sold, not to income tax or national insurance contributions when options were exercised. Capital gains tax at the time was levied at a rate of 30%, compared with the top rate of income tax of 60%—thus taxing share options as capital gains rather than income provided significant after-tax benefits to executives. Some of the advantages of approved executive share option schemes were subsequently removed when Conservative Chancellor of the Exchequer Nigel Lawson aligned income tax and capital gains tax rates, with a top rate of 40%, but a number of material benefits (including the availability of capital gains tax allowances and the fact that national insurance contributions were not levied on capital gains) still remained.

Approved executive share option schemes were also popular with companies because of their accounting treatment. Under generally accepted accounting practice at the time,

the cost to the company of providing shares was not charged as an expense in the profit and loss account, because the cost fell directly upon shareholders through the dilution of their shareholdings. It was not until January 2005, after the publication of a new reporting standard, International Financial Reporting Standard 2, that this practiced changed (IFRS, 2004). IFRS 2 now requires the fair value of an option to be measured at the date on which the option is granted and expensed over the vesting period.[7]

An economic recession at the end of the 1980s and in the early 1990s had a significant impact on executive pay. The FTSE100 index fell from 2423 in December 1989 to 2144 in December 1990, only fully recovering its value in 1992. Many executives found that their stock options were 'underwater', meaning that the exercise price was higher than the current share price. The investment committees of two major investor trade associations, the Association of British Insurers (ABI) and National Association of Pension Funds (NAPF), whose members collectively held a very substantial proportion of the shares listed on the London Stock Exchange and who issued guidelines about the use of share options in quoted companies, refused to allow options to be repriced or reissued, arguing that as shareholders had lost value there was no reason why executives should be let off the hook. Underwater options became a millstone round the necks of executives, who had to see share prices restored to the level of the option strike price before their options regained any value.

In response to the problem of underwater share options, three companies, Prudential Corporation, Reuters Group, and British Telecom, decided to award deferred shares rather than options over shares, placing restrictions on transfer rights and the receipt of dividends for three or more years until ownership had fully vested. Prudential's 'Share Participation Plan' was introduced on 1 January 1992. Reuters 'Long-term Incentive Scheme' was introduced during 1993, and British Telecom's 'Long-term Remuneration Plan' was introduced on 1 August 1994. One of the great attractions of these 'Long-term Incentive Plans', or 'LTIPs', as they came to be known, is that they still had value even if the relevant share price fell.

The introduction of the Prudential, Reuters and British Telecom deferred share plans coincided with the publication of two influential public reports on corporate governance, issued in the wake of a series of major corporate scandals, including the Maxwell affair.[8] The Cadbury Report, published in 1992, was commissioned by the Financial Reporting Council, the Stock Exchange and the accountancy profession to investigate ways of improving the financial aspects of corporate governance. Although not primarily focused on executive pay, it recommended that the existing accounting disclosure requirements for directors' pay should be extended so that details of the pay of the chairman and, if different, the highest paid director, showed salary and performance-related aspects separately, and that information should also be given about stock options, stock appreciation rights, and pension contributions.

The Greenbury report, which marked a significant development in the history of senior executive reward in the UK, was published in July 1995 (Greenbury, 1995). Established following the Cadbury Report, the Study Group on Directors' Remuneration was commissioned by the Confederation of British Industry under the chairmanship of Sir Richard Greenbury. Its formation was the result of increasing public concern over the salaries and bonuses of executives, especially the remuneration paid to the chief executives of recently privatised public utilities such as British Gas. The report's recommendations included a requirement that each company should include in its annual accounts a report by the remuneration committee giving full details of all the elements in the remuneration package of each

individual director by name, including basic salary, benefits in kind, annual bonuses, long-term incentives, and pension entitlements earned during the year (Greenbury report section B4, and paragraphs 5.8–5.12). It proposed that this be done in the format of a 'summary remuneration table', with a separate table for share options and long-term incentive schemes (Greenbury report, paragraph 5.12 and Appendix II).

The Greenbury report strongly encouraged the use of LTIPs by recommending that 'the performance-related elements of remuneration' should be designed to 'align the interests of directors and shareholders' and 'give directors keen incentives to perform at the highest level' (Greenbury report, section C4 and paragraph 6.16). The report said, 'remuneration committees should consider whether their directors should be eligible for benefits under long-term incentive schemes', and recommended, rather cryptically, that 'traditional share option schemes should be weighed against other kinds of long-term incentive scheme' (Greenbury report section C6 and paragraphs 6.23–6.34). The ABI and NAPF went further, issuing guidelines, which discouraged awards of stock options in addition to LTIPs, and prescribed the terms on which LTIPs should be issued, recommending phased grants, vesting periods of a minimum of three years, and the application of rigorous financial performance targets. Two of the most common metrics used in practice were growth in earnings per share and growth in total shareholder return.

