**Social Research Development Limited**

NON-PROFIT MAKING · LIMITED BY GUARANTEE


# APPROPRIATE PAY


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# APPROPRIATE PAY

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# APPROPRIATE PAY

Appropriate pay is reward according to service rendered the community, according to the work done and to the urgency of the need satisfied. The underlying assumption is that pay at the lower end of the scale provides basic subsistence and that no section of the community appropriates an unreasonable share at the expense of the remainder. The difference in pay between subsistence and reward should motivate through providing incentive towards working at the height of one's ability.

Here we take a close look at the distribution of incomes throughout the community and how this is changing, for pre-tax and for tax-free (take home after tax) income. Adjusting tax-free pay to allow for inflation, we see how real purchasing power has increased throughout the community. Inequality is then evaluated and recommendations made.

## Distribution of Income

What matters is the level of income, a question of what it will buy as well as how it has increased in relation to others, and of dividing the national cake. We want to see how different sections of the community progress in relation to each other and what effect taxation has on relative position and purchasing power.

We need to compare like with like and so compare incomes at the same level in the community, but at different points of time. In this way we get a clear and objective picture of level of remuneration and how it changes, for different levels within the population.

We know how incomes are distributed through published official statistics on the tax paying population[1,2]. By 1952 post-war conditions had settled down, and choosing 1952 as a base gives a period of comparison of sixteen years to date, which is as far back as is required. The last year for which income and tax data for upper income groups are available with reasonable certainty, due to delay in assessing surtax, is the year 1963. Hence changes are assessed here for period 1952 to 1963.

Income may be compared in different ways, for example emphasizing differentials or percentage increases, or biased towards a particular section of the community rather than another. Where such comparisons are made here, bias is pointed out where it exists.

What matters to the individual is what his take-home pay will buy, that is his purchasing power. Hence when comparing gains in income we compare how purchasing power has changed and how additional purchasing power is being shared out among the population.

## Changes in Pre-tax Income

Figure 1 compares the incomes of the tax paying population in 1963 with those in 1952. By numbers the population has not changed much, being about 20 million in 1952 and about 21 million in 1963. This is pre-tax income, that is before deducting tax. The fairly successful person earned in 1952 about 2.4 times and in 1963 about 2.6 times the income of the unsuccessful person. While the pre-tax income of the unsuccessful person increased by 81%, that of the fairly successful person increased by 92%, during those eleven years.

The overall pattern appears to have remained much the same and one might conclude that moderate success means 2½ times the income of the unsuccessful and that pre-tax remuneration increased by about 85% all round. But appearances are deceptive since use of percentages is misleading, shown by figure 2 which shows how pre-tax increases for period 1952/1963 were distributed. Increases are gain expressed as a percentage.

The lower paid gained least but there is not much difference between them and the bulk of the population which gained from 80 to 95%. As the well-off, namely the top 5% of the population, seem to be doing rather badly, there seems little (even for a socialist) to complain about.

But gain is additional spending money, and the picture looks quite different when we take this into account. Considering how pre-tax annual incomes increased during the eleven years between 1952 and 1963, we see that the income of the upper 1½% of the population increased by £1,320 and much more, that of the lowest 10% increased by only £174 and much less. This is a very big increase in inequality.

