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Social Research Development Limited

NON-PROFIT MAKING · LIMITED BY GUARANTEE

WORK AND REMUNERATION OF DIRECTORS

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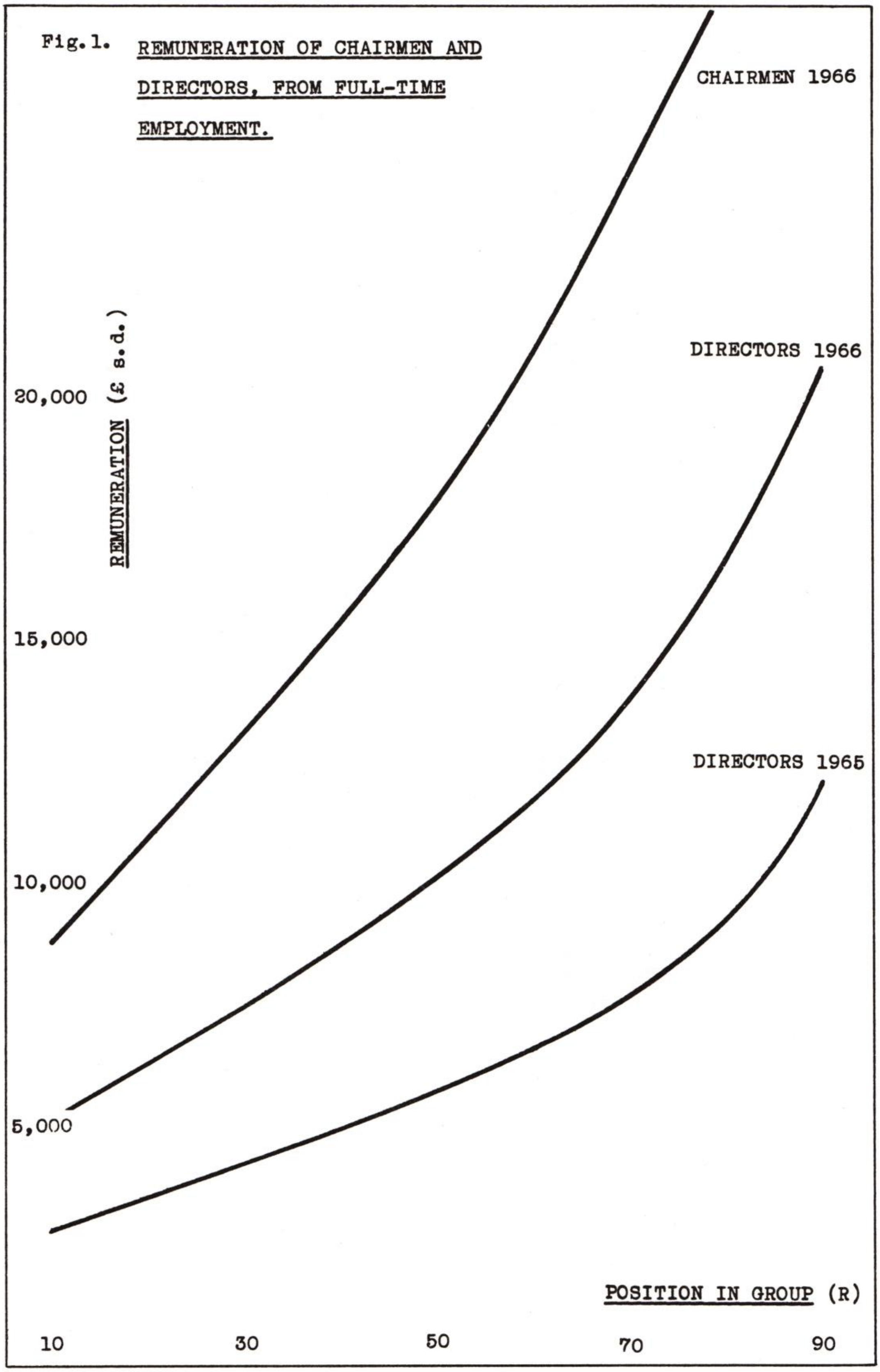
Fig. 1.
REMUNERATION OF CHAIRMEN AND DIRECTORS, FROM FULL-TIME EMPLOYMENT.
CHAIRMEN 1966
DIRECTORS 1966
DIRECTORS 1965
REMUNERATION (£ s.d.)
20,000
15,000
10,000
5,000
POSITION IN GROUP (R)
10
30
50
70
90