An important outcome of the Cadbury and Greenbury Reports was the UK Corporate Governance Code, first issued as an addendum to the Cadbury Report. The code was appended to the London Stock Exchange listing rules in 1994 and incorporated the Greenbury provisions relating to the determination and disclosure of executive compensation. These applied to companies for accounting periods ending on or after 31 December 1995. The code has subsequently been updated on a number of occasions, most recently in 2024, and is now the responsibility of the Financial Reporting Council. While the headings have changed, the code has always a section on executive directors' remuneration. This has focused on the twin objectives of improving disclosure and linking pay to long-term company performance. While increased disclosure has succeeded in creating greater transparency around executive pay, a perverse consequence is that it appears to have contributed to pay inflation. A CEO who believes he or she is underpaid relative to their peers will use public information to justify a pay increase. A CEO who is overpaid is unlikely to seek a reduction (Harvey et al. 2020).

Figure 3 charts the growth in share option plans between 1980 and 1996 and their gradual replacement by LTIPs between 1992 and 1998. Figure 4 plots the percentage of FTSE100 companies reporting share option and LTIP gains after 1999, showing how the value of LTIP gains increases rapidly after 2005 while gains from stock options fall away. The fall in the value of both LTIP and stock option gains in 2004 is the lagged effect of the fall in the FTSE100 index from 5217 in 2001 to 3940 in 2002.

After publication of the Cadbury and Greenbury reports it became normal practice for remuneration committees to take advice from external compensation specialists to validate their decisions. Accordingly there was a marked growth in the activities of pay consultants, such as New Bridge Street and Towers Perrin, who benchmarked pay and advised companies on 'best practice' in the design of executive reward strategies, further encouraging the use of LTIPs to align the interests of shareholders and executives (Bender, 2011).

Subsequent developments saw the Cadbury and Greenbury recommendations put on a statutory footing. The Directors' Remuneration Report Regulations (2002), which amended

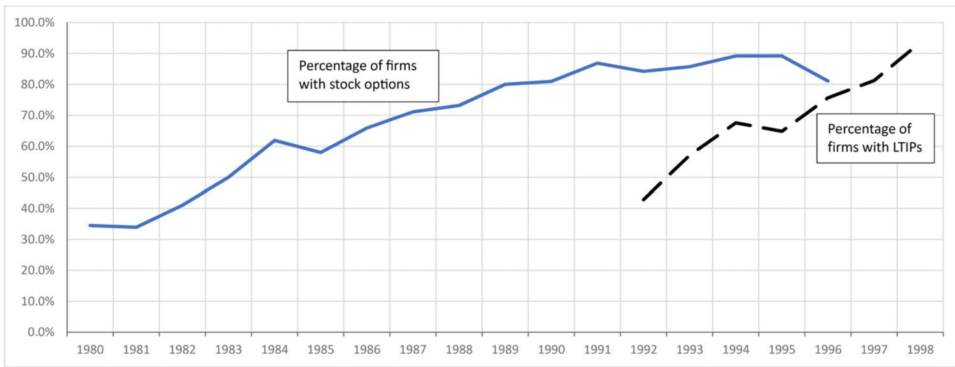

Figure 3. Percentage of large UK companies with share option plans and LTIPs.

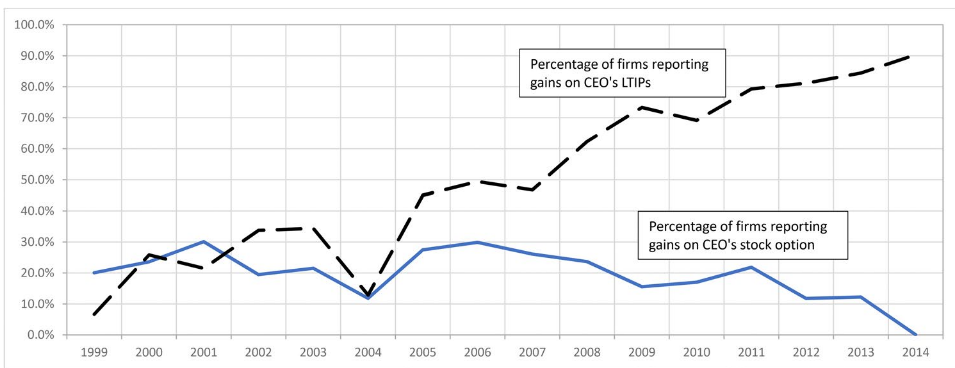

Figure 4. Percentage of FTSE100 companies reporting CEO share option and LTIP gains.