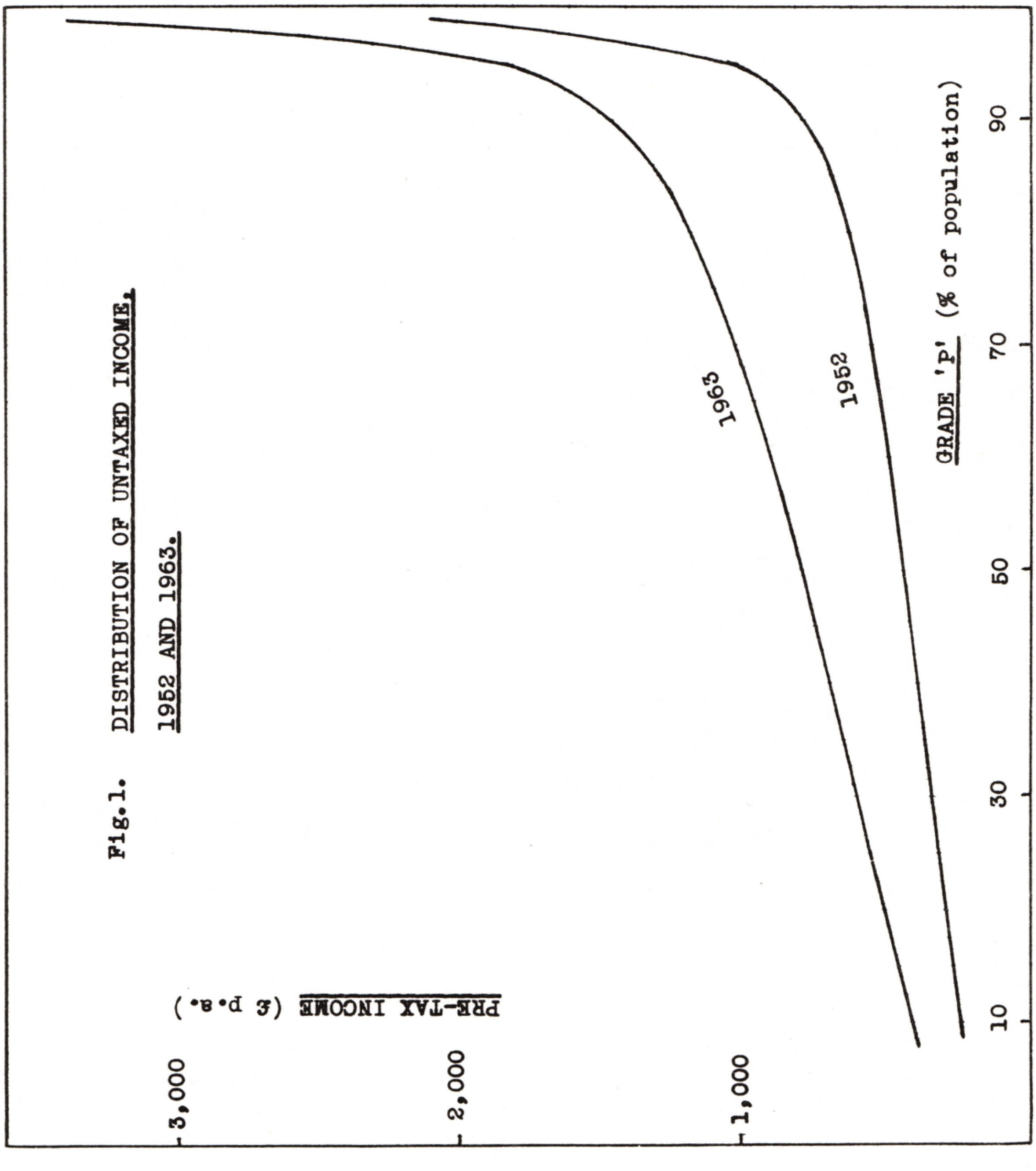



Fig.1. DISTRIBUTION OF UNTAXED INCOME, 1952 AND 1963.

