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Public Administration Select Committee

Top Pay in the Public Sector

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Oral and written evidence

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The Public Administration Select Committee

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Witnesses

List of written evidence

Oral evidence

Taken before the Public Administration Committee

on Thursday 30 April 2009

Members present

Dr Tony Wright, in the Chair

Mr David Burrowes	Julie Morgan
Kelvin Hopkins	Mr Gordon Prentice
Mr Ian Liddell-Grainger	Mr Charles Walker

Witnesses: **Ms Polly Toynbee**, *The Guardian*, **Mr Tony Travers**, LSE, **Mr David Clark**, SOLACE and **Mr Ben Farrugia**, TaxPayers' Alliance, gave evidence.

Q1 Chairman: Welcome to our witnesses this morning. The Committee has decided to do an inquiry, amongst other inquiries, into top pay in the public sector, an issue which is causing some interest at the moment. This is the first session in that inquiry and we wanted to hear some views, some perceptions, that we could then test against the evidence later on. We have brought together what we hope is a mixed panel to give us a set of interesting perspectives on this. We are delighted to have Polly Toynbee from *The Guardian;* Tony Travers from the LSE; David Clark from SOLACE, the Local Government Association; and Ben Farrugia from the TaxPayers' Alliance. In the context of this inquiry there are two related questions: Is there an issue about what is happening and what has happened to top level pay in the public sector? And, if there is an issue, what might be done about it? I would like to ask each of you to tell the Committee whether you think, first of all, that there is an issue here that warrants any attention.

Mr Clark: Quite evidently there is an issue, in that it would not be in the public domain so often were there not. If you look across the public sector, one of the things on which my organisation, the Society of Local Authority Chief Executives and Senior Managers, draws wry smiles is that concentration on the local government side, which is one of the very few areas where democratically elected people can determine the wage level, whereas if you look across to other things that really are in the public sector, such as university vice-chancellors and whatever else who earn more, for some reason they are not in the public domain as a debate so much. In a time of recession one of the things my colleagues are very clear about is that there is going to be a degree of envy about that and some understanding that somehow these people are protected. In fact I think it was a good parliamentarian who said that it was "getting out of control, it was like football managers" and I do not think he knew how right he was, because of course the thing about chief executives is that they get sacked quite a lot if they under-perform. I am sure here you will have had civil servants, and maybe they do not get sacked as often—I do not know, you would know more about that than I do. Yes, I think there is an issue. We have suggested to John Healey that we ought to publish what chief executives of local authorities earn in detail, but that it should be published alongside what they do in detail. I think everybody on the Committee—forgive me, possibly with the exception of yourself—has been a councillor, and when I was a councillor in the 1980s I did not know what the chief exec did for the four years I served as a councillor. So I think there is an issue of transparency, but it is not just about pay, it is about activity too. That would be my view.

Q2 Chairman: Thank you very much for that. Polly, is there an issue?

Ms Toynbee: Yes, I think there is an issue. I think people are very concerned if they see what they consider to be large numbers of people earning more than the Prime Minister, for instance. It seems to be a rule of thumb benchmark where it just does not seem reasonable, and you might find lots of reasons why it was or was not. I think, though, it is unfair to look at it in isolation from the general culture outside. What you have is a relatively small leakage from the extraordinary escalation of pay differentials over the last 20 years. For instance, the Institute of Directors themselves produced figures for CEOs to show that, over the last 20 years, average CEO pay compared to their average workforce went from 15 times to 75 times. That is just within a period of 20 years. When you see that explosion of top pay, mostly in the top 1%, it is not surprising that there is some leakage. In fact, in some ways it is surprising, perhaps, that there is not more. According to the TaxPayers' Alliance's own figures, only 387 people in the public sector are earning more than £150,000, so it is not a huge number of people, given how many public sector workers there are, but I do think it is a symptom of a much more general disease and that you should be looking at it in the round.

Q3 Chairman: Is the conclusion from that that you should attend to the source of the leakage rather than the leakage itself?

Ms Toynbee: I think both. I think that if you are going to make a comment about it, it would be appropriate to say that is an inevitable outcome and perhaps you should be looking quite hard at what is happening out there as well. I do not know if that is beyond your remit.

Q4 Chairman: Very likely, unfortunately, but thank you for that. Tony.
Professor Travers: In brief, there clearly is an issue. This inquiry is evidence that there is an issue. In part—and the point has already been made—the debate about bonuses and private sector pay understandably threw light then on some of the top public sector pay, some of which had been rising quite sharply in the last two or three years and probably because of a sort of contagion effect reading across from the big rises in some parts of the private sector. I think all that has got caught up in the wider public debate latterly which has a slightly Maoist tone to it, a slight sense that all high pay is now bad and everybody should be pulled down a bit, and so it is an issue. It simply is an issue in public debate.

Q5 Chairman: Thank you. Ben.
Mr Farrugia: I think there certainly is an issue and our concern at the TaxPayers' Alliance is the large examples of rewards for failure that we have seen. As was said earlier on, chief executives are frequently fired, but we have found plenty of cases where they then move on to higher paid jobs somewhere else. They are fired for incompetence and they move on to a superb job somewhere else with even better benefits or they are fired with enormous compensation packages. That is our concern, these very inflated salaries. Attendant to that is the lack of transparency. We find it very difficult to get those figures which Polly quoted. I think there should be a much larger public scrutiny of these figures which are very hard to get. For instance, there was the story yesterday about the gentleman from CDC earning almost £1 million. That is something that we would find it very difficult to find out even at the TaxPayers' Alliance. It took a committee to find that out. I think we need much greater transparency and far greater scrutiny and many less cases of these simple rewards for failure.

Q6 Chairman: Do you accept what has been said, what Tony called the "contagion effect"?
Mr Farrugia: I certainly acknowledge it. I think it has certainly been a factor.

Q7 Chairman: At the TaxPayers' Alliance you seem only to be concerned about things like levels of pay in the public sector. Things like tax avoidance and tax evasion you do not seem at all interested in.
Mr Farrugia: Our concern is the public sector and government. That is our focus. I am sure there are plenty of excellent groups focusing on tax avoidance and tax evasion, which are a private sector issue. I think our campaign team have put out some comments on tax avoidance and tax evasion which are both negative things that we do not approve of, but our focus is the public sector and pay is one of those things that is symbolic. It speaks to people. They understand it. People do not understand the complexities of some of those things.

Q8 Chairman: Those of us who pay taxes are quite interested in those people who do not pay taxes, are we not?
Mr Farrugia: Absolutely. But we all know about tax avoidance and tax evasion because Polly and *The Guardian,* for instance, have done extensive work on tax avoidance. That is their focus and ours is the public sector. The one particular issue we have been focusing on in the past year or so has been pay.

Q9 Chairman: Before we go on to talk about what we might do about it, let me ask whether there is agreement that, whatever else, we just need to know what is going on. The TaxPayers' Alliance has done important work in tabulating a lot of this, but there seems to be an emerging consensus that, whatever else, we just need to know the figures across the board. Is that a consensus?
Professor Travers: It would be very, very difficult to defend not having these figures in the public domain. It is public money, they are public institutions. Not having the numbers readily available, certainly for senior managers at the top of institutions, is going to be pretty difficult to defend, so I think it is an inevitability.
Mr Farrugia: I am pleased that David said that they are now supporting John Healey's call for local government—
Mr Clark: We said it before John Healey.
Mr Farrugia: Okay. I am pleased about that too. Our experience and my personal experience of dealing with council chief executives is that they are incredibly reluctant and they will use any means possible to withhold the information. They do not want it out in the public domain and I am pleased now that they might be forced to do so. It is not an experience that we have had, this openness. There is no desire for transparency among many chief executives. Of course, I am generalising. There will be some who do and some who are very forthcoming, but there is a sense that in some parts of the public sector they want to hold on to this information.

Q10 Chairman: Do we know which part of the public sector is worse in terms of this transparency? Is it local government? Has it been local government?
Mr Farrugia: It has been local government. I hope that changes. Despite a lot of negative comment about non-departmental public bodies and other quangos, they tend to be rather good and annual accounts tend to have very good annual remuneration reports. Our problem is the extent of the public sector. So much of it is the grey area. We do not know what these bodies are or who they are and consequently we cannot pick them out and investigate them. But, yes, so far it has been local government that has been the hardest nut to crack.

Q11 Chairman: Does anyone else want to say anything about the transparency issue before we go forward?
Mr Clark: I am an ex-serving chief executive, in York. The day came when I said to my sons that I was moving to London, and they said, "Does that

mean you're not going to march with the Army any more, daddy?" and I said, "I'm awfully sorry, yes, it does mean that," and they said, "Yes, but it's good isn't it, the children in the playground won't keep shouting at us because you earn so much money, will they?" Of course, in a city that size—it only has a population of the London Borough of Bromley—everybody knew how much I earned. It was advertised at the time when I applied for the job. The local papers ran it. There is quite a lot of transparency in a lot of areas, so I would not want to get away with this idea that we are just moving from this age of secrecy to an age of enlightenment. In a lot of places, it has been like that anyway.

Q12 Chairman: Let me just tell you that the hounding of MPs in the playground is far in excess of anything you ever experienced.
Mr Clark: It was never a career I wanted to pursue.
Ms Toynbee: On the question of transparency, though, I am not quite sure why we would want to be extra transparent about the public sector without a little bit more transparency perhaps in the private sector as well. There should be a culture of people essentially expecting to know what other people earn, where they stand within their own organisation, where they stand within their own occupation. I think there has been, in recent years, much more secrecy than there used to be about people knowing roughly. All the polling evidence is that people miscalculate where they are on the earnings scale much more than they used to. Perhaps in the days when trade unions were more vocal, people understood more what other people earned. I think, for democratic reasons, that is important.

Q13 Mr Prentice: Most of us here earn about £64,000 a year. Do you feel able individually to tell us what you earn? I ask that question, Polly, because you said why just the public sector, why not the private sector. Should not our tax returns, everyone's tax returns, be put to the public domain? It happens in Sweden. People running for elective office in the United States disclose that information.
Ms Toynbee: I think it is a very good idea. I mean, it would be a huge culture shock at first.

Q14 Mr Prentice: It would.
Ms Toynbee: It would be like nudism, everybody taking their clothes off, but if everybody did it at once, the shock would last a year or two.

Q15 Mr Prentice: Just do not go there.
Ms Toynbee: I think it would be a very good idea. I do not mind saying what I earn, but I think it is a taboo that is quite dangerous at the moment. If you want to know what I earned: I just received my end of year thing from *The Guardian* and it said I earned £106,000.