WORK AND REMUNERATION OF DIRECTORS

A member of the Prices and Incomes Board speaking[8] at a conference of the Industrial Society in London, said that the responsibility for Britain failing to achieve much more rapid economic growth would lie with those who have the power to put it right, i.e. with "the Government and the boards of directors of almost all our major undertakings", the fault mainly of some 5,000 people.

This report discusses what is known about the work and income of directors since some of them consider themselves underpaid and so lacking incentive. It examines the evidence and evaluates the claim from this important section of the community, since we need to provide incentive where needed and reward where earned. We need to look at how directors are paid and at what changes have taken place.

Directors

About 38,000 directors are listed in the 1967 Directory of Directors, all on boards of very roughly 13,000 companies with a paid up capital of over £50,000 each. Of these directors, 14,000 are members of the Institute of Directors, which had a membership of 44,000 in December 1966. Hence 30,000 of the Institute's members serve on the boards of smaller companies, as illustrated by table 1. These 68,000 directors direct our large companies and control a good few of the smaller ones. This determining directing level is here referred to by "directors". Pay should relate to responsibility and to assign responsibility one needs to consider directing employers and not employed directors. This determining directing level does not include directors who are full-time salaried employees who are almost forced to agree to the suggestions of their chairman or managing director on whom they depend for livelihood. Directors who are salaried employees, dependent for example on but one directorship, are 'employed directors'. We need to distinguish between directing employers and employed directors.

The average board for the size of company we are considering consists of one chairman, one managing director and between four and seven directors, all full-time. The

Institute membership, as can be seen from table 2, consists of one chairman and two managing directors for every one and a half ordinary directors. The Institute of Directors thus represents chairmen and managing directors rather than directors as a group.

The Institute of Directors represents and speaks for directors as a whole. In fact its membership consists largely of chairmen and managing directors, who are 'employers'. The Institute of Directors thus would seem to represent and speak for directors' employers, exerting pressure on the community. In the pages of its journal 'The Director' and through the press it is claimed that directors are underpaid for the work they do, that they lack incentive. But surveys of their own members apply more to chairmen and managing directors than to directors.

The number of directors on boards of large companies together with the Institute of Directors membership, gives some idea of the number of directing employers. It is unlikely to exceed 68,000 and this tells us something about their incomes.

In 1963 there were 20,842,000 persons who paid income tax. In this taxpaying population, the top 68,000 persons each earned more than £7,000 p.a. in 1963, while the top 5,000 each earned £20,000 p.a. and above.

It seems difficult to see how they can be either underpaid or lacking incentive, even after taxation, seeing that their incomes today are much larger than they were then.

Remuneration

A director is paid in different ways. He gets a salary, fees per attendance and benefits, which are often related to profits, as agreed by the company. Fringe benefits are:

Share of profits by way of bonus as profit sharing.

Share ownership and share options, with consequent capital gain.

Gratuity on retirement. Compensation when dismissed.

Pension, including expensive 'top hat' benefits. Employers' contributions need to be compared, not those made by employee out of his own earned income.

Company car.

Help with children's education from his company, not mentioning the large sums he receives indirectly from the state when sending his children to 'public' schools.

Medical insurance, expenses and examinations. (A medical check-up at the Institute of Directors costs £26.5.0 at present).

Life assurance.

Telephone allowance.

Payment of club and professional institution fees.

Purchase of employer's products at reduced prices.

Family allowances provided by employer.

Holiday bonuses. Longer holiday period with full pay.