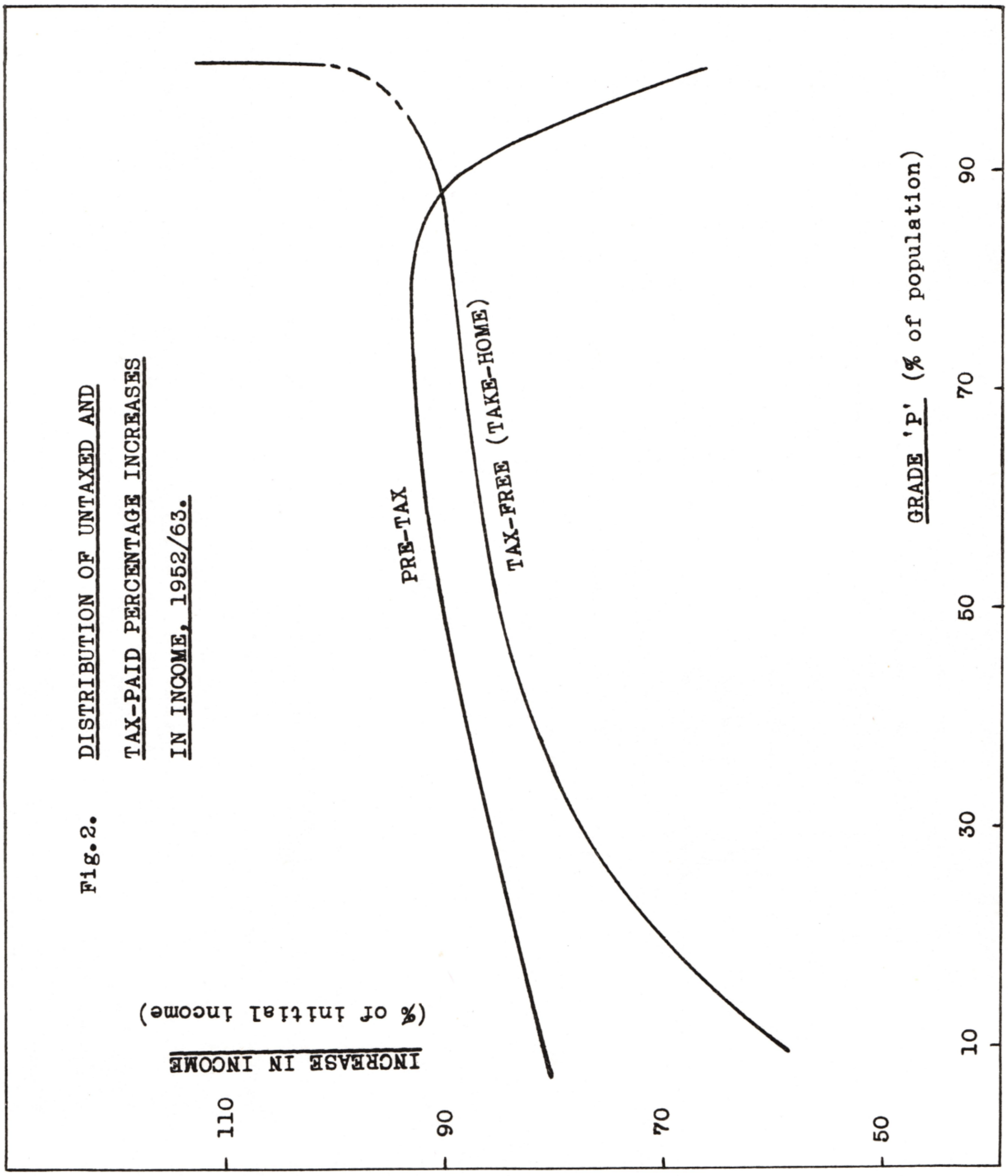



Fig.2. DISTRIBUTION OF UNTAXED AND TAX-PAID PERCENTAGE INCREASES IN INCOME, 1952/63.

At the lower end, we have 2 million tax payers whose pre-tax income has gone up from £216 p.a. to £390 p.a. or much less, while at the upper end we have 300,000 whose income increased during the same period from £1,900 p.a. to £3,220 p.a. and much more. Looked at another way, while 2 million people gained a mere £174 p.a. or less, 300,000 gained £1,320 p.a. and more.

The earnings of manual employees depend very much on hours worked, that is on the state of the economy, and inequalities are much greater during a time of unemployment, during economic crisis and stagnation.

We see that poverty and differentials increase even in an affluent society under full employment, as long as attention remains focussed on percentage increases instead of on amounts, through use of indices which are expressed as percentage increases or as ratios.

## Effect of Income Tax

Consider increases in tax-free income, without as yet considering the effect of rising prices due to inflation. We see from figure 2 which illustrates effect of taxation on percentage increases, that the lower paid have had far smaller gains than the better off. The lower 30% of the population are losing out. They receive smaller percentage increases of smaller incomes.

The great inequality between the well-off and the rest of the population is revealed when one looks at the spending money these percentages represent, illustrated by figure 3. While the bulk of the population gains a little, the annual additional spending power taken by the top 2½% of the population is, by comparison, very large indeed.

Figure 3 shows how pre-tax and tax-free increases are distributed among the population. About 10% of the increase is collected by the Government as income tax. The more successful have gained, and retain, more. They, namely the upper 10% of the population, pay a little more tax but retain far larger sums. The facts do not support the contention that initiative of directors and top level executives is being sapped through excessive taxation: it is at the lower end of the scale that tax should be reduced or reversed.