the Companies Act 1985, required all UK companies with shares listed on stock exchanges in the UK, EU, New York or NASDAQ to include a detailed report on directors' remuneration in their annual report and accounts. Details of the specific information which had to be included in the report was set out in a new schedule to the Companies Act. The regulations mandated that an advisory resolution on the directors' remuneration report was to be put to shareholders at each annual general meeting—the UK being the first jurisdiction to introduce such 'say on pay' provisions. This requirement appears to have had some moderating effect on pay levels (Ferri & Maber, 2013). Company boards do not like countermanding votes even when the results are non-binding, and have tended to take the reputational implications of adverse votes very seriously. Notable examples of adverse votes include GlaxoSmithKline in 2003, Royal Bank of Scotland and Royal Dutch Shell in 2009, Aviva and WPP in 2012, and BP in 2016.[9] All led to changes in controversial pay proposals, especially those which were regarded as so-called 'rewards for failure'.

Further developments in company law have increased the amount of information in the system, apparently without having any significant moderating effect on pay. Additional regulations—the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations—were issued in 2008 amending the information which was to be included in the directors' remuneration report. However, it was not until the publication of the Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations

in 2013 that companies were required to disclose total remuneration from all sources (including pension contributions and stock awards) as a single figure. The 'single figure' requirement, which came into effect for accounting periods beginning after 1 October 2014, had been somewhat controversial because of the difficulty in deciding how to value stock awards. The regulations require the value of awards to be disclosed at the time of vesting, when the assessment of value is relatively straight forward, in comparison with the equivalent US regulations which require awards to be valued at the date of grant, for example by using the Black and Scholes formula or a similar methodology. For financial years ending on or after 1 January 2019, the Companies (Miscellaneous Reporting) Regulations 2018 now also require firms to disclose pay ratios (i.e. the total pay of the CEO compared with the median pay of all full-time UK employees).

Figure 5 charts the increase in FTSE100 CEO pay indexed from January 1984 compared with the rise in the FTSE100 index since its inception. It provides further evidence that FTSE100 CEO pay is not strongly correlated with share price performance. While the CEO pay index broadly tracks the FTSE100 index from 1984 to 1999, it is clear from Figure 5 that after 1999 the relationship breaks down.

Successive UK Governments have argued that it is primarily the responsibility of investors, not government, to provide a brake on executive pay. Although some active investors have historically taken an interest in senior executive reward policies in portfolio companies—Hermes Investment Management is a notable example (Becht et al. 2009)—investment managers have not had much incentive to intervene in pay matters. Before promulgation of the Directors' Remuneration Report Regulations (2002), their ability to do so was in any case limited. While a £3.25 million pay award to the CEO of a FTSE100 company might seem a lot of money, to a large investment management firm with £50 billion of assets under management, holding one per cent of the company's shares, the amount involved is relatively trivial, especially if the question is about whether the CEO's bonus is ten or twenty per cent higher than it should be.

In July 2016, UK Prime Minister Theresa May announced a series of proposals intended to tackle high executive pay, which she described as being a consequence of 'elite collective action'.[10] These included disclosing the ratio of CEO reward to median worker pay, putting worker representatives on the board, and making say-on-pay laws binding. A green paper published in November 2016 subsequently rowed back from many of the proposed measures, restating the UK Government's historic position that executive pay is primarily a matter

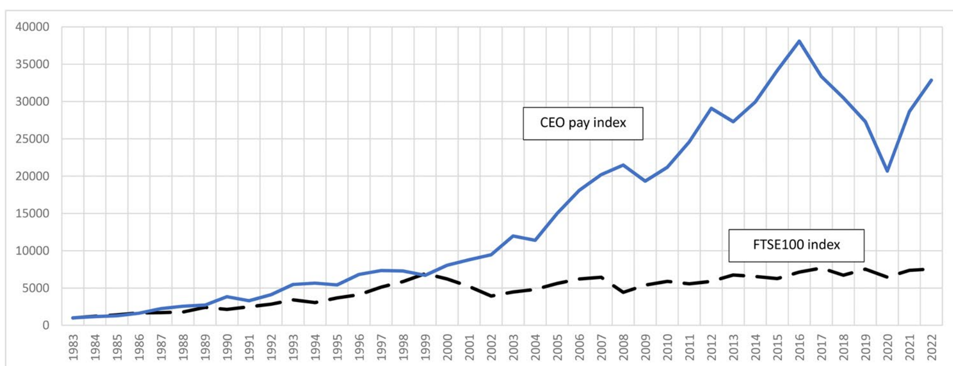

Figure 5. FTSE 100 index vs. CEO pay index, 1984–2022.