Widows' and orphans' pensions.

Accident insurance.

Removal expenses on initial engagement.

Expense and entertaining accounts.

Trips abroad. Travel concessions.

Social security of a high order. Payment of full remuneration while ill. (This is an important component of any pay and depends on for how long or often it is made and whether this entitlement is cumulative).

Secure from reduction of income through stoppage of overtime or reduced working week, during economic crisis.

Fringe benefits may[6] amount to £2,000 p.a. on a basic salary of £7,000 p.a. and while any one director is unlikely to be receiving all or even most of the fringe benefits listed above, the large additional sum of £2,000 to be added to £7,000 did not include some large items from the list above.

Access to social services and benefits is another aspect of remuneration which could be included here, and unearned income is really a form of mutual benefit at the kind of upper level we are here considering.

Length of holidays and hours worked are important aspects of remuneration, and are fringe benefits only in so far as their level differs for different levels in society.

We need to arrive at an objective measure of the worth of fringe benefits, which allows for what the individual earns already. The value of fringe benefits to the recipient is the grossed-up value of the benefit, is what he would have had to earn at his level of taxation so as to have the value of the benefit remaining after tax has been deducted.

Remuneration Data

The Institute of Directors surveyed[3] the remuneration of its members, as at February 1966. The survey covers a larger range of company size as compared with other surveys which looked at a few large ones only. One needs to remember its bias towards managing directors and chairmen.

Coulthard reported[4,5] directors' remuneration in relation to size as indicated by sales turnover. Information is given on size of board and "average full-time director's emoluments" for just under one hundred companies with a sales turnover between £1 million to £1,500 million, p.a. No distinction is drawn between chairmen and directors, but only full-time directors are included. As in Coulthard's other work, apart from fundamental differences in defining and estimating income in each case, the sample is too small and unrepresentative for valid conclusions to be drawn.

Coulthard, a director of P.A. Management Consultants Limited, published another article in The Director[7]. His data is drawn from only 64 companies from among the 400 largest in this country. Since we have roughly 13,000 companies with a paid up capital exceeding £50,000 each, his sample is quite inadequate, being too small and unrepresentative.

Included are many part-time chairmen and directors and, since income from part-time is much less than that from full-time directing, this makes it appear that directors earn less than they do in fact receive. He then compares these reduced incomes with the full-time earnings of manual employees, which include overtime payments, to back up a pay claim for directors.

The Institute of Directors has in the past emphasized[2] the essential difference between 'directing' and 'managing', so why is Coulthard astonished that there are a few executives earning more than £10,000 p.a. who are not on the boards of their companies? His sample is small and conclusions drawn from all his directors taken together need to be regarded with some reserve so that, bearing in mind the scanty evidence, one is even more surprised to find him jumping to conclusions about differences in pay between overseas and home executives and directors. He also states that there are no natural laws for the determination of remuneration, perhaps unaware that the natural laws are well known, that they have been used for some time, been generally available[1] since 1961.

Coulthard's basic data can be converted into objective form. Table 6 gives the data objectively; full-time directors are listed separately from part-time directors, while a distinction is drawn between chairmen and other directors. Other data has also been correlated to a common basis for comparison. Remuneration data is here given for unsuccessful, median and successful chairmen and directors, as defined by table 3. The letter R stands for position of individual in his group. For example, the R.10 director is unsuccessful as a director, since 90% of directors earn more than he does. Similarly the R.90 director is successful since only 10% of directors earn more. Table 4 gives remuneration data from the survey undertaken[3] by the Institute of Directors. Table 5 gives Coulthard's data on effect of size of company.

Remuneration Patterns

Figure 1 illustrates the remuneration pattern for directors as a whole which emerges from the data given in tables 4-6. Coulthard's earlier data (table 5) is not included as it is based on average emoluments from published balance sheets, based on remuneration received by a board rather than by individual directors.