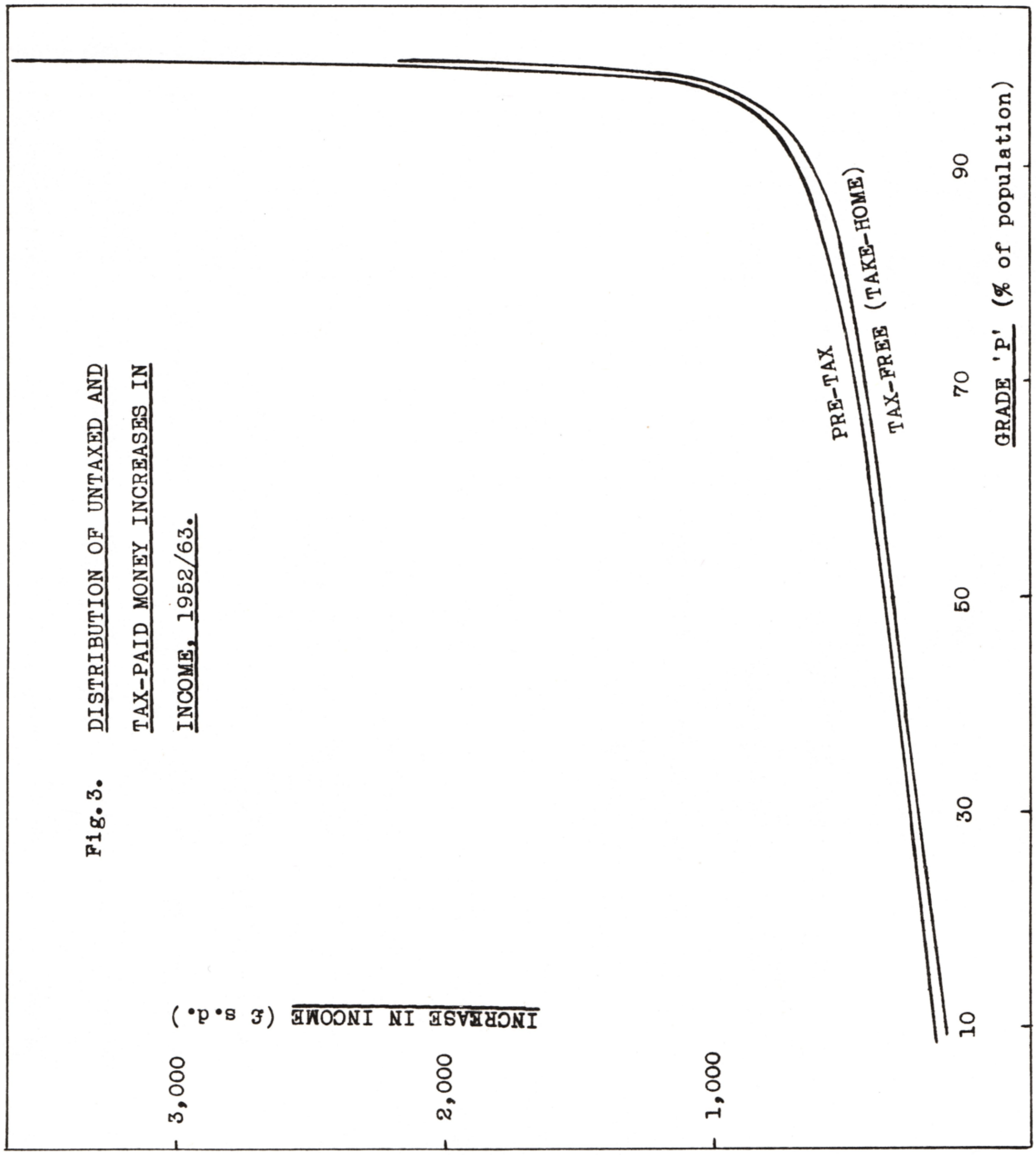



Fig.3. DISTRIBUTION OF UNTAXED AND TAX-PAID MONEY INCREASES IN INCOME, 1952/63.

As illustrated by figure 2, spending money of the lower 10% of the population increased by only 60% of their initially small amount, while that of the upper 10% of the population increased by 90% of their previous income. Directors[4], in the uppermost 0.375% of the population, increased their already large income by 110%.

## Effect of Inflation

We need to consider the value of any increase to the recipient in terms of purchasing power and increasing standard of living. Before assessing material gain we need to deduct from increases received the part which has been absorbed by increases in the cost of living.

Assuming that all costs increase by the same percentage, we could reduce each increase correspondingly. But it would be unreasonable to apply such a correction to surplus income as well as to that spent on necessities or reasonable living. Suppose we assume that only the top 5% of the population earn more than is required for reasonable living. Their additional income is surplus income. Hence we deduct from the increases of the top 5% the same amount as is deducted at the 95% level, as having been absorbed by the increasing cost of living. At the lower end of the scale all income is spent on necessities and income does not keep pace with increasing costs nor does it rise to provide a better life through sharing in increasing standard of living. We cannot justify deducting at the lower end the same percentage of an already meagre increase. Hence to allow for increases in cost of living we deduct the increase in living cost at the 20% level from all those earning that or less.

The retail price index for 1963 was 1.37 times that for 1952. Higher living costs thus absorbed an amount equal to about 40% of the 1952 income, but the result of the adjustments outlined in the preceding paragraph is to limit the amount absorbed in meeting higher costs during this period to not less than £110 p.a. at the lower end of the scale, and to not more than £340 p.a. at the other. What is left is betterment, i.e. additional purchasing power, and table 1 shows how this was shared out during the period 1952 to 1963.

Table 1 shows that an individual who during these eleven years retained his position, for example at the unsuccessful level in the community, is better off at the end of the eleven year period by about £20, which compares with corresponding increases of £180 and £1,820 at the median and successful levels, respectively. The lower 30% of the population are doing badly and the comparison explains the present preoccupation with child poverty, with squalor amidst affluence, and the hardship of those whose income is fixed.

| Position in general population (P) | Position in ruling level (R) | Tax-free 1952 income (£) | Tax-free 1952/63 gain[1] (£) | Cost of living rise (£) | Betterment[2] (£) |
|---|---|---|---|---|---|
| 10 | | 216 | 127 | 110 | 17 |
| 20 | | 266 | 187 | 110 | 77 |
| 30 | | 309 | 241 | 124 | 117 |
| 50 | | 398 | 337 | 159 | 178 |
| 90 | | 688 | 632 | 275 | 357 |
| 95 | | 845 | 785 | 340 | 445 |
| | 10 | 2380 | 1800 | 340 | 1460 |
| | 50 | 2740 | 2160 | 340 | 1820 |
| | 90 | 3520 | 3320 | 340 | 2980 |

Notes 1 Gain is increase in tax-free income (take-home pay).