for shareholders, and outlining a range of options aimed at enhancing shareholder voting rights, encouraging greater shareholder engagement with executive pay, strengthening the role of remuneration committees, improving pay transparency, and increasing the effectiveness of long-term pay incentives by replacing LTIPs with restricted stock awards.[11] Significantly, there was no reference to putting worker representatives on the board. The government's response to the green paper consultation drew back even further, proposing only that the Financial Reporting Council would be invited to revise the UK corporate governance code to be more specific about the steps listed companies should take when they encounter significant shareholder opposition to executive pay proposal and giving remuneration committees broader responsibility for overseeing pay arrangements their company. They also invited the Investment Association to set up a public register of listed companies encountering shareholder opposition to pay awards of 20% or more.[12]

An analysis of the shareholdings of FTSE100 companies shows the difficulty of relying on investors to regulate executive pay. A snapshot of holdings at various significant levels for each of the top 35, 50 and 100 companies in the FTSE 100 index on 31 December 2015 is set out in Table 3.[13] Six companies have been excluded because they had a single dominant investor. On average 67.2% of shares held by the 100 largest shareholders in each company are owned on behalf of retail investors by institutional shareholders (banks, insurance companies, mutual funds, pension funds, private equity firms, and other financial investors), 8.4% by trade investors, 9.0% by governments (for example, sovereign wealth funds) and only 6.1% directly by individual investors. The top 100 shareholders, on average, hold in aggregate 68.8% of the total share capital. In a typical company a small number of institutional shareholders (median = 5) have holdings of between 3 and 6% of company's share capital, five investors might control more than 25% of the voting rights, 19 might control 50% of the votes and 82 might control 75% or more.

What is apparent from this analysis is that, except in the small number of cases that have been identified, there is no single dominant shareholder. Even though, on average, five institutional investors control 26.5% of a company's shares, sufficient to block a special resolution, this does not constitute a significant level of control, even if the five could be persuaded to act in concert. There is a collective action problem. It takes on average 19 institutional investors to control 50% of the votes and 82 to control 75%. This is too large a number to make it likely that coalitions to vote down executive pay proposals will naturally emerge.

As well as the UK Corporate Governance Code, the Financial Reporting Council also publishes the UK Stewardship Code for institutional investors, first issued in 2008. This has largely been silent on matters relating to executive pay. However, there have been some signs that, since 2016, as a result of continuing negative publicity, large institutional investors have taken governance over executive remuneration more seriously. A number have issued important policy documents. For example, the Norwegian Sovereign Wealth fund said that it wanted to get rid of LTIPs altogether, as it sees them as particularly problematic. BlackRock has issued a number of policy statements emphasising its stewardship responsibility when it comes to executive pay.[14]

A public register maintained by The Investment Association (successor to the investment protection committees of the ABI and NAPF) which tracks shareholder dissent at listed companies, established in response to the government's green paper, shows an increasing number of pay revolts since the register was introduced in 2018. It suggests that institutional

Table 3. Analysis of shareholdings in FTSE100 companies on 31 December 2015.

	3% Shareholders		Number of shareholders representing ≥10% of ordinary shares	Number of shareholders representing >25% of ordinary shares	Number of shareholders representing ≥50%% of ordinary shares	Number of shareholders representing ≥75%% of ordinary shares	Top 100 shareholders				
	Number	% Of total share capital					Institutional investors	Trade investors	Investment by the State	Individual investors	% Of total share capital
FTSE 35											
Mean	3.7	22.7	2.6	9.4	37.0	81.4	70.5	7.7	9.2	5.9	63.5
Median	3.0	19.7	2.0	7.0	32.0	97.0	73.0	8.0	11.0	4.0	63.8
Std. deviation	2.3	15.2	2.5	8.2	24.7	26.1	11.5	3.1	3.7	5.8	17.8
FTSE 50											
Mean	4.2	24.3	2.4	8.3	34.6	78.7	69.2	8.3	9.1	6.4	65.4
Median	4.0	21.4	2.0	7.0	32.0	97.0	71.0	9.0	11.0	6.0	67.7
Std. deviation	2.3	14.1	2.2	7.2	24.4	26.7	10.7	3.6	3.7	5.4	15.5
FTSE 100											
Mean	5.1	26.9	2.1	7.4	28.2	72.9	67.2	8.4	9.0	6.1	68.8
Median	5.0	26.5	2.0	5.0	19.0	82.0	70.5	9.0	10.0	6.0	72.2
Std. deviation	3.6	13.9	1.7	7.0	21.8	26.7	12.0	7.7	9.2	5.9	17.7