This data shows that the remuneration of directors as a group appears to have increased very substantially in a single year, the increase being 75% between 1965 and 1966. An explanation may be that directors of larger companies (table 6 for 1966) earned in any case more than members of Institute of Directors (table 4 for 1965) most of whom may be working in smaller companies.

Size of company

Coulthard's earlier article gives at least some indication of the effect of size of company on remuneration, as shown by table 5. There is hardly any difference in remuneration for the range £1-10 million p.a. sales turnover, but multiplying this sales turnover a hundred fold may double a director's remuneration.

This is data from just under 100 companies, and average incomes vary from £8,000 to £16,000 p.a., dependent on size.

Chairmen and directors in part-time and full-time employment.

Figure 1 and table 6 clearly show the difference in remuneration between chairmen and directors. Chairmen are one level above directors and their remuneration indicates this, as they receive about 1.8 times as much as directors. Part-time chairmen receive about 2.7 times as much as part-time directors.

Income from part-time employment, from a single appointment, is 0.3 and 0.2 of that from full-time employment, for chairmen and directors, respectively.

To sum up:

		remuneration ratio
Chairmen/directors	Full-time	1.8
	Part-time	2.7
Part-time/full-time	Chairmen	0.3
	Directors	0.2

When considering the total income of part-time directors, one needs to know the number of part-time directorships held and the remuneration received from each. The remuneration of a part-time director who earns £2,000 p.a. from each of three part-time appointments is £6,000 p.a.

38% of members of the Institute of Directors hold more than one directorship[3], which agrees with the figure of about 34% given by Coulthard. Both include chairmen among directors, and the data of the Institute of Directors is heavily biased towards chairmen and managing directors. The number of appointments held was found to be distributed as follows:

number of boards	% of total	
1	58	
2	14.4	part-time = 38%
3	9.1	
4	6.9	
5 or more	7.6	
no answer	4	
Total	100.0	

According to this table, the median part-time director holds about 2½ appointments.

Size of boards

Table 5 gives information about the size of the board of directors in large companies. Coulthard's ratio is about 9½ directors per chairman, which implies an average board of one chairman, one managing director, and eight or nine directors, for larger companies, which compares with the more usual chairman, managing director, together with between four and seven directors, all full-time.

Underpaid and lacking incentive?

It is a little difficult to believe that the income of directors increased by 75% in one year. This high percentage is a reflection of the doubtful value of data published so far on incomes and remuneration.

While size of company appears to have little effect on remuneration of directors, at least for the range £1-10 million p.a. sales turnover, multiplying this a hundred fold may double a director's remuneration. It is thus possible that some of the apparent difference between the 1966 and 1965 remuneration data for directors is due to the 1966 sample being biased towards directors in larger companies. Even so, there would seem little doubt that remuneration of directors increased appreciably in that year.

The fact is that instead of being underpaid their incomes are increasing quite rapidly[9], which applies to tax-free take-home income, which includes indirect payments amounting to a great deal of money. Such indirect payments need to be included in any assessment of directors' incomes, as grossed-up, i.e. pre-tax income.

There is no evidence of any lack of incentive for chairmen or for directors. On the contrary, unsuccessful chairmen and directors earned £9,000 and £5,000 in 1966, the differential between success and unsuccessful amounting to another £30,000 and £15,000 p.a. respectively. One can only conclude that reward and incentive payments are great.

Remuneration needs to be related to work done and to how well it is done. Since 1961 Britain's gross national product increased by about 16%, that of W. Germany, USA, France and Italy by 30-40%, that of Japan by over 80%. Comparing reward with performance one concludes that performance is inadequate and may seriously question whether chairmen and directors are giving value for money received.

Conclusions and Recommendations

1) The remuneration of chairmen and directors is increasing very appreciably and more than adequately.

2) Differential pay, i.e. incentive towards succeeding in their profession, towards doing well, is great and more than adequate.

3) They are paid in many direct and indirect ways, receiving fringe benefits. All such payments should be included in any assessment of income, as an increment of pre-tax income at his level of taxation, such that the value of the benefit remains after taxation.