2 Betterment is increase in purchasing power, i.e. what is left of an increase in take-home pay after the rise in the cost of living has been met.

Table 1 SHARE-OUT OF ADDITIONAL PURCHASING POWER AMONG POPULATION, 1952/63.

The ruling level amounts to the top 0.375% of the population (about 78,000 in 1963), and their incomes are very much bigger than those received by the population. Median betterments for the population and for the ruling level are £180 and £1,820, each year, respectively.

## Sharing out the cake: Inequality

The tax paying population is here divided into three levels: general population, upper, and ruling. These are defined in table 2.

| Level | Symbol | Percent of total tax-paying population | 1963 | |
|---|---|---|---|---|
| | | | Number of incomes | Pre-tax income range |
| Ruling | R | 0.375 | 78,200 | 6,600 - 20,000+ |
| Upper | U | 1.125 | 234,500 | 3,220 - 6,600 |
| General population | G | 98.5 | 20,529,300 | 275 - 3,220 |
| Population (total) | P | 100.0 | 20,842,000 | |

Table 2 RULING AND UPPER LEVELS

| Level | Percent of Population | Share[1] received (%) | Inequality | |
|---|---|---|---|---|
| | | | Between levels | Relative |
| Ruling | 0.375 | 19.4 | 51.6 | 96.6 |
| Upper | 1.125 | 28.0 | 24.9 | 46.6 |
| General population | 98.5 | 52.6 | 0.53 | 1.0 |
| Total population | 100.0 | 100.0 | | |

Notes 1 Share of total available increase in purchasing power, expressed as percentage of total for all levels, i.e. of total for the country as a whole, after deducting income tax and after deducting amounts needed to meet increases in the cost of living.

Table 3 INEQUALITY IN SHARING OUT ADDITIONAL PURCHASING POWER, 1952/63.

There can be no hard and fast dividing lines, but general population includes professional as well as manual employees, ruling level consists mostly of directing employers while in between we have the upper level which includes among a broad range of individuals also directing employees. For illustration, table 2 gives the 1963 income range for each of the levels.

Table 3 shows how the available increase in purchasing power has been shared out among levels, estimated from income distributions. Available increase in purchasing power is the additional sum distributed as betterment, i.e. what is left of total take-home pay, after paying income tax and after covering increases in cost of living.

The increase received by an individual in a level is estimated by dividing the total increase received by all in that level by the number of individuals in it. It should be appreciated that there are wide variations in increase and share received within any one level, i.e. the comparison is valid for levels, but not for specific individuals. In particular, in the general population, the poor are much poorer, and compared to them the inequalities are much greater. Also the figures given here do not include unrealized accumulating wealth such as that accruing to shareholders through undistributed profits and capital appreciation. Again, inequality is much more glaring than appears from comparing levels.

Table 3 gives the inequality and clearly shows the effect of numbers. 98.5% of the population received 53% of the additional purchasing power, while at the other end of the scale, 0.4% of the population received 19% of the additional purchasing power.

Inequality between levels is measured by the ratio of what was received by an individual in a particular level to the increase everyone would have received had the available sum been shared out equally among all the population. Table 3 shows that a person in the ruling and upper levels received 52 and 25 times this 'equal share', respectively, while each person in the general population provided these large increments by taking only a half of the 'equal share'. Each person in the ruling level gained about 100 times, and in the upper level gained about 50 times, the increase received by a member of the general population. 0.4% of the population are getting 100 times the individual gain in purchasing power obtained by the general population.

## Appropriate Pay

We have seen that the increases in national wealth are being shared out most unequally. Not only are the have nots increasing in number, but the differential between the haves and have nots is increasing at the same time. The tax-free incomes speak for themselves. A 1952 differential in take-home pay of £2,500 p.a. increased to £4,560 in 1963.

We need to adjust the total income from all sources to ensure effective utilization and appropriate sharing out of the increasing national wealth. The recommendations made here would remove the most glaring inequality. Incentive to do well and reward for good work are not affected by them since reward for increasing skill and professional excellence are not affected by the proposed adjustment.