Q16 Chairman: It is good to have the question but I am not going to press the answer—unless you are going to volunteer, Tony?
Professor Travers: "If only" I will say. I think the point you are making is a good one. This is a sort of taboo. What is interesting is we are discussing about making public and agreeing about making public some numbers which, in general in society, are a slightly awkward taboo. It is not a thing people discuss widely in public. That is why there is a sort of grating noise when you are discussing it.

Q17 Chairman: Yes. We talk rather readily about the public sector without perhaps stopping to think the public sector is a rather different beast than it was a generation or so ago. We are getting submissions from bodies that we think are in the public sector—and you mentioned university vice-chancellors—who tell us, "We are not, we are private organisations." Some describe their particular status, which means that they are in a special category. Of course the whole trend of policy has been to move in that direction, to create all kinds of disaggregated kinds of bodies. It is a much more variegated public sector now than it once was. Is not the implication of that that you will have much more variegation and, as it were, self-determination in the pay structures?
Mr Farrugia: Yes. Absolutely. I definitely accept the fact that in an enormous varied, as you say, public sector, with very different jobs, from a university vice-chancellor to the head of a police force, you are going to get very different needs, very different candidates and very different pay scales. I think you have touched on a point that we need more clear lines of where the public sector is. The man on the street has no idea where the public sector begins and ends, and the reason these stories build up so much steam is that people are shocked when they find out that these people are getting paid with taxpayers' money. That is the key.
Professor Travers: I agree with that, but it is even more complicated, I think. There are now, because of successive governments' policy, a significant number of companies that are, for want of a better word, "parastatal"; that is, they only exist because the public sector buys services from them. Answering the question of whether some of those companies are really in the private sector, when they get 100% of their work, let us say, from the public sector, is a very, very awkward one. Public-private partnerships have made this a very murky piece of territory indeed to say where the public sector ends and the private sector begins. If you start then setting general rules for which pay is and is not revealed, you will undoubtedly find a large piece of grey territory in which it is very clear that the TaxPayers' Alliance will have a lot of trouble deciding who to look at and who not.

Q18 Chairman: Are you talking about companies like Capita?
Professor Travers: Yes, companies of that kind, but in fact there are more complicated ones than that. If you look at, say, the companies that were in one case rebuilding the London Underground, the public-private partnership companies for that, they were created solely to do work which is 100% public

sector work and yet they are in the private sector. It is very complicated. This has had problems, of course, for public sector accounting which other committees have had to look at in the context of what is on and off balance sheet.
Mr Farrugia: It is very complicated, but if I may bring it back to the transparency issue, if the public sector led the way in having incredibly transparent pay, in terms of in their annual accounts, for instance, then hopefully they would set an example for the private sector and even these parastatal bodies would set an example that everyone else would follow.

Q19 Chairman: Does anyone else want to come in?
Ms Toynbee: On the question of comparing public and private pay, I think the TaxPayers' Alliance sometimes use an amalgamated figure that is very deceptive. If you add up all of the public sector workforce together and divide it by the number of people and you do the same for the whole of the private sector, the public sector comes out as very much better paid, and you think "Good heavens." until you realise that nearly all the low-value, low-pay jobs have been outsourced. The dinner ladies, the porters, the cleaners and all of those people are not any longer in the public sector technically, which makes these comparisons very difficult. Whereas the private sector, on average, has 8% professionals, the public sector is now very much more professionalised (because it has outsourced its unprofessional/ non professionals) and has something like 24% professionals. Those crude comparisons look very alarming to the public, but it is a very unfair way of averaging things out.
Chairman: Yes. We have been reading your spat with the TaxPayers' Alliance and enjoying it hugely. We are hoping it will continue because it will provide us with good information.

Q20 Julie Morgan: The Equality Bill is going to be introduced a week on Monday, the second reading, and that of course will ask for, at the first stage, voluntary pay audits. I think there is going to be more openness as a result of the Equality Bill. Obviously the purpose is to illustrate the gender pay gap that does exist, as we know, in many places. I wondered on this transparency issue whether you think that this will be a step forward.
Ms Toynbee: Definitely. It is a small step, but yes.

Q21 Mr Walker: I think that there does need to be something done in the public sector to curb pay at the very highest levels. To balance that, I recognise there are head teachers paid £120,000 who do a simply outstanding job. They have changed the prospects of children in a way that would have been almost unimaginable a decade ago. I think we need to temper the argument here. Do you regard the TaxPayers' Alliance as the sort of witch-finder general riding into the public sector and crucifying people and driving stakes through their hearts? Sometimes it does seem like that. Your rabid hostility to anybody working in the public sector seems odd.
Mr Farrugia: I think that is slightly unfair, in so much as I certainly hold no hostility towards particular people in the public sector. I think we are probably the only group who are pursuing this voraciously. I feel that perhaps there is room for more people to be doing so. At the moment we are the only people standing up, investigating this and putting it to the press and putting it to the people, and saying, "These are the facts. This is the data you can get from published accounts. You make up your own minds." I know it has been interpreted that we have this kind of blood-lust for the public sector but I think that is unfair.

Q22 Mr Walker: But it is not unfair. The danger of the TaxPayers' Alliance is that you are clearly a very studious, academic gentleman, but the way the TaxPayers' Alliance allows itself to be represented in the press is really as just a rent-a-quote organisation. If the boot needs to be put into the public sector, be it civil servants, Members of Parliament, anyone in the public pay, get the TaxPayers' Alliance to it and they will put the boot in. Does that ever concern you, that sometimes the TaxPayers' Alliance does allow itself to be portrayed as a rent-a-quote organisation as opposed to a serious, research-based think tank?
Mr Farrugia: It does not concern me because I work in the same office with the people who are providing the quotes to journalists and they are not doing that. Journalists come with stories for them and I strongly believe they are representing a true and honest opinion which I think quite a lot of people in the public hold as well.

Q23 Mr Walker: I notice your Chief Executive Matthew Elliott has worked in the public sector. He was a researcher to an MEP.
Mr Farrugia: He was.

Q24 Mr Walker: Paid by the taxpayer. How does he feel about Members of Parliament and MEPs paying researchers out of their staffing allowances? Because we get a lot of grief from the TaxPayers' Alliance. I think it was £125,000 last year I trousered, when, in reality, £103,000 of that was paid to my excellent staff. Surely Matthew Elliott knows that because he has been paid by the taxpayer out of a European parliamentary allowance.
Mr Farrugia: I am afraid I am not here to speak for Matthew Elliott. I have no idea where his particular feelings are on this issue. I only have mine.

Q25 Mr Walker: It is funny that his experience does not seem to colour his thinking. Anyway, moving on, Polly Toynbee, of *The Guardian*, I do not agree with much of what you believe in but I respect your right to believe in it, but what are your concerns about the public sector? You are the champion of the public sector but when you start having concerns about the public sector that sets alarm bells ringing with me. Where specifically do your concerns rest within public sector pay inflation? Is it in the sort of uber managerial class that has appeared over the past decade that seems to be extremely busy and working very hard the whole day through doing perhaps not much?

Ms Toynbee: I think it is not the sort of superheads turning around very difficult schools. As you have said, it was 387 earning over £150,000. I think that at that level there is a danger of them losing touch with what is ordinary any longer. I think it does cause public concern. I do not want the public sector to be brought into any kind of disrepute. I think perhaps the honours system had something to do with this. There used to be a system where you got honours for public sector because you were, on the whole, paid less than somebody doing as difficult a job. As David said, there is hardly a more difficult job than to be chief executive of a really complicated, large county or inner city area, where you are covering a vast array of quite different things, with quite different demands, where you go from child protection to schools to social care for the old to running your streets and your parks. Not many executives in the private sector, where they only have one target, which is their bottom line, have to deal with anything as complicated as that. I do not think that means that they should therefore be paid more, but I think they deserve more respect. Sometimes the respect comes from not perhaps being paid quite so much but from people recognising that they are public servants who want to do it—which is true of most of them. They are not in it for the money, they want to do it because it is an honourable thing to do. I think perhaps the honours system should recognise this and there should be rather fewer honours for bankers, fewer honours for people who earn monstrous sums of money—I cannot see why they get honours as well—and rather more honours for people doing public service, for being paid less for very hard jobs.

Mr Farrugia: I think Polly makes an interesting point there. If you take local government chief executives, if they have now chosen to pay themselves private sector wages, essentially, for their jobs, then they are going to lose that kind of respect because no-one is going to think they are doing it out of duty, they are going to think they are doing it, quite rightly, perhaps out of their own self-interest. I think that is a very important point: if we are going to have this duty, then people have to believe it and being paid a private sector chief executive wage does not tell people that is what is going on.

Ms Toynbee: Not all of them are. They are still paid a great deal less than chief executives in FTSE companies.

Q26 Mr Walker: There are some salaries that do make my eyes water. Is it British Waterways where four people are earning over £400,000 or something? That just seems remarkable.

Mr Farrugia: They would argue that they do a lot of mainstream commercial work and so consequently their salaries reflect the mainstream commercial business, but they are funded by the taxpayer. Yes, they make money from selling land along our lovely canals, but the majority of their funding comes from the taxpayer.

Q27 Mr Walker: I wish I had known about those types of jobs before I decided to become a Member of Parliament. Anyway, thank you very much.

Mr Clark: In the local authority chief executive world, they are not paid anything like their opposite numbers in the private sector, nor indeed some public sector jobs. You are right, people do not go in it for the money; on the other hand, I can report that there has been rather a good thing to come out of the TaxPayers' Alliance work—I never thought anything good would, but it did—and that is that we run a graduate scheme and the number of graduates thinking of local government as a career as a result of thinking you can earn decent money there, so that you do not have to go into banking or anywhere else, has really gone up. So every cloud has a silver lining, as far as SOLACE is concerned, on the subject of pay.

Q28 Chairman: I would like to hold on to an important point that Polly raised just then and Ben agreed with, because, if it is true, it has quite important implications. It is this idea that if public servants start earning these very large amounts of money, then it devalues the currency of public service. The way that people see them and see their organisations may change. If that is true, that really does have profound implications, does it not? Do you think it is true? Tony, do you think it is true?