4) Performance is inadequate.
Remuneration should depend on performance. While pay and incentives appear to be excellent, performance appears inadequate and it seems that the community is not getting value for the large sums being absorbed by chairmen and directors as a group.

5) Chairmen receive about twice as much as directors. The rewards for leadership are theirs and so should be the responsibility for inadequate performance.

References

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

2. Standard Boardroom Practice. The Institute of Directors, London, July 1964.

3. The Director Observed, The Director, April 1966.

4. L. Coulthard, The Market Price for Directors, The Director, Aug. 1966.

5. L. Coulthard, Directors' Pay: Five Key Questions after the Freeze, The Director, Oct. 1966.

6. Hay - MSL survey, Observer, 4 Dec. 1966.

7. L. Coulthard, If Disclosure Came Today, The Director, Mar. 1967.

8. Guardian, 30 June 1967.

9. Appropriate Pay, Social Research Development Ltd. report, 1968.

Illustrations

Number of Directors	
in small companies (3)	in large companies (3)
30,000 (2)	24,000 14,000 (1)
30,000	38,000 (2)

Notes: (1) Source: Directory of Directors (1967).

(2) Source: Institute of Directors (30/12/66).

(3) Small companies have paid up capital of less than £50,000. Large companies are considered to be those with paid up capital of more than £50,000.

Table 1 Number of Directors

Title	% of total
Chairman	21
Managing director	41
Director	35
No reply	3
Total	100

Table 2 Membership of Institute of Directors. [3]

Position of director among directors.	Degree of success among directors.	% age of directors who earn less.
R10	unsuccessful	10
R50	median	50
R90	successful	90

Table 3 Positions among directors

Position in Group	Remuneration (£ p.a.)
R10	2,700
R50	5,700
R90	12,000

Notes
1. Remuneration: total taxable income.
2. Period: As at February 1966.
3. Group: Members of Institute of Directors. Includes part time directors but more chairmen and managing directors than directors.
4. Includes a broad range of size of company. Median company employed a capital of £150,000.
5. Source: Reference 3.

Table 4 Remuneration of Directors, 1965.

Average Full Time Director's Emoluments (£ p.a.)			
Position in group (R)	Size of company (Sales turnover in £ mill p.a.)		
	1 - 5	5 - 10	100 - 1500
10	5,100	5,300	10,500
50	8,200	8,400	16,000
90	14,000	14,300	25,500
Average board (full time directors)	6	8	9 (3 - 24)
Sample (No. of companies and "nationalised industries")	30	30	34 + "4"(4)
Data reference	5	5	4

<u>Notes</u> 1. Remuneration = average full-time director's emoluments

$$= \frac{\text{emolument figure (fees excluded)}}{\text{no. of full time directors}}$$

where emoluments = fees, salary, commission, expenses, pension contributions, payments in kind, stock options.

2. Period: 1965/66.
3. Group: a few large companies.
4. Largest in country.
5. Includes chairmen and managing directors.

Table 5 <u>Remuneration of Directors in Relation to Company Size</u>

Remuneration (£ p.a.)		
Position in group	Chairmen	Directors
Full time		
R10	8,600	5,100
R50	18,000	10,000
R90	38,000	20,000
Part time (6)		
R10	2,800	(7)
R50	5,500	1,800
R90	11,500	5,200
Sample (3) (No. of persons)		
full time	42	463
part time	22	151
total (4)	64	614

Notes

1. Remuneration: Fees and percentages, sums paid as expense allowance in so far as these sums are charged to U.K. income tax, company contributions to pension funds, estimated money value of other benefits.
2. Period: financial year ending 1 Jan. 1967.
3. Group: 64 large companies.
4. Total number of chairmen and directors covered by survey is 678.
5. Source: Reference 7.
6. Of order of.
7. Insufficient data.

Table 6 Remuneration of Chairmen and Directors 1966.

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For more information see Financial Times, 14 Sep 1968, p.17.

The report is called 'Appropriate Pay' and can be obtained from us, price 7 gns.

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