investors are increasingly taking their stewardship responsibilities in respect of executive compensation seriously. However, not all major shareholders are actively engaged. Vanguard, an index-tracker investment house which has been hugely influential in driving down management fees for investors, rarely votes against executive pay proposals. LGIM, which had previously issued a number of position papers on executive pay, announced in November 2021 that it would stop almost all direct comment on pay because, according to Angeli Benham, Senior Global ESG Manager, 'most companies don't act on the remuneration feedback we give them'.[15]

A further development of note in the period took place in 2018, when Weir Group plc, a multinational engineering company with its headquarters in Glasgow, ditched its complex LTIP and replaced it with a simpler restricted share plan. This involved the maximum total compensation of the CEO and CFO being reduced by nearly 25%. The new plan involved a 'haircut'—the maximum award available under the restricted share plan was 50% of the maximum award available under the LTIP, an 'underpin'—a more robust set of criteria defining who was eligible to receive a restricted share award, longer vesting and holding periods, and an enhanced overall shareholding requirement—the CEO and CFO were required to double their shareholdings to 400 and 300% of base salary respectively. These requirements are to continue after the individuals' employment with the company ceases, tapering down to zero over two years post-employment.

A notable feature of the Weir Group case is that the successful implementation of the restricted stock plan in 2018 followed an earlier proposal in 2016 to replace the LTIP with a combination of restricted shares and performance shares. This had been roundly rejected by 72.36% of Weir Group's shareholders. Clare Chapman, who became Weir Group's remuneration committee chair in 2017, consulted widely with shareholders and worked tirelessly to build consensus, eventually winning the support of proxy advisers Glass Lewis and Institutional Shareholder Services, who had not previously recommended a vote in favour of a restricted stock plan. The proposal also won the support of the Norwegian Sovereign Wealth fund, a major shareholder, who praised the Weir Group board's 'willingness to challenge conventional thinking on executive remuneration'. The new plan was eventually approved by 92.35% of Weir Group's shareholders.[16]

Since the adoption of Weir Group's proposals, restricted stock plans have been adopted by a number of FTSE100 companies, including BT Plc, Burberry, Lloyds Banking Group, and Whitbread. It has become increasingly clear that securing shareholder approval for a restricted stock plan requires the previous LTIP to be eliminated entirely, a haircut of 50%, vesting and holding periods of five years or more, and higher executive shareholding requirements.[17] Some commentators have predicted that restricted stock plans, subject to fifty per cent haircuts, with extended vesting and holding periods, but without complex performance conditions, may replace LTIPs in much the same way that LTIPs replaced stock option schemes in the 1990s (Bachelder, 2019). However, to date there is not much evidence of this.

While not strictly part of the period under review, it should be noted that executive pay has continued to rise after 2022. In 2023 median FTSE100 CEO pay increased to £4.5 m. In May 2023, Julia Hoggett, CEO of the London Stock Exchange, proposed that investors should back higher CEO pay to discourage companies from moving their stock market listings overseas. At the same time a number of companies began to push for higher CEO pay to bridge the gap with the US.[18] It seems that FTSE100 CEO pay will continue to be a controversial subject!

5. Discussion

This section identifies certain features of the historical data which are important to our understanding of the rise in the pay of CEOs of large UK public companies since 1968 and which are consistent with key elements of the two competing theories set out in section 2.

Optimal contracting theorists argue that CEO pay can be explained as a power function of company size and that market capitalisation is a good proxy for this. The FTSE100 index is a measure of the market capitalisation of the one hundred largest companies listed on the London Stock Exchange compared with the base period of January 1984. To test Gabaix and Landier's (2008) 'power function of company size' proposition with UK data, Figure 6 plots the log of the FTSE100 index against the log of the CEO pay index.

The result is a strong match between the two lines, which broadly supports the thesis advanced by Gabaix and Landier. However, it does not explain what the mechanism is for determining CEO pay; Elster (2007) has explained how mechanisms—'frequently occurring and easily recognisable causal patterns' (p. 36)—are an important part of social scientific theorising.