Professor Travers: There are not that many of them in the stratospheric league. I agree there are some. I think the reason that some of them started to go upwards was because there has been significant pressure from governments of both parties, as it were, for the public sector to use more private sector expertise, and that has, at the margin, involved looking at the private sector to bring people in. You can see that headhunters, or whatever they are called, in doing that will have jollied up the pay a bit in order to try to tempt people in from the private sector. There have been some significant and highly paid people within the private sector, and it is all a complicated set of steps that have led to these big jumps in a small proportion of private sector pay. But, overwhelmingly, chief executives in public sector institutions are not paid those stratospheric sums. There is a small number. The Prime Minister as a benchmark is actually a good one, I think, and where they do get way above that level it will corrode and erode the way people look at public service because the figures do not make sense. I think Polly used that term "do not make sense".

Chairman: I represent a small district council area and the chief executive of the small district council earns twice what I do. Obviously people think that is wholly unfair and they want me to be paid more, but it causes quite a lot of comment of a negative kind locally, that this person running this small district earns that kind of money. I just sense that it does corrode the way that people perceive local government.

Q29 Mr Prentice: But why should he not—if it is a he—be paid twice what you are paid? That begs all sorts of questions. Exactly the same is true in Pendle, which is a small district council in Lancashire, where Steven Barnes, the Chief Executive, earned £125,770 in 2007–08. When people reflect on the salary that Mr Barnes gets, they think, "Well, over the years, he has lost responsibility for housing"—council housing has gone over to Housing Pendle—"he has lost responsibility for leisure services"—all leisure services, swimming pools and so on, have gone over to Pendle Leisure Trust—"all back-office functions in the local authority have gone over to the private sector Liberator, and yet I do not think his salary, over the 16 years that he has been Chief Executive, has dipped in any one year to take account of the reduction in his responsibilities." I am looking at you, Tony Travers.

Professor Travers: We are tottering again on the edge here of the ravine marked "Comparability Exercises." You will remember from the 1970s the efforts to undertake what were in the end chaotic comparability exercises between different kinds of jobs in the public sector and private sector to try to decide what would be fair public sector pay. Your point is well made. You could go on with that kind of comparison: If a district council chief executive is paid £125,000 and the chief executive of a very complex, inner city council is paid £175,000, is one of them paid too little and the other too much or are they both paid too much? I am saying I do not know the answer to that question.

Q30 Mr Prentice: Very eloquently you are saying you do not know.

Professor Travers: It is as complicated as saying that it is a comparability exercise where we are now trying, as it were, to compare different sorts of public sector jobs with each other and all of them with the private sector, and I do not think those exercises have ever been very successful.

Mr Clark: I would agree entirely.

Ms Toynbee: A little earlier Tony brought up one of the causes of this. I think it is about comparability, in a way, but in a very negative way. In the private sector, as we have chronicled in our book, you have headhunters called in by private companies and the directors sit around considering: "Are we an upper quartile company or a bottom quartile company?" and they all say, "We definitely want an upper quartile person with an upper quartile salary." The same thing is now happening in the public sector too. David knows about this. People are being headhunted from a very, very small group of people. They say, "We want someone who already has experience of running a very large county," and that is only going to be a small number of people. If you are having all these counties competing in a tiny pool, that is a self-inflating mechanism for pay. I think the role of headhunters in both private and state sector ought to be looked at in the course of your investigation.

Mr Clark: It is also the role of government. I am interested in what Gordon had to say. Presumably you would think that he might get some more if the Government gives him another unfunded mandate to deliver and that would be equitable. What is happening in a number of cases—and we have seen it—is that leaders of councils, often large shires, when they lose their chief exec, publicly say, "We only want somebody who has been the chief executive of a county council before and it must be an excellent rated county council." Then you look around and that is nine people, five of whom are nearing retirement. Once you do that, you are going to get spiralling wages. One of SOLACE's positions on this is that councillors are a little risk-averse. If you were in Lincolnshire, for example, they have a chief executive, an excellent chap called Tony McCardle. Prior to that he was Chief Executive of Wellingborough District Council. He is doing an excellent job and he is never quoted as on a big inflated salary—much to his disgust actually, but, nevertheless, he is not. If councillors realised that there is quite a lot of talent out there, in districts as well as in other areas, and were prepared to take bets a little more, it would not have the impact. I think it is one of the perverse effects of all this strange CAA-ing and CPA-ing and whatever else, where people get stars and all of a sudden you think, "Right, I have to have somebody who already has the stars," but there is not much evidence that that is true.

Q31 Chairman: That is interesting.

Mr Farrugia: We are often told that these executives such as SOLACE represents could walk out of their jobs and walk into excellent private sector jobs, and I have no doubt they could walk into excellently paid private sector jobs as consultants. But there are very few who have genuine private sector experience. I know Tony made a good point that in some quangos there have been people brought into the public sector who have inflated wages, but by and large we see career public servants who have never been tested in the private sector justifying their pay on the grounds that they could just leave and go and earn fantastic money elsewhere, and so they deserve this. That is a concern for us, because where is the proof of the pudding?

Q32 Chairman: We have business appointment rules in the Civil Service because private companies are queuing up to take former civil servants.

Mr Farrugia: I would like to see that in local government. I would like to see some local government chief executives and some large regional quango chief executives who are there to promote business, who genuinely have a business background and who can say, "I was earning £1 million and now I am being paid £100,000 to do this public service."

Professor Travers: I do not disagree with that, save I would like to add a footnote. The reason the comparability is so difficult is that it is very difficult to compare the jobs. Among the many things that are difficult to compare are the downside risks if things go wrong. I completely accept that in the private sector the downside risk of things going wrong is bankruptcy and that is a very bad thing for the companies concerned, but certainly in some parts of the public sector, the downside risk of things going wrong is total ruin. If things go wrong in some parts of the private sector, the risks to the executives concerned are very, very great indeed, both for them personally but for their long-term reputation. I am not saying you can price that but they are very difficult things to compare.

Q33 Mr Prentice: My Chief Executive—and I do not have a fixation about the Chief Executive, I just do not—was awarded, I see from the stuff produced by the TaxPayers' Alliance, a retention payment of £15,366. It gets back to the point you just made, David, about councillors being risk averse. They want to hold on to the person they know. Are these retention payments common place in local government?
Mr Clark: No. They occasionally appear when parliamentarians have decided to reorganise local government, because the danger that you have in reorganisation is that everybody jumps ship into the new, and the old one that is being closed down has nobody running it. There are times when they are used and it is usually around where there are major reorganisations and you do not want the new reorganised councils to steal all your staff. But they are not common place—you know, a handful.

Q34 Mr Burrowes: Is not the public sector out of step with the private sector in relation to, for example, salary increases? Should we not be taking a leaf out of Obama's book in having a pay freeze for White House staff? In terms of showing a lead, would it not be right for Gordon Brown to be insisting that in Number 10 they take a similar pay freeze, like the private sector is having to do, given the recession?
Mr Clark: I still hold to a belief that local authorities are individual sovereign bodies. Whitehall may do something if it wishes to do so itself, but I suspect that you did not take many orders from Number 10 when you were an Enfield councillor because that was not how you would have experienced this in a sovereign body. I do think—and certainly my organisation has already been talking about—"What should we be saying professionally?" I accept that this is a decision which definitely lies with elected members and elected councillors, but, professionally, we take the view that in a recession like this it is very hard to justify pay awards at all.

Q35 Mr Burrowes: But more particularly Number 10.
Mr Farrugia: Yes. I think you make a very good point. I hope Polly would agree that, when senior executives are discussing with frontline staff about cutting their pay, it would make much more sense to go into those conversations saying, "We are freezing our pay" or "We are cutting our pay. We are shouldering this pain with you." We have not seen evidence of that.
Ms Toynbee: I think that is true. You cannot underestimate the power of gesture, quite often, when you are in a national crisis. I think the higher top tax rate was in that category, in a way. It said, "We're all in this together. We share the pain fairly." I think that what Obama did in the White House was very sensible in that context, and I do not see why we should not have more of it here. In terms of public or private, it is important to remember that, according to England Data Services, the cycle is different in pay for public and private sector, and often public sector is countercyclical. In 2008 the private sector average pay increase was 3.8% and the public sector 2.7%. It will probably reverse itself this year and maybe next, but then when things pick up it will go the other way again, so you need to look at it over a reasonable span of time. I think gestures for top people is a good idea—I think you are right—but in terms of overall pay, I think it is important that ordinary people in the public sector do not fall too far behind and that you look at the different cycles.

Q36 Mr Burrowes: We have spoken about the particular examples in relation to town hall chiefs, so let us take the example of the Cabinet Secretary. Should he be paid more than the Prime Minister?
Mr Farrugia: I think he might be one of the cases where evidence could be put forward that he has an extraordinarily complex job with very particular responsibilities that mean he should be paid at least equal to, if not around or in the range of the Prime Minister, if not a little above. I do understand that he gets paid significantly more currently. Even at the TaxPayers' Alliance, although hard for some members to believe, there are certain people who are going to demand higher pay than the Prime Minister, but the Prime Minister is going to be a useful benchmark. Anyone over that should be considered extraordinarily well paid in the public sector and there must be extraordinarily good reason why they are being paid more than that.

Q37 Mr Burrowes: Polly, you have said that you feel there is something wrong with any public servant earning more than the Prime Minister. Is the Cabinet Secretary included in that?
Ms Toynbee: I do not quite see why he should not be. It seems to me odd, because, after all, you have come all the way up through the Civil Service, you have not come from somewhere else, so I find it odd.
Professor Travers: Being Prime Minister of the United Kingdom, because of the centralised nature of the state, is a very, very exercising job. It is a bit like being Mayor of England in some ways. You are almost an executive running everything, responsible for every bedpan in every hospital, and so on. I think that makes the argument for the Prime Minister being seen as some kind of a limit pretty powerful.

Q38 Chairman: As an extension of this, if we are tossing the idea of benchmarks and such like around, what about this idea that there should be some connection between the top earner in an organisation and the bottom earner, that there should be some kind of ratio that would bound the range of salaries? Does that make sense?
Ms Toynbee: It is a bill that has just been brought into the House of Lords by Lord Gavron and Lord Taverne and I think it is a very good idea. All they are suggesting—a very modest proposal—is that at the front of every company report, on the front page, it should say what the relationship is between the highest paid person in that company and the average of the bottom 10% of people working in that

company. It might be that we get some incredibly well paid cleaners shortly! Again it is transparency, making people think about that as a first step before you start to implement something. I think it should apply equally to public companies and to the public sector.

Q39 Chairman: Would that make sense in local government, to have an explicit ratio between the chief executive and the lowest paid worker?
Mr Clark: I suppose you could try it but I think we are back to that problem that Tony describes, which is the fiendish complexity of local government. Let us take Gordon's example of Steven in Pendle.

