

# TIME TO THINK:

## EXECUTIVE REMUNERATION AND WORKFORCE PAY

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*The need for remuneration committees to have a broader remit to consider workforce engagement and pay is highlighted in the 2018 UK Corporate Governance Code, which requires committees to review workforce remuneration and related policies, and take these into account when setting the policy for executive remuneration.*

*The Ellason team is experienced in supporting remuneration committees on matters pertaining to the governance of executive and employee pay – please contact us if you would like to discuss further.*

### **1. What is expected of the remuneration committee regarding workforce pay?**

Remuneration committees in FTSE-listed companies are required to: review workforce remuneration and take this into account when setting the policy for executive directors; disclose in the remuneration report what engagement with the workforce has taken place on executive pay; and explain the reasons why executive pay is appropriate using internal measures, including pay ratios and pay gaps.

### **2. What should committees look at when reviewing workforce pay?**

The FRC recommends that the committee's review of workforce pay covers the company's overall pay philosophy, as well as details on the individual components of employee pay, including base pay, benefits and all aspects of variable pay – regardless of where this is managed in the business. Many companies now also receive data on workforce demographics and engagement to help inform the committee's decision-making process around senior executive pay.

Companies are encouraged to disclose in the directors' remuneration report how the

committee has taken workforce pay into account when making decisions on executive pay.

The level of detail provided in remuneration reports on company-wide pay matters has increased in recent years, with some companies now providing detailed disclosure on workforce pay policies and alignment of pay principles and policies across the business.

### **3. How are companies engaging with employees on executive pay?**

As highlighted in the FRC's recent review of the UK Corporate Governance Code, the extent to which companies are openly engaging with employees on executive pay matters remains mixed. Some companies now report using employee forums and town hall meetings as an opportunity to guide employees through the executive remuneration policy. This often includes explaining how the remuneration policy is aligned with the company strategy and shareholder expectations, and how remuneration is linked to the wider pay policies in practice. It can also be an opportunity to clarify how the executive pay structure is subject to longer deferral

periods and shareholding requirements. However, care needs to be taken to ensure that such processes are not seen to be one-sided and that an open dialogue can take place, with the outcome of this reported back to the committee.

#### **4. Does the CEO pay ratio apply to us?**

Quoted companies with more than 250 UK employees are legally required to calculate and disclose their CEO pay ratios – specifying the CEO's most recent total remuneration figure as a ratio against the total remuneration of employees ranked at the 25<sup>th</sup>, 50<sup>th</sup> and 75<sup>th</sup> percentiles on the basis of full-time equivalent pay. The disclosure is designed to allow interested parties inside and outside the organisation to understand how remuneration policies across the organisation compare to the executive pay policy. Committees should focus on evolving a clear narrative around how the executive pay outcome has aligned with business performance, as well as how success has been shared more widely across the organisation.

#### **5. What are the requirements for gender pay reporting? Do they apply to us?**

Since 2017, any organisation (whether listed or unlisted) that has more than 250 employees has been required to publish figures about their gender pay gap. As part of its annual work programme, remuneration committees should work closely with management and the Board to understand the key figures, the drivers for any gap and the initiatives in place to help close the gap and improve diversity across the organisation.

#### **6. Is there an update on requirements around ethnicity pay reporting?**

In 2018/19, the UK Government consulted on options for employer-led ethnicity pay reporting. Following the consultation, the Government met with businesses and representative organisations to understand the barriers to reporting this data, and explore further what information could reasonably be published. However, a formal recommendation is yet to be made. In the meantime, a number of companies have started collecting data on ethnicity, with some FTSE-listed companies voluntarily publishing ethnicity pay ratios (e.g. Barclays, ITV and NatWest Group).

#### **7. What has been the impact of Covid-19 on executive and workforce pay alignment?**

As companies respond to the impact of the pandemic, the relationship between the executive and employee experience will be keenly scrutinised externally. Committees will need to balance sensitively the need to continue to incentivise senior executives, for whom variable pay is a large part of the pay package, whilst ensuring that the executive experience is not out of line with that of employees, shareholders and other stakeholder groups.

Whilst shareholders appreciate that management are responsible for the majority of decisions on broader workforce pay matters, they want to understand how the Board challenges and oversees this, and how remuneration committees ensure that pay decisions across the organisation are fair and equitable.