When it comes to the mechanism by which CEO pay is determined, it is evident in the historical development of executive pay in the UK that isomorphism, a component of the market failure approach, is a major factor in the determination of executive compensation. Perhaps the most significant example of isomorphism is the normative impact that Jensen and Meckling's seminal paper in 1976 has had on the structure of executive pay in both the US and the UK. Jensen and Meckling argued that companies should reward executives with incentive contracts in order to align their interests with those of shareholders. This much cited paper provided justification for the rapid growth in stock option awards after 1980. It was reinforced by Jensen and Murphy's Harvard Business Review article entitled 'CEO incentives – it's not how much you pay, but how', which recommended that CEOs should be paid in company stock (Jensen & Murphy, 1990a). Pepper (2018) has noted how Jensen and his co-authors switch from a positive theory in the 1976 paper to a normative theory in 1990. Having failed to find strong (positive) evidence that pay is correlated with financial performance, they argue (normatively) that companies are not doing things the right way. Companies have continued to follow this normative advice.

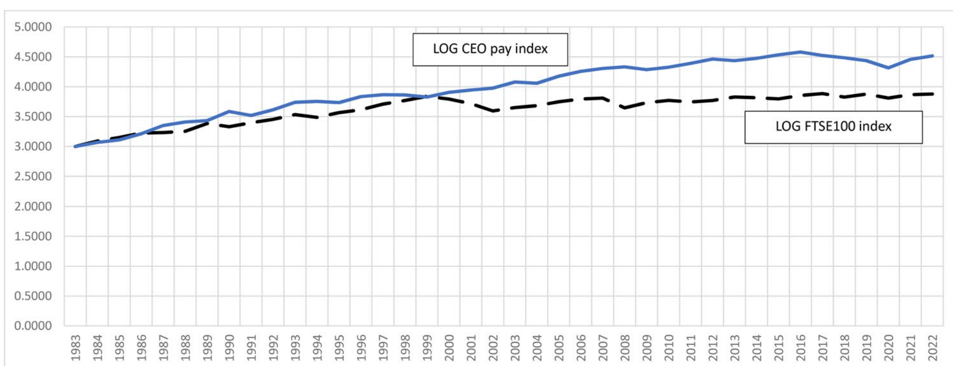

Figure 6. LOG FTSE100 index vs. LOG CEO pay index.

Other examples of isomorphism can be observed in the data. Mimetic isomorphism can be seen in the way in which remuneration committees copy the pay practices of other organisations. Many of the patterns seen in the UK data are similar to those seen up to fifteen years earlier in the US executive compensation time-series constructed by Frydman and Saks. The imitation of US executive pay practices including share options in the early 1980s is an example of mimetic isomorphism. In 1980, only a small minority of companies had share option schemes and share options gains represented just 1% of total reward (Table 1). The prevalence of share options after 1984 in FTSE100 companies is readily apparent in the data. By 1990 over 80% of FTSE100 companies had implemented share option schemes, although option gains still represented only 9% of total pay.

The replacement of share options by LTIPs in the early 1990s, and the use of earnings per share and total shareholder return metrics as the most common performance conditions, are both examples of mimetic isomorphism operating between companies within the UK. After publication of the Greenbury report in 1996, the proportion of FTSE100 companies awarding LTIPs rapidly increased. For some time share option schemes and LTIPs operated in parallel, but the ABI discouraged concurrent awards under both types of plan. By 2015, the vast majority (91%) of FTSE100 companies had implemented LTIPs, largely replacing share options which were granted by only a minority (13%) of companies. LTIPs gains represented 47% of total pay.

Coercive isomorphism is exhibited in the way that companies are constrained by laws and codes established by government and regulators. High taxes and the $3^1/_2$% cap on salary increases evidently had a dampening effect on top pay in the late 1960s and 1970s. The ABI and NAPF's guidelines on the use of share options in quoted companies, the Greenbury report's endorsement of performance-related long-term incentives, and the ABI and NAPF's guidance about conditions attaching to the award and vesting of LTIPs, are all examples of coercive isomorphism, which, perhaps perversely, has contributed to pay inflation. The Finance Act 1984 tax exemption for approved share options is a further example of a government mandate encouraging a particular type of pay structure.

'Best practice' recommendations by remuneration consultants (often based on the principle of 'this is what other companies do') are a further example of normative isomorphism. Remuneration consultants also encouraged pay-benchmarking against peer group companies (Bender, 2011; de Vaan et al. 2019). This is another form of mimetic isomorphism, which leads to ratcheting up when comparisons are unfavourable (a company is paying under the odds in comparison with the peer group), but not a ratcheting down when a company is paying over the odds—consistent with the 'Lake Wobegon effect' and 'Remuneration Committee's Dilemma' described above in Section 2.