Q40 Mr Prentice: Oh, not again.
Mr Clark: Oh, yes. I mean, I like Steven, so—

Q41 Mr Prentice: He is not going to speak to me.
Mr Clark: No, I know—not after I tell him, anyway. If you look at what they are doing in partnership with Liberator, a lot of staff are now employed by Liberata—which is a good company and it seems to be doing a good job as far as I can see. Their Chief Executive, of course, earns significantly more than Steven, by a ratio of four, something like that. Where would you do the comparison? Would you do the comparison with the people who were working in that Liberata part or with the people who were working in the leisure part—all of which is held together in a partnership, as you know, which Steven and the leader chair? How you would do it is tricky. It sounds attractive and so we start looking at the fiendish complexity of all the people who actually now deliver public services, even in a relatively small place like Pendle.
Professor Travers: On the back of a mental envelope, if you were to compare, certainly in local government currently—and Ben may know the answer to this—in a sense the top pay compared with, say, the average pay, is going to be in a ratio of, I do not know, four, five, six to one. Typically 4:1, 5:1, 6:1. In some parts of the private sector the ratio would be very different. It would probably be much bigger. But, again, because of the comparability problem, I am not sure whether, when we knew that, it would tell us quite as much as you would hope. That is all I am saying.
Mr Farrugia: My concern would be that it would pull wages further up and significantly.
Professor Travers: It would pull them up.
Mr Farrugia: It would pull them up, because as has been implied, I think a lot of the lower paid workers in the councils have now been farmed off, and, as you implied, a lot of the services are gone where there would be lower paid workers. Of course there are lower paid workers in local government, but, increasingly, we see people creeping into that £50,000 plus. Increasing numbers. Every year, year on year, tens in every council are added on. That would be a fear we have.

Q42 Mr Prentice: I have just been reading Polly's book *Unjust Rewards.* You tell us that the tolerable ratio—the person on the most modest salary and the top earner—is 14:1 and if it goes above that then presumably it is intolerable. Then you quote Sir Terry Leahy at Tesco. He gets 400 times what the person in the checkout presumably would get and the boss at Punch Taverns, Giles Thornley—this really is eye-watering—gets 1,148 times the minimum wage. That is what you tell us in your book. I suppose my question is not to you but to Ben of the TaxPayers' Alliance: Do you think that is fair? Do you think that anything that happens at the private sector, even those kinds of ratios that I have just read out, is fair game?
Mr Farrugia: I think they are entirely to do with that particular company. I think they are their choice.

Q43 Mr Prentice: Their choice?
Mr Farrugia: It is their choice.

Q44 Mr Prentice: Their choice.
Mr Farrugia: They are a private sector operation.

Q45 Mr Prentice: Okay. You say in your evidence to us—and you are talking about the public sector—that managers enjoy "massive salaries". I would like you to tell me what you consider a "massive salary" today.
Mr Farrugia: I consider a massive salary for a manager to be anything over £100,000.

Q46 Mr Prentice: I see. But you do not have a view on "massive salaries" in the private sector?
Mr Farrugia: That is certainly a massive salary. Whatever Sir Terry Leahy gets paid is an enormous salary.

Q47 Mr Prentice: It is enormous.
Mr Farrugia: It is huge. It is enormous.

Q48 Mr Prentice: That is not something you would concern yourself about.
Mr Farrugia: It is set by Tesco. We pay for these public sector managers. You can choose not to shop at Tesco, if you so choose. Consequently Tesco will go bankrupt and Sir Terry Leahy will get paid nothing. We all have to pay tax and we all pay the public sector executives whether we choose to or not.

Q49 Mr Prentice: That is interesting, because we have a tax rate which is very flat indeed: top earners at 40 pence, which is going up if the present government is returned to 50 pence. If the Conservatives are returned at the next election, it will be going up to 45 pence. Just as an issue of fairness—fairness—do you think there should be a more progressive tax system in Britain, so that the Terry Leahys and the Sir Philip Greens and the rest of them who get stratospheric earnings, pay more into the exchequer?
Mr Farrugia: I think we have a very progressive tax system.
Mr Prentice: Okay.
Chairman: I do not want to get too wide on this. Gordon is leading us down avenues that we do not need to go down.
Mr Prentice: But it is interesting.

Q50 Chairman: Interesting. Always interesting. In the first discussion we had, Ben, I was slightly puzzled by your answer. I thought you consented to the leakage and contagion argument that we had right at the beginning of our discussion, and if you assent to that, which you did, then presumably you cannot say I am not concerned about what happens in the private sector, because if there is contagion presumably you want to attack the source of the contagion.
Mr Farrugia: If I understand, you are saying that stratospheric salaries in the private sector because of the contagion effect are going to have—

Q51 Chairman: Yes.
Mr Farrugia: I think you certainly have a point there, but my focus is the public sector. I do not comment and I do not research on the private sector. If those are definitions—and I am sure other people much more informed than I can comment on them—my concern is that people pay tax, they have to pay tax, they do not shop with government, they do not choose these services, and these are salaries being paid out of general taxation, and so, consequently, I can comment on their salaries. I cannot comment with any strength on private sector salaries.
Ms Toynbee: So far as public companies are concerned, of course, most of that money is taken out of the people's pension funds, because most money in the publicly quoted companies is people's pension funds. It does not come from nowhere or from choosing to shop there or not. It does come out of the companies' coffers.

Q52 Mr Walker: Sir Terry Leahy is a constituent of mine. There are not many pension funds complaining about Sir Terry Leahy's performance, because he has delivered a huge return for them since he has been at the helm of Tesco.
Chairman: I have to bring us back to the main business again and I am going to bring Ian in, if I may.

Q53 Mr Liddell-Grainger: Tony, we have gone around this issue for the last hour and a bit, but where do we go from here? We have to have curbs. Do you say to chief executives and councils, "Look, I am sorry, this is what we are going to have. We are going to band the whole thing"—in other words, one stars or two stars or whatever you want to use. We have to come up with a solution to this problem. We have to say somewhere along the line: Do you take chief executives on one side, do you take quango chiefs on another? Do you have banding for every type of organisation within the public sector, which means that you will be into that band regardless of how many people are in it—whether it is Pendle or, in my case, Somerset, which are two different sizes?
Professor Travers: In the short term, the spirit of the age will clamp quite a lot of this pay—not just the spirit of the age but in fact there is going to be—again outside this particular inquiry—probably ten years of public spending constraint from next year onwards, or the year after onwards, and that will act as a very effective brake on all sorts of things in the private sector, including almost certainly pay. There will be a trade-off between pay and the number of people employed for quite a long time. Personally, I am not in favour of centrally imposed bands on these things. I said earlier on I do believe in publicity so that people locally and nationally can see what people are paid and then create political pressure about those numbers if they wish to as the Taxpayers' Alliance does and others here do in different ways. Having centrally imposed bands on all of this is not the right way to go, different people should be paid differently. If you are chief executive of Birmingham you should be paid a different amount set in Birmingham compared with the Head of the Health Authority in Newcastle-upon-Tyne. These things ought to have much more local freedom, if anything, because more local freedom would actually create more local pressure of the kind that apparently the ex-chief executive's children met in the playground and that would create local pressure for sensible pay.

Q54 Mr Liddell-Grainger: But, would it? I am going to ask Ben this now. What Tony just said was leave the press to do all the work and people like yourselves to come up with the answers. I have just been trawling through this and there are about 200 pages.
Mr Farrugia: Yes, almost.

Q55 Mr Liddell-Grainger: Nobody locally is going to listen to the *Wolverhampton Wanderer* weekly paper and say, "Oh, that's what he's paid, we must change that". Is that not unrealistic?
Mr Farrugia: I hope not. That would be a very low opinion of democracy. I would hope that people are reading their local papers, are reading their national papers, are hearing how much their local government executives are getting paid. There is one thing we have not discussed which is the pressure on councillors. David implied that councillors are a bit fearful and they want to hold on to their executives. My hope would be that local people would put pressure in elections on their local councillors saying, "Listen, when you get in we want you to put a brake on these salaries". That only applies, of course, to those which are set by—

Q56 Mr Liddell-Grainger: Your boss worked for an MEP and I think he would tell you that does not actually happen in reality.
Mr Farrugia: That would certainly be my hope and the reason why we do the *Town Hall Rich List* and the *Public Sector Rich List* is to enable that. With quangos you have a separate issue because these people's pay are not—

Q57 Mr Liddell-Grainger: Can I give an example, and David will probably get involved in this one. In Somerset we have had an unmitigated disaster with a deal with IBM, half a billion quid, it is an absolute fiasco. It was done under secrecy and nobody could find out what was going on. Somerset will not even come back to me with who the portfolio holders are. That is not getting into the public domain because

the public cannot find out. That argument does not work because we do not know. I do not know as an elected representative, one of five MPs in Somerset.
Mr Farrugia: I think Tony and I would both support the steps taken by all three parties to say that they must do it. I should not have to send a request to Somerset asking to release the information, it should be there every year on their website for everybody to see.

Q58 Mr Liddell-Grainger: I will let you know the figures for those, incidentally. I do know them, so I will let you know.
Mr Farrugia: Thank you.

Q59 Mr Liddell-Grainger: It comes back to the argument that we cannot get at the truth anyway. My chief executive is paid more than 100,000, he will not release the information and the councillors are saying, "Oh no, we don't really want to do this" because it is a political football. So you are not going to get any further, are you, because Tony's and your argument of "Just let the press do it" is not going to wash.
Mr Travers: We have all agreed, I think, that it would be indefensible for the top pay not to be in the public sector. I suspect, without knowing anything about the deal that you are referring to—

Q60 Mr Liddell-Grainger: That was just an example.
Mr Travers: —that will have been enmeshed in complications to do with so-called commercial confidentiality. That is about a contract. In a sense, problems of commercial confidentiality, the public knowing things about big contracts that are being written, are somewhat different from the questions of what people are paid where I think we have all broadly agreed that publicity would be good and then the media would be able to—

Q61 Mr Liddell-Grainger: Let us take another example, the Learning and Skills Council.
Mr Farrugia: Yes.

Q62 Mr Liddell-Grainger: Hopeless.
Mr Farrugia: A large failing quango.

Q63 Mr Liddell-Grainger: Farcical. That has not been changed by any public opinion, that is Government that has said, "We're going to split them into three different quangos".
Mr Farrugia: Yes.

Q64 Mr Liddell-Grainger: We have gone no further forward.
Mr Farrugia: Absolutely. If next year it emerges that the chief exec who recently resigned got a million pounds in pay-off, which is not out of the realms of possibility, then hopefully the Taxpayers' Alliance will put that out there and condemnation will fall down upon them because that is not right. That is our concern. If I could add something to the transparency argument, maybe in public sector executive contracts they have to be firmed up so we do not get these enormous payouts for people who have failed and who are proven to have failed.