What matters is the purchasing power of take-home pay and increases in this are the betterment. Income tax can be used to adjust the incomes distribution so as to apportion betterment more appropriately. Betterment is discussed in Appendix 1 and it can be restricted by income taxation so that it does not exceed that at the successful (95%) level, when the upper 5% of the population each receive the same large gain, and so that the lower 30% or so of the population receive the gain at about the 30% level.

This redistribution of gain would be without hardship to anyone, and would adjust the distribution of gain and betterment as illustrated by figure 4. The additional amount collected from the highest incomes is used to reduce tax payable by the lowest income earners, and to increase their take-home pay through direct or indirect payments from the tax-collector when take-home pay is unacceptably low. The total income to the state from income tax collection remains unaltered.

For example, the additional amount of tax collected in this way during 1963, compared with 1952, would have amounted to about £330 millions, p.a., which would ensure a gain of about £210 p.a. for 25% of the population. The result would have been a 1963 minimum wage of £545 p.a. (about £10.10.0d. per week) and over 5 million people would have benefited by it. Unresolved is whether some should benefit more than others, for example whether single persons should be treated differently from say widowed mothers, or whether a distinction should be made between a family's first and second income.

Figure 5 shows how the adjusted gain compares with increases for period 1952/63, thus illustrating the effect of redistributing increases in the way described here. Those at mere existence level would have had an assured tax-free gain of £210 p.a., the very successful would have had a tax-free gain of £785 p.a. It is important to appreciate that differentials, i.e. the incentive to succeed in the community, would have increased above the 1952 differential, during this period, by an additional £785 - £210 = £575 p.a. take-home pay.

What we have said about adjustments applies to particular positions, to particular income levels in the community. It enables income-tax rates to be adjusted but does not apply when looking at increases given to particular individuals. Such increases depend on changes in skill, professional excellence and on demand as compared with supply, resulting in corresponding upward or downward movements between income levels in the community. We must continue to give increases for additional skill and professional experience. Where this is not done, difficulties are experienced.

## Professional Employees

The work and pay of professional employees have been analysed and compared with that of manual employees. Professional employees such as doctors, engineers, managers and scientists, are paid according to a fairly rigid national scale of remuneration[3]. It is a scale which determines reward in accordance with the responsibility carried and which is used to determine annual increments. The scale, in connection with a similar scale at a different point in time, may be used to determine how a particular individual has maintained his position within his group or how a group has maintained its position in relation to other groups.

The professional employee, at the start of his career, ought to expect considerable increases in remuneration and status. But increases for economic factors are determined by manual employees' wage rates instead of by their earnings[3], so that professional employees are losing ground. The rate at which status is reducing is such that there is no positive reward for the professional employee for the increasing responsibility he carries as he grows older. In other words, the professional employee must work at an ever higher level of responsibility so as just to maintain his status.

There is thus little or no incentive for the individual professional employee to carry greater responsibility.

## Conclusions and Recommendations

Poverty and differentials increase in an affluent society as long as attention remains focussed on percentage increases instead of on amounts, through use of indices which are expressed as percentage increases or ratios. The great and increasing inequality between the well-off and the rest of the population is revealed when one looks at amounts each receive as their share of the increasing national wealth.

10% of the population are sinking into direct poverty, their gains in income being wiped out and being overtaken by the increasing cost of living. This process has been going on for many years.

The next 20% are being reduced to relative poverty, are losing out.

At the professional level there is lack of incentive. Increasing skill and professional experience are not being rewarded by appropriate increases in remuneration.

The top 0.4% of the tax paying population, about 78,000 people, including directing employers, are receiving gains in individual purchasing power which are 100 times those received by individuals in the general population (95% of the population).

The facts do not support the contention that initiative of directors and top level executives is being sapped through excessive taxation. Most pay some additional tax but retain far larger sums than others. It is among people who earn the lowest incomes that taxation should be reduced or reversed.

An increase in incomes at the top is not in fact followed by corresponding increases at lower levels. This is as expected, since income depends on the work being done, on the rate for the job.