Successive UK governments of various political persuasions have failed to put a brake on executive pay, believing instead that executive pay in the private sector is primarily the responsibility of shareholders. The failure of institutional investors to stop inflation in executive pay is a specific example of the general theory of groups (Olson, 1965/1971). What governments have done, with the intention of providing investors with the information necessary to carry out monitoring activity, is progressively increase the level of disclosure required of companies about executive pay strategy and total rewards paid to individual directors. Olsen argued that, because executives exercise management and control over large corporations and are able to further their own interests at the expense of investors, there is a collective action problem. Minority shareholders in public companies have a reasonable expectation of receiving regular

dividends and capital gains proportionate to the level of risk they are taking. While it is in the interests of shareholders to monitor the activities of managers, they will want to do so at minimal cost. Historically investors have accepted rent-seeking behaviour by managers as long as their reasonable expectations of income and gains are met, because the cost of intervention would exceed any individual benefit. I call this 'the investors' collective action problem'. In control systems terms, far from creating negative feedback, which would have helped to moderate pay, the information-rich environment resulting from statutorily-enforced disclosure requirements has had the effect of fuelling pay inflation by creating a positive feedback loop. Senior executive incentive contracts are endogenous—executives, directors, and compensation consultants spend time and effort designing them, taking into account observable firm, industry, and executive characteristics. As a result, compensation contracts are inevitably correlated with these observable characteristics, which in turn affect firm behaviour, performance, and value. This also helps to explain why CEO pay and company financial performance are not strongly linked. In recent years, some major institutional shareholders have taken a greater interest in executive pay. Enhanced disclosure rules and 'say-on-pay' provisions have reduced the costs of collective action and increased the possibility of successful intervention. Nevertheless, for many shareholders the quantum of top pay is not of particular concern when compared with total management expenses and governance costs. The decision by LGIM in November 2021 to stop direct comment on executive pay, referred to in the previous section, is an indication, if one is needed, that the investors' collective action problem is still alive and kicking.

There is a notable inflection point in the data in the late 1990s when top pay rose steeply. This inflection point coincides with the emergence of LTIPs as a significant component of executive pay packages. Figure 1 shows how increases in executive pay over and above inflation are largely attributable to the increasing prevalence of long-term incentives. Frydman and Saks point out that the value of pay awards, as perceived by executives, may be affected as riskier forms of remuneration, such as stock-based pay and long-term incentives, have become a greater fraction of compensation packages—see also Pepper and Gore (2015) who conjecture that companies increase the size of LTIP awards to compensate executives for the perceived discount in value compared with an equivalent cash award. It also means that the accounting cost booked under IFRS 2 will be greater than the subjectively perceived value, making LTIPs an inefficient form of reward.

These features of the market failure approach to executive pay—isomorphism, the remuneration committees' dilemma, the investors' collective action problem, and the 'perception discount' that executives apply to the value of LTIPs—are additive and not mutually exclusive. Together they contribute to our understanding of why the pay of CEOs in large UK companies has increased so significantly since 1968. In these and other respects the patterns in the UK data broadly match patterns which can be observed in the longer time-series constructed by Frydman and Saks, but with a time lag of up to fifteen years, depending on which elements of the data we are talking about.

6. Conclusion

In this paper, I contribute to the literature on British business elites by examining the development of pay structures and levels for CEOs of large listed companies in the United Kingdom for the period 1968–2022. The history of senior executive pay in the UK since 1968 began with a bureaucratic approach to remuneration in the days when the UK economy was

dominated by nationalised industries. This was followed by the imitation of American pay practices—especially stock options—in the early 1980s, along with the ending of high marginal tax rates which had had a dampening effect on top pay. It continues with the emergence of LTIPs during the recession of the early 1990s, the expansion of LTIPs as a result of normative and coercive isomorphism following publication of the Greenbury report in 1995, and subjective valuation issues which meant that executives undervalue their LTIP awards. Increasing directors' pay disclosure requirements throughout the 1990s in response to public concerns about high pay perversely led to accelerating pay rises because of isomorphic social comparisons. Benchmarking carried out by companies with others in their referent groups led to inflation in CEO pay. This was reinforced by social comparisons with peers carried out by instinctively risk-averse CEOs, who may also have subjectively discounted the value of their LTIP awards. Central to the problem of executive pay are a prisoner's dilemma at the heart of the work of remuneration committees, and a collective action problem faced by institutional investors resulting in spiralling top pay inflation which has been a feature of executive pay throughout the period covered by this paper.

As well as contributing to the historical literature of British business elites, the paper also makes an empirical contribution with the construction of a new data set of UK CEO pay covering the period 1968–2022. A further contribution is in seeking to establish 'best fit' between this data and the two main theoretical approaches to executive compensation, optimal contracting theory and the market failure approach.