Q65 Mr Prentice: That is going to be covered.
Mr Travers: At the risk of being rude to my hosts, is it not a fact that as the Learning and Skills Council is a national quango should not the ministers who appoint such quangocrats and committees of the House hold it to account. It is a national organisation, so if there is a failure I would have thought it is in the holding of that particular body to account where the problem lies.

Q66 Mr Prentice: Mark Haysom, who was responsible for those terrible cock-ups with the educational maintenance allowance, students not getting their £30 a week and so on, has gone. I do not know if he has gone with a huge pay-off, I suspect he has not because there were two significant cock-ups involving the Learning and Skills Council and I would be astonished if he walked away with a million.
Mr Farrugia: So would I.

Q67 Mr Prentice: Good.
Mr Farrugia: But it could happen.
Mr Prentice: The other thing I would say to Ian is that the Government is acting on this.

Q68 Mr Liddell-Grainger: They are going to full disclosure, which is not before time, but at the end of the day, and this is why I came back to you on the banding, now we have an opportunity to do it because we know exactly what they are getting paid, their bonuses, et cetera. Quangos are just getting out of control, they are everywhere, they pervade our lives, they are running parts of district councils, doing all sorts of things such as the Foundation for Swimming Pools. Surely we must be able to sort this out in this way, that you know if you go in there this is roughly what you are going to get instead of having a free-for-all. You talked about the star system, only nine people on a four star council. That has got to be a better way, has it not?
Mr Clark: I think what you describe is something quite different. I think it is fiendishly difficult for a local person to work out who is running what, but that has been a construct of many years of different legislation which has set up elaborate networks, partnerships, boards and other issues. Obviously I was not quite a councillor when the London County Council ran health in London, but if you look at the way local tax-paid-for services have been splintered into a whole range of agencies, the transparency of trying to get that sorted for an individual is very difficult. Even in a wonderfully run city like York, if you were to ask a citizen, "Who is responsible for this? Is it me as the chief executive or another agency?" it is very difficult to know. I do have to say I think the proliferation of tax-paid-for bodies would probably have been much better served had democratically elected councils taken on some of those duties and set up just another stand-alone agency.

Ms Toynbee: I think it has been a consequence of 30 years of governments not wanting to be seen to grow the state and yet the state has taken on more functions so it outsources everything, it creates quangos. It outsources things either to private companies or to quangos so that it can claim it has kept the state itself at the centre within a reasonable number of people. Very often they will say, "We have cut X number of civil servants" when actually they have put them somewhere else, or they have put the function somewhere else. It is part of the "shrink the state" ideology that has created something that in the end really is not accountable in the way that it ought to be.

Mr Liddell-Grainger: Is not David's argument that 50 years ago the burghers of York would have run everything, top to bottom, they would have run the lot, but now there are so many quangos, foundations, trusts, every other thing which has grown out of this sort of government centralisation, as you have rightly said, that is where we have gone wrong? Do we need to go back to saying we will give elected councils, such as York, the power to just get on with it and run it top to bottom, instead of going to unitaries and all this, just run the thing as local burghers?

Chairman: I do not want to get away from our mainstream business. These are all interesting questions but they do take us into territory which is not ultimately ours, if you do not mind me saying so.

Q69 Mr Liddell-Grainger: I was just trying to get the pay structures and pay scales.

Mr Travers: Everything other than local government is to some degree national government. If they are appointed bodies, non-departmental public bodies of various kinds, they all have their route back into a minister in the Government and it seems to me that the Government could do that for its own quangos if it wanted to now, but they do not. I think that is because, in a sense, it has been seen that different quangos have different functions and are different from place to place; a big health authority chief in one place is different from the same job somewhere else. Why do I feel national banding and a national equivalent banding quango to do it all might make it worse even than it is, because there would have to be a quango to do it remember.

Q70 Chairman: Something like the Senior Salaries Review Body, which obviously governs a range of public service pay, you do not think any idea of extending or inventing a body that would seek to do that over a wider canvas would make any sense?

Mr Travers: I think the Senior Salaries Review Body in the work that it does to try to unravel, as I understand it, what comparable pay is in other parts of the public sector or for equivalent jobs sometimes overseas when a new job is invented within the public sector, there may be some benefit in pushing that information out and having a debate about it. I am not sure it would always answer the question what this particular chief officer or senior officer should be paid, because we have tended to think only of the top officers but, of course, for every one of them there are several beneath, and trying to set all their pay centrally does sound like a complicated quango all of itself.

Q71 Mr Prentice: On this point, the top paid person in the public sector is the Chief Executive of Network Rail and, according to the Taxpayers' Alliance list, he gets £1,244,000 a year. When I asked ministers in the Department for Transport whether they are consulted in any way, shape or form on the salary and bonuses of board members in Network Rail I was told it was not a matter for them, not a matter for the Government, it is a matter for the company's independent remuneration committee. Is not the question this: who sits on these remuneration committees, not just for Network Rail but for Royal Mail, Channel 4, Nuclear Fuels, the Financial Services Authority and so on and so forth? If the Government really wanted to influence salaries and bonuses they could suggest people like Ben Farrugia to sit on the remuneration committees of these public bodies.

Mr Travers: Without going down the complicated route of Network Rail, I think as a not-for-dividend company it is something really complicated. All the systems you have described are ones that the Government has to some degree assented to. Even if they say, "It's not for us, it's for this body to make these decisions", the systems are all ones that Government has created. Network Rail is particularly so, a fascinating construct. I do not think that the Government can get out from under saying that at some level it is responsible if not for the precise pay level then certainly for the arrangements that lie behind the way the decision is made. Of course, it would be possible for another government to say, "We will set all these salaries nationally". You will know better than me the history of the Morrisonian public corporation and the effort to distance these decisions from Government. That leads us to a debate about whether or not Government should directly run these things or whether they should be done at arm's length, which is a separate debate again.

Q72 Chairman: Gordon's question was the broader question of who does the setting. The one sure fact in this discussion is that these top public sector salaries have gone up considerably in recent years. That is the one sure fact, so the question who is doing the setting that is producing that consequence is worth exploring. Who sits on these remuneration bodies in these different organisations?

Mr Farrugia: Board members.

Q73 Chairman: Should somebody else sit on them who brings a public interest perspective to it, as we do with appointments to quangos now, we have independent people who sit in on the appointments so you cannot have crude patronage? Why could you not have independent appointees who sit on the remuneration committees for all these public bodies?

Mr Farrugia: I think it is a very good point. I am not looking for a job on the independent remuneration panel of the Royal Mail or anything. They are vested

interests by and large. I have looked at them closely and by and large they are board members who are then appointed to sit on the remuneration panel voting their and their chief executive's pay, which does not make any sense at all. Often there are non-executive board members as well, but increasingly they are getting paid as well now, and handsomely. I completely agree that there is a significant problem and that is a problem that could be addressed, maybe not with law but, as Tony says, by ministerial action to say, "You must put more independent people on these boards".
Ms Toynbee: They are doing this because they have been told to mimic the private sector and make themselves look as convincingly like an ordinary private company as possible, so they do exactly what private companies do, though slightly less so.
Mr Farrugia: That is possibly very true, but no reason to do it. Maybe that is a reason not to do it.

Q74 Chairman: David, how would that work in local government because it is sort of in-house, is it not?
Mr Clark: It is completely in-house. In local government we do not have these sorts of committees, except for elected members where certainly in most cases there are independent people now who chair committees that set the earnings of elected members. By and large the wages paid for chief executives have not gone up massively actually. There are a few at the top that people often talk about, but the average district is still earning less than 100,000 as a chief exec. For me, every time I have been involved in anything to do with this it is councillors and it is usually all-party saying, "This is what we want", they seek advice, and you can seek advice from my organisation but equally from Hay and various other people, about what the market is and you can decide how to go. There is one north-east authority which wanted to go for a chief exec but they were advised they would be going at exactly the same time as all the new unitaries so they simply put in an interim for a while, went later and actually paid less because the councillors had thought it through and did their job properly because they were not going to go out when everybody else was going out which would have an inflationary effect. My view is that the democratically elected member is actually best-placed to do it and by and large seems to do a good job.

Q75 Kelvin Hopkins: If I can go back to when Tony was talking about what happens in the private sector when things go wrong—bankruptcy—and what happens in the public sector when a manager gets things wrong. If I can contrast perhaps Sir Fred Goodwin, bankrupt banker, who should be down at the Jobcentre getting his Jobseeker's Allowance, but is actually on £700,000 a year for a monumental failure that has cost the taxpayer many billions. That is the price of failure in the private sector. In the public sector, almost at the same time, we had the woman who was Head of Children's Services of Haringey, at the time of the Baby P scandal. She has been humiliated, her career is in tatters, her reputation has gone and she is not getting £700,000 a year. I am not saying she should but, on the other hand, there is a contrast. I somehow think life is now less painful for Sir Fred Goodwin with his billions of pounds cost the taxpayer than it is for the Head of Children's Services at Haringey. Indeed, that is the pattern, is it not, in the private sector, that people do not suffer in fact?
Mr Farrugia: I actually think that you could find examples in both. Off the top of my head I have a few examples of public sector executives who have left an organisation for gross incompetence almost and then walked into another even better paid job, and then again, and then again, and then again, and their career goes from strength to strength almost on the grounds of being fired for being incompetent, which does not make any sense, they are not humiliated and they are getting paid very handsomely for it.

Q76 Kelvin Hopkins: Is this not precisely what Polly said, that in some areas the public sector is trying to ape the private sector? We have seen a hospital chief executive who was sacked some years ago but finished up with a higher paid job in another hospital.
Mr Farrugia: Absolutely. I think they are apeing the private sector.

Q77 Kelvin Hopkins: So they are apeing the private sector, because that is what happens, you look after your mates.
Mr Clark: I think your phrase was "fired for nearly gross incompetence". I think gross incompetence is actually like pregnancy, you either are or you are not, you cannot be nearly. Let us just look at some of the people who have been fired before we get carried away. In a number of cases they have been fired for pure politics. Let us go back to Lincolnshire pre-Tony McArdle when Mr Speechley was the leader and forced out a chief executive who then got a huge pay-off, and why was he forced out, he was forced out because he was the one who called in the police who eventually put Mr Speechley in jail. He then returned to the chamber with a tag! In those circumstances the chief exec got a big pay-off for being sacked for doing the job, so it may be that somebody is nearly grossly incompetent but in a lot of cases they get the push for doing the things that you would want them to do.