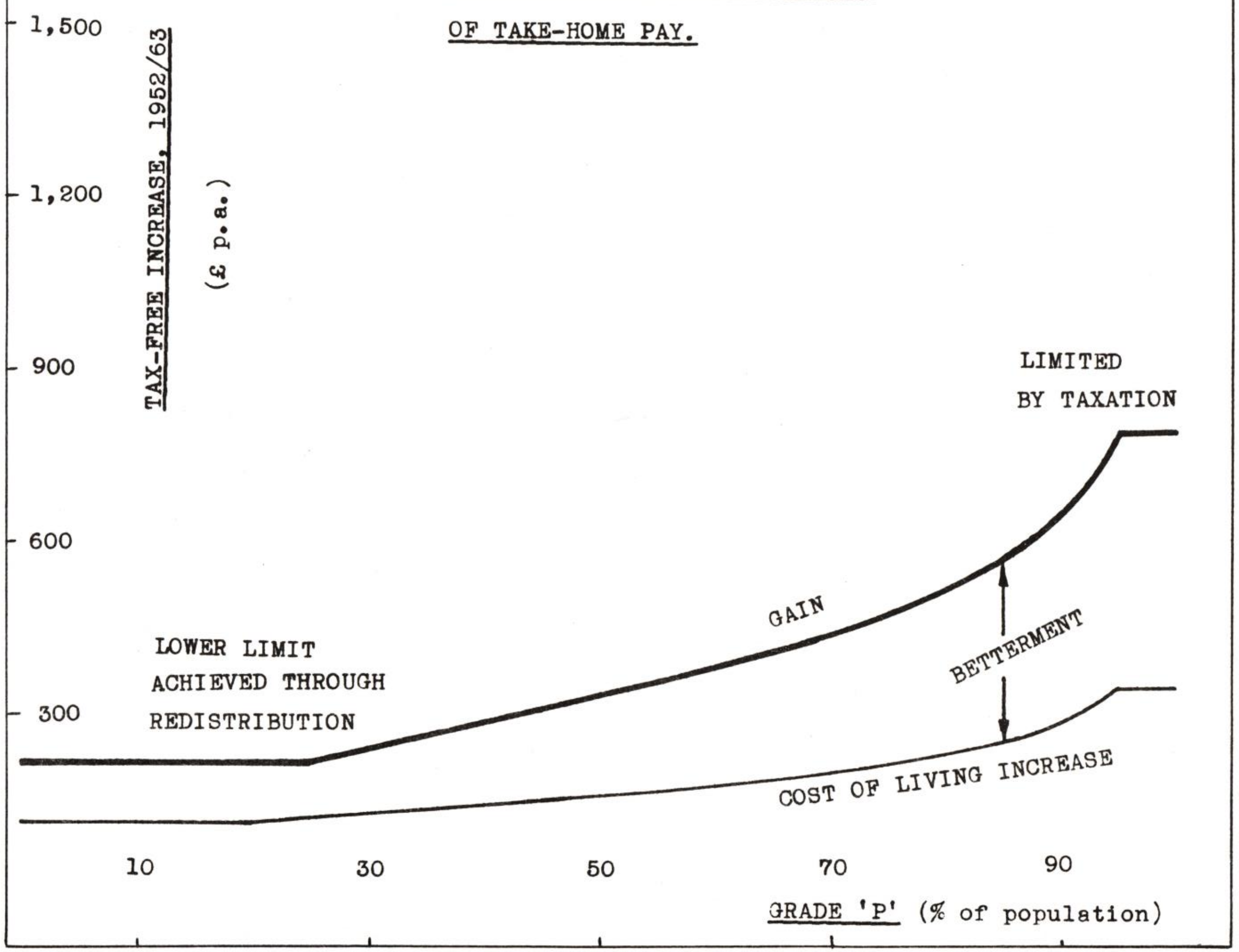
The incidence of income tax should be adjusted so as to apportion betterment more appropriately, where by betterment we mean increase in purchasing power of tax-free pay.

Betterment should be restricted so that the top 5% of the tax-paying population receive the same large gain each, namely that at the 95% level. By gain we mean increase in tax-free income and the money collected by restricting betterment should be distributed among the lowest income earners in such a way as to give them the same gain each, this being the minimum.

This would materially affect the lower 25-30% of income earners, through reduced taxation or through direct or indirect payments to them from the tax collector, at no hardship to anyone, at no additional cost to the government.

We must continue to give increases for additional skill and professional experience.

Fig.4. BASIS FOR REDISTRIBUTING INCREASES IN PURCHASING POWER OF TAKE-HOME PAY.