Notes

1. Under provisions dating back to the Companies Act 1948, companies were required to disclose the total of the fees, salaries and taxable benefits of the chairman and the highest paid director, if different. The number of other directors receiving total emoluments was shown in bands of £5,000. Details of share options, stock awards, or pension contributions at an individual level were not required. Disclosure requirements increased with the publication of the Directors' Remuneration Report Regulations, 2002. Even so, it was only after the publication of further regulations—the 'Large and Medium-sized Companies and Groups (Accounts and Reports) Amendment Regulations, 2013'—that companies were required to report in respect of each director a single total figure for remuneration, including salary, taxable benefits, pension contributions, annual bonuses, and long-term incentives, including stock awards.
2. The FTSE100 index was launched in January 1984. It is a market capitalisation-weighted index, which replaced the FT30 Index as a performance benchmark for investors. The FT30 Index, a price-weighted rather than market capitalisation-based index, was first published by the Financial News in 1935.
3. Elster's focus is on governance of the polity, but I argue that the phrase 'securities against misrule' (itself borrowed from the title of a work by Jeremy Bentham) aptly describes an approach to corporate governance which focuses on preventing corporate malfeasance.
4. Jensen and Murphy (1990b), found only a very small empirical relationship between CEO pay and performance. Ten years later Tosi et al. (2000), concluded that incentive alignment as an explanatory construct for CEO pay was at best weakly supported by the evidence, based on a meta-analysis of over 100 empirical studies. Two other meta-analytic reviews have provided further evidence that CEO pay and financial performance are not closely linked: see Essen et al. (2015), 164–202 and Aguinis et al. (2018).
5. See Apple (1984).
6. See Skapinker (2009). Richard Giordano made a repeat appearance in the history of top pay in the UK when in 1994 as Chairman of British Gas he was involved in a major controversy about

'fat cat pay'. British Gas was a utility company with a national monopoly whose shares had been listed on the London Stock Exchange as part of the Conservative Government's privatisation programme. Following privatisation, the company's long-standing CEO, Cedric Brown, was awarded a 75% pay increase, causing outrage in the national press. See Cope (1996).

7. In the UK the disclosure requirements in the directors' remuneration report (as opposed to accounting treatment in the profit and loss account) are subtly different from those found in the US. In the 'single figure' disclosures, it is the value of share awards at the time of vesting which are included, rather than the value of share awards at the time of grant.
8. On 5 November 1991 the body of Robert Maxwell, a media mogul, was found floating in the Atlantic Ocean. It was assumed that he had fallen overboard from his yacht, the Lady Ghislaine – the official ruling was of accidental death by drowning. After his death, Maxwell's publishing empire collapsed as banks called in their loans. At the same time, a massive hole was discovered in the pension fund of the Mirror group, money having been diverted fraudulently by Robert Maxwell in an attempt to shore up the finances of his business empire.
9. See Macalister et al. (2016).
10. See Fooks et al. (2016).
11. Department for Business, Energy and Industrial Policy (2017).
12. Department for Business, Energy and Industrial Policy (2016)
13. This data was obtained from Orbis http://www.bvdinfo.com/en-us/our-products/company-information/international-products/orbis.
14. The Norwegian Sovereign Wealth fund's paper 'Remuneration of the CEO –Asset manager perspective' was published by Norges Bank Investment Management on 17 April 2017 (Norges Bank Investment Management, 2017). BlackRock's statements include 'Executive Compensation: The Role of Public Company Shareholders', a Policy Spotlight issued in April 2019 (BlackRock, 2019), and 'Investment stewardship's approach to executive compensation', dated January 2020 (BlackRock, 2020).
15. Vanguard's 'failure to exert influence over high pay' was the subject of an article in the Financial Times by Madison Marriage on 7 May 2017 (Marriage, 2017). LGIM published policy statements on 'UK principles of executive pay' in 2016 and 2020, and a further paper entitled 'Corporate governance and responsible investing policy' in February 2021. Its ending of feedback on executive pay 'after finding it mostly ignored' was reported by Harriet Agnew in the Financial Times on 21 November 2021 (Agnew, 2021).
16. The primary source of data on The Weir Group is Harvard Business School case 9-319-046, revised 17 January 2019, prepared by Lynn S. Paine and Federica Gabrieli (Paine & Gabrieli, 2019).
17. See The Purposeful Company Study on Deferred Shares Progress Review, published by The Purposeful Company Steering Group in September 2020 (The Purposeful Company Steering Group, 2020).
18. See Raval (2023); Raval et al. (2024); O'Dwyer (2024).

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