Q78 Kelvin Hopkins: There was another example of precisely that in London some years ago where exposing corruption cost a public servant his reputation, job and everything. I want to go on to a broader point relating to this. Gershon talked about there being a fourth dimension in public sector employment to the three-dimensional role of the private sector. I would have said one dimension, perhaps you are just making a profit, but in the public sector there is also often a legal duty, a duty of care, a public service ethos which involves caring about what actually happens to the people you govern, children in care and so on. People die because of lack of care. In the private sector it is primarily about profit and, therefore, you do not have that dimension. I think there is a difference in that the private sector is paid much more than the public sector. Is it not changing the nature of the public sector and diminishing those important values by making them behave more and more like the private sector?

Ms Toynbee: I think that the role of the public sector in setting moral standards is very important because if we add up the 387 people who earn over £150,000 it is peanuts in terms of total spending by the state, we are talking about very small sums of money overall. If you were to set a benchmark with nobody earning more than X you would not save all that much money. The reason it seems to be worrying you is not so much the actual pennies saved but the message that it sends and the ethos, as you say. It seems to me that in the course of your inquiry you need to slightly widen it and say why do pay differentials matter, what is out of control, why does it matter when things get so far from top to bottom. I would like to suggest that perhaps you call Richard Wilkinson, author of a book that is just out called *The Spirit Level*, who has done terrific research across the world about the countries that are most equal in terms of their earnings and their outcomes in terms of the economy, happiness, successful societies. He is an epidemiologist. It is very, very convincing evidence. It shows that countries that really do not allow the disparities to get out of hand and have very good public services are better through and through. It seems to me that there is something in the core of that that you are reaching for here that is not just about efficiency of the public sector but the message the public sector sends out.

Q79 Kelvin Hopkins: Within the last week I have spoken to a number of people in the health sector—I will not go into detail—and clearly some of the very senior people regard their good managers as the ones who have a good financial performance, not the ones who are actually concerned about the care of their patients. Sometimes that is exposed, like Stafford Hospital, but by and large the pressure is on financial performance of Primary Care Trusts and hospital trusts and that is how they are judged. As you say, Polly, is this not diminishing our public service and making it poorer?

Ms Toynbee: Yes.

Mr Clark: It is also an inevitable consequence of policy, is it not? If you take the local government context, you had Terminator 1, which was the Thatcher years which were essentially political, seeing local government as a political enemy and doing something about it, the building over the water, but in the current climate of Mr Blair and Mr Brown what you have actually got is Terminator 2, the rise of the management consultant, where there is a belief that business techniques and management consultancies can actually make everything better. In one or two cases it can but, you are right, this idea that you can measure everything and everybody's financial performance and that produces the best home help to go out and visit my dad is actually just plain daft.

Q80 Chairman: If we can now talk in shorthand because we have been going for a long time and I have got to bring it to a conclusion. Surely we accept the idea that someone who genuinely makes an organisation better should probably be paid more than someone who does not, and certainly more than someone who lets the organisation get worse?

Mr Clark: Yes.

Q81 Chairman: Is not one of the problems at the moment that that does not seem to happen? We can point to organisations which are not good where people get paid a lot of money, even go downhill and get paid a lot of money. There is no clear link between actually what people are doing in organisations and the amount of remuneration they are getting. Is that not a real issue for us?

Mr Travers: You are right, of course, but you can see the world you open up by adopting the idea that people who are really good get more and those who are not so good get less creates the very world in which the top will indeed escalate. I am not disagreeing with you, you can see there is a choice between a sort of flat rate for all, a banding system or something, which would be fair at some level and would allow public service ethos people to deliver good services because they want to do it and they are not doing it all for the money, but if you get into a world of rewarding the good and penalising the bad you will create a range which will have a top and we are back to where we started.

Q82 Chairman: If you say to someone, "You're coming here, we're a no-star organisation, you make this a four star organisation and we'll give you more money", that is reasonable, is it not?

Ms Toynbee: The academic evidence on performance-related pay is that it really is a chimera, it becomes very quickly box-ticking and hitting certain targets and does not produce better overall results. There is no academic evidence that it does, and yet it has been adopted almost wholesale by the Government, by management consultants, people who have just assumed that performance-related pay must produce performance. There is not any academic evidence to back that up.

Q83 Mr Prentice: In your *Spirit Level* example, the people running complex organisations in, let us say, Finland or Sweden would be trying as hard as people in this country to make sure the organisations they were running were successful presumably.

Ms Toynbee: I think the point is when people want to run the top of an organisation, whether it is a big hospital, a big local authority or a big company, they are people who are terrifically driven anyway to be the top and to be the best and that driving force of staying top dog in your organisation, public or private, is really what motivates people much more than the money; the money is often a question of the Silverback saying who has got the most beans. The money itself is not as important as the relative status of what you do, it is only one indicator of status, and one should not imagine that money is the only indicator of status.

Q84 Mr Walker: Just on that point on performance-related pay. I am not an expert on performance-related pay but somebody who came in on a zero star council and turned it into a four star council would increase their market value, so if that council wanted to retain that person they would have to match what his or her market value was on the open market. You do not necessarily have to have performance-related pay for someone to advance their earning potential. That is more of a statement than a question.
Ms Toynbee: Would you want them then to be poached by somebody else, another council that would push their pay up more, and when they had been there for a while another council would poach them?

Q85 Mr Walker: You would have to take that decision.
Ms Toynbee: That would be an escalator.

Q86 Mr Walker: You would have to make the commercial decision as the council, "Do we want to keep this person because it's work in progress or have they now achieved the improvement we're looking for so we can have more of a managerial type person at the top and this person can go on?"
Ms Toynbee: You will not know that person as being the one who has been most responsible for it, there will be a whole range of people and reasons why certain public organisations rise and fall. It is not always either the praise or blame of the guy at the top.
Mr Walker: You and I both know, and I think we agreed, that in certain secondary schools the quality of the headteacher makes all the difference, and that is something we have woken up to rather late in the day.

Q87 Julie Morgan: I was surprised, David, when you said that chief executives' pay had not actually gone up that much. Could you expand on that? I have got the example of Cardiff, where I am one of four MPs there.
Mr Clark: I know you are, and a former councillor.

Q88 Julie Morgan: Obviously the Cardiff Council Chief Executive's pay has gone up quite a lot, I think about 30,000 over two years. Cardiff is the sort of city that is very diverse and it needs somebody good at the top, so I am not criticising him in any way, but what comments have you got on that?
Mr Clark: By and large district councils have not felt this pull, although there are some that have. Unitary cities such as your own have seen a greater increase but, in fact, the average wages of chief executives in Wales still lag behind the English ones quite considerably. I suspect what is happening in a number of places, particularly a capital city such as that, is that somebody has taken a view that they do want to retain, in this instance it is Byron Davies, is it not? If you look at the pay settlement, which is what I am indicating, of 2% and 2.5% last year, the amounts going up have not been as great for chief executives. What has happened though is in a number of fairly high profile places councils have decided to do what Charles Walker described and have said, "We think we're in a hole. We want somebody and we're going to try and buy the best" and that has forced up a percentage. We reckon somewhere in the order of 20% of posts have had quite large increases in the last two or three years and in others not so much. It is slightly complicated, of course, because if you went to Cornwall, Cornwall has high wage inflation for its county but it is now a unitary county and its six other chief executives are no longer in post because those districts have been abolished. When you start unpacking all those sorts of things, overall it has not gone up that much.

Q89 Mr Burrowes: Where is the trigger for this public scrutiny and determination of pay levels? Is it taxpayers' money? Should there be a threshold of how much public money is going into an organisation? Do you then involve universities and other charities, indeed banks now and PFI-led companies? How far do you spread the net?
Mr Farrugia: Network Rail is a good example of what Tony mentioned of these very grey area bodies where we underwrite all the debt for it but, for instance, there is almost no Government oversight of Network Rail.

Q90 Mr Burrowes: You criticise it but what would you specifically recommend? You can publish a report about the pay, but in terms of solutions where would you say this should trigger off a particular mechanism or we really should know how to scrutinise it?
Mr Farrugia: I certainly feel that in terms of Network Rail's failures, and everyone says consistently every year they have some quite public failures in terms of engineering and so on, people would feel the chief executive and the executives should maybe carry the can for some of that, although admittedly it is probably not their personal responsibility.
Mr Burrowes: There may be some successful ones as well.

Q91 Kelvin Hopkins: It now costs five times more to lay a mile of railway track under Network Rail than it did under BR, four times more to do maintenance, the quality of work is less and the senior staff are paid much more. Should you not be much more worried about that than you are about chasing chief executives who have got the responsibility of children's services, education or whatever?
Mr Farrugia: Can we not chase them all? Can we not focus on them all?

Q92 Kelvin Hopkins: I am in favour of chasing them, but let us look at where public cost is: the banks, Network Rail.
Mr Farrugia: Absolutely.

Q93 Mr Burrowes: What is the trigger? We have looked at failure but let us look at success.

Ms Toynbee: What we suggest quite modestly in our book is that the Low Pay Commission should become the Pay Commission and it should suggest guidelines and benchmarks. Nothing to be enforced, because you can start that way by saying, "We think for this sector or that sector a reasonable disparity between the top and bottom should be in this range". Then it gives people, whether they are people investigating the public sector or whether they are shareholders in the private sector, something to get hold of and say, "Look, you've exceeded the recommendation by this much, you must give us a reason why there is something very special in your case". I think you could begin with something advisory like that that allows those who have to hold people to account, whether shareholders or councillors or whoever it might be, to say, "This is what comparability should be, not what the head-hunters say".

Q94 Chairman: This would cover both the private and public sectors?
Ms Toynbee: Yes, I think so.

Q95 Chairman: Tony, would that be acceptable or would it lead you into the problems that you were describing earlier on?
Mr Travers: To answer the question directly, and this is not to imply it was not a good answer, if we are looking for a post-modern way of trying to work out what is in the public sector and what is in the private sector, to answer the question does this organisation have its roots in an Act of Parliament might give you a clue as to where one ended and the other began, for want of any better way of doing it. I think the idea of flexibility is a good one in how any such agency of the kind that Polly has outlined or any other approached what was in the public sector and the private sector because it will not change, but there are private companies these days that have their roots in an Act of Parliament, whereas Tesco clearly does not.

Q96 Chairman: I think the banks probably do.
Mr Travers: They would have changed status latterly, would they not, Chairman?