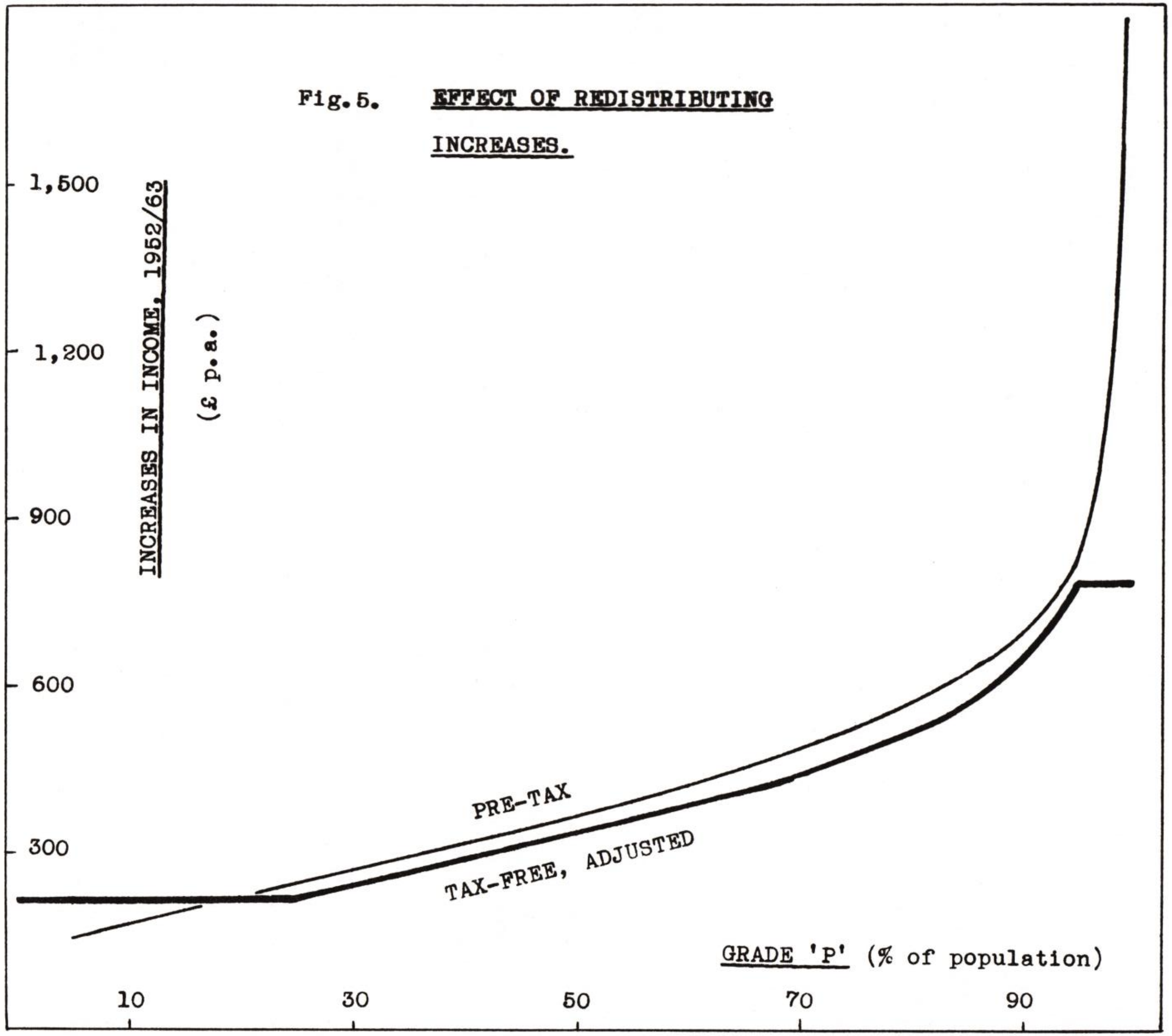



Fig.5. **EFFECT OF REDISTRIBUTING INCREASES.**

## References


1 Annual Abstract of Statistics, H.M.S.O., No. 96, 1959.

2 Annual Abstract of Statistics, H.M.S.O., No. 103, 1966.

3 The Status and Remuneration of the Professional Man in Industry, M. Davidmann, Social Organisation Ltd., 1961.

4 Work and Remuneration of Directors, Social Research Development Ltd. report, 1968.

## Appendix 1

### Betterment

Betterment is what is left from an increase in after tax take home income after deducting that absorbed by higher living costs in the same period. This applies to any specific income level in the community and changes can be evaluated from income distributions for the community as a whole.

Betterment = increase in purchasing power
COL = increase in cost of living
Gain = increase in tax-free income

These three terms, over the same period, are related as follows:

Betterment = Gain - COL

The amount absorbed by higher living costs has been taken as a percentage of initial income, taken as that in 1952 in the worked example. The percentage is taken as the change in the cost of living index, limited in amount to not less than that at the 20% level, and to not more than that at the 95% level. These amounts were £110 and £340, respectively, for period 1952/63.

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## WORK AND REMUNERATION OF DIRECTORS

This report describes and discusses the work and remuneration of chairmen, managing directors and directors. It describes remuneration patterns, compares chairmen with directors, part-time with full-time employment and remuneration, gives information on the effect of size of company and about the size of the board.

Directors are paid in different ways, including fringe benefits. An objective measure of the worth of fringe benefits is discussed.

Remuneration data and surveys are analysed. Some are shown to be based on inadequate data. Reward and incentive payments appear to be great. The remuneration of directors, as a group, may be increasing at a substantial rate.

For large companies, for 1966, a curve is given for the remuneration of chairmen, and also one for directors, which compare their remuneration, showing the degree to which it depends on relative position, that is on success. It applies to full-time employment. Remuneration ratios are given for chairmen compared with directors, and for part-time compared with full-time employment for chairmen and directors.

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