Q97 Mr Prentice: Polly, I have been very diligent in reading your book, I have to say, because you tell us on page 52, "A High Pay Commission might curb excesses if it were to set benchmarks for top pay". If I were Sir Philip Green or one of these private equity people I would say, "Polly Toynbee, dream on". Philip Green paid himself £1.3 billion, handed the money over to his wife who lives in Monaco so he could not pay taxes, and he was knighted!
Ms Toynbee: You in Parliament can do something about that.

Q98 Mr Prentice: It just sounds a bit hinky, the High Pay Commission, because this is advisory and I keep telling people we live in a big, nasty capitalist world where the people who make the real big money are just going to laugh.
Ms Toynbee: I hope you are going to be doing something about Monaco anyway and HMRC is now going to be more vigorous about pursuing people.
Chairman: And we are taking honours away, so we are on the case for you.
Mr Walker: I do not agree with that, except in Fred the Shred's case.

Q99 Chairman: It is pretty clear, is it not, that those people who are directly, as it were, comparable with the private sector have to be treated in a rather different way from people who are not. If you are a finance director or an IT director, of even if you are the Director-General of the BBC and you are existing in an environment where you instantly are comparable and can change your skills readily with a major private sector player, is not the market there different from markets in other bits of the public sector?
Ms Toynbee: I think the BBC have got it wrong, they misperceive things. There are a lot of excellent people who would like to be Director-General of the BBC and, therefore, to have to compare themselves with a now collapsed market in television has been a big blunder in terms of the respect that the BBC is held in and it is regrettable.

Q100 Chairman: Presumably things like IT directors, finance directors, are interchangeable between public and private sectors, are they not, and you have to pay the rate for the job?
Mr Farrugia: Are they? Are they genuinely interchangeable? A lot of them will be.
Mr Clark: You are certainly getting finance directors in IT. If you were a London borough at the moment you would be rather pleased with the recession because you get an awful lot of people who used to work in financial services applying for those sorts of jobs. When Canary Wharf does very well a lot of people leave local government. Yes, you do see that.
Mr Farrugia: Is the job directly comparable? Your funding is going to be the same, the risks to your own position are smaller. Surely all these things must play into consideration as well.

Q101 Chairman: I think it is probably a more complex equation than you suggest. Is there anything you would like to say to us in terms of what we might do? You have said many things to us already but is there anything else you might want to say to us that you have not had a chance to say before we end?
Mr Travers: Very briefly, and Polly referred to this, the issue of public sector pay is tangled with other things that you will not want to enquire into this time, such as the honours system, such as public sector pensions, so it cannot be viewed entirely freestanding of these separate issues. Indeed, in a recession the comparison between what is going on in the private sector and the public sector and perceptions of that, that is obvious. The honours system and pensions are both linked in with the question of basic pay.

Chairman: A good reminder. We wanted a session that would get the juices of the Committee going and it has absolutely done that, it could not have been better. We are extremely grateful to you for all of that and we shall feed off what you have been telling us as we do further inquiries into this area. We now have to go and talk about our own expenses! Thank you very much indeed.

Thursday 21 May 2009

Members present

Dr Tony Wright, in the Chair

Paul Flynn
David Heyes
Kelvin Hopkins
Julie Morgan
Mr Gordon Prentice

Witnesses: **Mr Peter Boreham**, Head of UK Executive Remuneration, Hay Group, **Mr David Evans**, Head of Pay and Labour Market Services, Capita Survey and Research Unit, **Mr Christopher Johnson**, UK Human Capital Leader, Mercer (formerly of the Cabinet Office) and **Mr Hamish Davidson**, recruitment consultant, gave evidence.

Q102 Chairman: We are very delighted to welcome this morning Peter Boreham, who is Head of UK Executive Remuneration at the Hay Group, Hamish Davidson, who is a recruitment consultant of long pedigree, David Evans, Head of the Pay and Labour Market Services, Capital Survey and Research Unit, and Christopher Johnson, UK Human Capital Leader at Mercer. The reason we have assembled you together is because you know everything there is to know about executive pay in both the public and private sector. As you know, we have asked you here because we are looking at the issue of top pay in the public sector and, because you know all about it, as you are in the business of finding people for appointments and advising on pay levels, we thought you were good people to bring in. Could I start with a couple of questions to kick us off? Do you think there is an issue here? We have started doing this because it has been said that there is an issue about what is happening to top pay in the public sector. Are we right to think that there is an issue there that needs investigating or not?
Mr Johnson: The straight answer is, yes, there is an issue, and the issue for me has got two parts to it. The first part of it is that it seems, in terms of the public and political debate about executive pay in the public sector, there is not a consensus about what it should look like, so there is a lot of pressure claiming that public servants are paid too much, and yet you can argue, which is my second point, that there is insufficient money for executive pay for the public sector to recruit and retain the talent it needs to deliver on what I would argue is actually a very challenging task, which is in a period of pressure on public expenditure, pressure to deliver high quality services to citizens and to satisfy the taxpayer about value for money, good leadership and management is going to be crucial. In summary, I think there is insufficient consensus publicly and politically about the nature of public pay in the public sector and, secondly, I think there is a real challenge that public sector organisations are facing, which is securing and retaining the calibre of talent they need to deliver on the expectations that are being placed upon them.

Q103 Chairman: Thank you for that, but I am not sure from that whether you are telling us, because of this need to go out and get the very best talent in this market place, we should be paying people more. Is that the conclusion?
Mr Johnson: There is an interesting conundrum here. It is possible to get really good people to join the public sector. The Civil Service, which is one part of the public sector that tends to be more open at senior levels, has done very well securing talent coming in and much of the time the private sector has been willing to look at the opportunity in the round, quite often taking a significant reduction in earnings, but seeing a very attractive role at the heart of doing something important for the country and balancing those things together and saying, "Yes, I would like to come and play a part." So there are people that it is possible to recruit, but two challenges flow from the back of it. One is that I do not think I can see consistently the ability of the public sector to attract great talent, and, secondly the pay levels that you need to put on the table to attract people in are higher than the pay levels of the people that are already in the public sector and there is a very significant internal relativity pressure which is, I think, becoming quite a serious problem.

Q104 Chairman: Is it possible to say, in general terms, whether top pay in the public sector is too high or too low?
Mr Johnson: I think it is, in general terms, too low, because in general terms we are not able to secure the talent into the public sector.

Q105 Chairman: That is a novel contribution to our deliberations. Can I hear from the others on that?
Mr Boreham: I think from our perspective at Hay Group, we are concerned at the way that pay has grown quite rapidly at the top roles in the public sector, not because the growth itself is wrong, because I think we share some of Chris's points about attracting top talent, but the growth has all been in the form of fixed guaranteed remuneration. I think we would be happier if a greater proportion of remuneration was linked to the value that those organisations were delivering to their users and to the broader public.

Q106 Chairman: We will come back to that, I am sure. Hamish, do you want to come in?
Mr Davidson: I would agree exactly with that point. Right across the piece, to be honest, I think you have to take note that there are really three categories of post that we might be talking about here. Certainly in terms of the ones you were looking at yourselves,

there will be the non-executive chair type roles, there will be roles for agencies and bodies that are dealing fundamentally with organisations in the private sector, for example the FSA, where you need to compete for a particular kind of candidate, and then the rest, and I think the rest of those posts, in terms of how the salaries are moving, have been fundamentally influenced in recent years by the movement on pay and inflation in local government.
Mr Evans: I think there are differences across the public sector. I think there is a danger in looking at the public sector as a whole. I tend to cover the NHS. I think if we looked at different parts of the public sector, we would find different pay levels. I think there is also the issue of who you compare yourselves to in terms of the private sector in establishing some of the proper benchmarks.

Q107 Chairman: There is work to do to explore as well whether we ought to try and get some more coherence into the public sector, or at least coherent principles into the public sector, but we will come to that later. Can I ask one further question before I hand over to colleagues? You are a collection of, I think you call yourselves, recruitment consultants. You do not. Perhaps you would tell us what you call yourselves.
Mr Boreham: We have one recruitment consultant.

Q108 Chairman: I thought we had the head-hunters and the recruitment consultants, or remuneration consultants. Is that right?
Mr Boreham: The three of us are involved in advising remuneration committees and organisations on how to pay their people.

Q109 Chairman: Perhaps you would just tell us what you actually do?
Mr Boreham: Let us imagine we are doing a project for a foundation trust hospital. The remuneration committee of the board would approach us and would ask us to help it. We would help that remuneration committee to develop their pay strategy: where in the market is it pitching its pay, who is it comparing itself to, where does it want to be positioned? We will then produce some market data looking at how they are doing against that strategy, make recommendations about salaries, whether or not they should be looking for variable compensation and, if so, how would that be designed. That would be a fairly typical project for us.
Mr Evans: We undertake a salary survey of NHS trusts in England. Something like 66 trusts take part in that survey, so we collect data in terms of what they are paying in terms of basic salary, bonus, perhaps car benefits, other conditions of service, and we would use that, as Peter said, to share that with the trust in terms of establishing a benchmark. If they were a major city teaching trust we would try and suggest that they also benchmark themselves with other like trusts in terms of establishing whether they were paying a comparable rate.
Mr Johnson: I think the point I would add to those two observations is that an important area of support that public sector organisations need is understanding the right mixture of things to do and that they are put together in one package. So it is not just about pay, it is about the structure of the contract and the reward arrangements of the individual, and there are many things that are attractive about working in the public sector that are not about pay. For example, if you were a senior commercial person, say, in a big organisation like BP or Shell, you could be interested in coming into the public sector because the scale in which you are operating in a commercial role is much more significant than might be the case out in the private sector. So helping organisations to understand how to balance these different factors together and to structure a reward proposition, I think, is a very important piece of advice and then informing it about what goes on competitively and what does that imply about the level of pay, I think, is then a second part of the support that public sector organisations need.

Q110 Chairman: So we understand the area, how much would you get paid for helping with a typical appointment of the kind you are talking about?
Mr Boreham: For one of our clients the fees would vary enormously, but if we were talking about a very simple piece of benchmarking, that would be a few thousand pounds. If you were talking about a very substantial top to bottom review of strategy, design of incentives, and so on, that might head towards £100,000.

Q111 Chairman: I am asking innocent questions. I cannot quite understand why these organisations do not know themselves well enough to be able to run appointment systems. I do not know why they have got to add several thousand pounds to every appointment to get people like you involved. You tell me.
Mr Evans: It is not only appointments, it is when they are reviewing their annual increase, effectively.
Mr Boreham: It is a question of expertise. The reality is in the public sector the level of reward expertise within most organisations is limited compared to the private sector, partly because the private sector has exciting toys to play with like incentive programmes and company car schemes, share schemes, and all those things. Typically, the level of reward expertise in the public sector is limited, so they are buying expertise. They are also buying independence and they are buying a broader perspective, because the reality is we work with quite a lot of organisations, so we bring a perspective across the sector, across several sectors, which will allow them to make better decisions.

Q112 Mr Prentice: Why do we not have a review body for foundation trusts? What do you do that a review body could not do in recommending salary increases for the top people in NHS foundation trusts?

Mr Boreham: NHS foundation trusts have devolved responsibilities. Therefore, they have devolved responsibility for remuneration.

Q113 Mr Prentice: I understand all that, but we have got senior salary review bodies for the military, for the judiciary, for MPs, but we do not have one for NHS foundation trusts?
Mr Boreham: The judiciary and MPs are centralised, whereas foundation trusts have devolved commercial freedoms. Therefore, their boards are responsible for determining pay and, therefore, they need pay advice that is particular to that organisation, whereas the judiciary are appointed centrally: they are on centrally controlled contracts.
Mr Evans: The Senior Salaries Review Body does cover NHS very senior managers who are employed by strategic health authorities, primary care trusts and ambulance trusts.

Q114 Mr Prentice: I understand that, but not NHS foundations trusts. So you have got two different ways of determining the pay of very top people in the NHS.
Mr Evans: Yes, and that has created tremendous problems, because trusts and foundation trusts have got the freedom to set salaries, whereas the other bodies that are covered by the very senior managers framework are constrained, and that has caused some tensions, because PCTs and strategic health authorities feel that they cannot recruit and retain because salaries are moving faster, because people like foundation trusts have increased them at a higher rate. So there is tension within the NHS.

Q115 Mr Prentice: Do you think all parts of the NHS should be treated in the way that NHS foundation trusts are treated: that they should all determine their own pay?
Mr Evans: Government policy is that we are moving to a situation where there will be more foundation trusts where more organisations have got the opportunity to apply for foundation trust status.

Q116 Mr Prentice: Is a fragmented and atomised NHS where every part of NHS family, if I can put it that way, can determine their own pay to get the best people something that you would advocate?
Mr Evans: Yes, I think I probably would, within some sort of framework, within some sorts of constraints, and they are subject to monitoring by people like Monitor, who monitor their performance, and how they set their remuneration, again, is subject to public scrutiny.

Q117 Mr Prentice: Hamish, you do something slightly different, do you not? Could you add your bit to this?
Mr Davidson: We probably come in at a later stage, in the sense that an organisation decides there is a vacancy, or a vacancy looming, and my job is to: go along and help them articulate what the job and the person specification is; and then to work out a strategy of how we might attract candidates; to then potentially go and find those candidates through a combination of advertising and, possibly, head-hunting; to perhaps assess those candidates at initial interviews, et cetera; take soundings on them; to go back to the client with all the materials, for the client to agree on the particular shortlist to see; and then to assist the client make an appointment. I take them through that entire process.

Q118 Mr Prentice: A mischievous person could say that these organisations, first of all, spend several thousand pounds identifying the pay level they are going to be working at, and then they have got to pay several further thousand pounds to employ someone to go out and recruit somebody.
Mr Davidson: They may well do. Some of these organisations, of course, recruit themselves. Certainly in central government posts I would have thought at least over half of the posts are undertaken themselves. The reason for the increased use of head-hunters over the years and moving to somewhat more of a private sector system of recruitment is fundamentally: (1) If you have tried and failed to appoint, then maybe you have to go back to the market again, and you think, “We will need some assistance generally with candidates.” (2) There has been a thinning of HR capacity to actually help on the recruitment process as bureaucracy has been cut back and resources pushed to the front line. (3) The increased complexity of the roles, particularly at chief executive level, means that the kind of skills you are looking for are in very short supply and, therefore, it is a narrow pool, and some of these people are not so prone to apply of their own volition. (4) There may be the perception generally from clients that there are very few people who could do the job and, therefore, they will need to be teased out. (5) There has been an increasing desire to bring in some kind of independent assessment to assist those undertaking the appointments. (6) There may be a desire to test the market anyway, to test internal candidates against what is available externally. (7) There has been an increased “mortality” rate, particularly of chief executives, particularly in the NHS and local government, if they are perceived to have failed and the organisation is not delivering; and (8) also, of course, to address the diversity issues, where there has been a particular desire to bring in a greater range of candidates than the typical male, stale and pale that you have had before. For all these reasons, I think you have seen an increasing tendency on occasions to utilise the services of recruitment consultants.

Q119 Mr Prentice: But when you have said all that, if you are looking for an instant way to reduce the public sector pay bill, you could remove yourselves from the picture and that would produce an instant huge saving, would it not?
Mr Davidson: It might do, but, of course, one of the interesting tendencies in recent years is that candidates have become more and more reluctant to apply of their own volition for posts, unless they think that there is strong likelihood that they are going to be a candidate and, indeed, possibly get appointed. There has been a change in behaviour

from, say, 20 years ago when I was first doing this kind of work in the public sector, a dramatic change in behaviour, for a whole variety of reasons.

Mr Boreham: I think there is also a danger that, if organisations review their own pay policy without external independent advice, they may come to some spurious conclusions. I will give you an example. We are a local authority. Our turnover is half a billion pounds. If we look at the listed company market, that would put us into the FTSE mid 250. A FTSE mid 250 chief executive would be paid a salary of half a million, plus bonus. Let us set our salary policy at half a million. It sounds superficially reasonable, any of us could tear that to shreds as a policy, but I think you need an external perspective to do that, otherwise you end up either with misinformed decisions or, indeed, the executives themselves pushing for something and the non-executive directors not having enough confidence to push back.

Chairman: There is a further charge against the effect of your work, which Kelvin is going to talk to you about.

Q120 Kelvin Hopkins: I am deeply sceptical about all of this, may I say. If I was being very cynical, I would say you are all part of a little club levering up a small group of people's salaries and taking a big cut yourselves, because that is what you do. Maybe this is unfair, but Polly Toynbee says head-hunters have deliberately inflated pay, poaching top players from a tiny pool of people and using this very small market to lever up the price. I find her argument quite persuasive.

Mr Davidson: I read Polly's statements with interest, and she is, of course, slightly skewing the real perspective here. If I can explain this in terms of what the real reason for salary inflation actually is, particularly looking at local government. I am aware that this is taking events out of scope here, but it has a knock on effect to the posts that you are considering. Question: why has there been salary inflation at all? I have made the point already that a lot of these jobs have become much more complicated, so it is perceived that fewer people can do the jobs. The second point is that, compared with 20 years ago, central government now rates highly the best of talent in local government. Twenty years ago they did not. If I had gone to do a senior level recruitment exercise for the Civil Service and suggested we head-hunted within the local government community, I would have been laughed out of court. Today local government is considered one of the few areas of public service where there are real, solid delivery skills, and delivery skills are what are being looked for. The second point is the unintended consequence of the CPA[1] regime, which ended up causing many organisations to decide: rather than appoint someone on the up, we will need a serving chief executive from elsewhere who has learned their mistakes first time around and knows what to do differently and has a minimal learning curve; and that links into a third point that does not seem to have come up in your evidence to date, which is a behaviour one. In the public sector people do not tend to take a cut in status or a cut in salary; period. People do in the private sector, but typically not here in the public sector. If you are moving into not-for-profit, yes, but generally the public sector will not take cuts in status, and will not take cuts in salary. Fourth, there is also an increasing tendency, and it has not changed, to draw the present specifications very narrowly, and therefore, again, one is dealing with an ever declining pool of candidates in terms of how the positions are specified right at the outset. Fifth, there is also an increasing tendency, as I have suggested, of candidates not responding to job adverts themselves. Candidates are much more concerned about confidentiality nowadays. Again, 20 years ago they would have been quite open with the leader of the council and with colleagues about the fact they were going for a job. Today they are not. They are worried about leaks, they are worried about undermining the relationship with their leader, they are worried about the knock-on effects of destabilising their organisation if word gets out that they might be leaving. Consequently, candidates are waiting to be approached and they are very suspicious. Years ago I recruited, it ended up being, Bob Kerslake (then CX of LB Hounslow), to the post of chief executive at Sheffield. I managed to assemble what was considered a very strong shortlist in those days—this must be about at least eight years ago. I could not achieve the same today because not enough candidates of calibre would all agree to go forward, and the point that Polly misses—this is all building up towards salary inflation—is that people need to be teased out, that the balance of power has shifted more to the candidates to be able to negotiate hard on their salaries. The final point that Polly completely missed is that, unlike in the private sector, where typically a head-hunter's fee will be based a percentage of their eventual remuneration (their pay), that does not apply in the public sector. For the most part and with few exceptions, in the public sector recruitment consultants charge a flat fee.

Q121 Kelvin Hopkins: It is interesting what you say, but I am still unconvinced. If I believed there was a real correlation between higher salaries for the people you have recruited to public authorities and the performance of those public authorities, I might be convinced, but I do not think there is. Indeed, we have got some examples of people in the quasi public sector on vast salaries, each of whom, or the organisations they are organising, have performed not well. I do not want to single them out, but I could. I know a fair amount about several of them, and I am not impressed with their performance, even though some of them are paid over a million pounds a year. In the NHS some of the NHS trusts have appointed smart money-saving business types who have squeezed the services and the services have suffered as a result. Stafford Hospital might be a case, and the money they have squeezed out merely goes to pay their high salary and their bonus for

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squeezing the money out. It does not actually help anyone apart from themselves and, then, of course, they move on and say, "It was not my fault." I am just not convinced that this is the way forward. I may say I have been involved in many public appointments myself, I have been on interview panels, and we have made very good appointments without any advice from yourselves.

Mr Davidson: I would not deny that that is the case in most situations, but there are a number of situations, equally, where organisations decide they do want assistance or they have tried to recruit and failed. You have been fortunate in your own experience. I doubt any of us here would disagree with the thought that a very rigorous performance appraisal is required, and I doubt if any of us would disagree with the fact that failure should not be tolerated. However, one observation I would make is that it does depend on how you judge failure. I was involved, as some of you may know, in the recruitment of the Sergeant at Arms and the Secretary to the Speaker of the House of Commons, both of whom fell out with Mr Speaker and both of whom subsequently disappeared. It was not a question of their performance though, they were not perceived to have failed in their jobs, but the relationship might have done. So we have to be careful about what is perceived to be judged as failure.

Q122 Kelvin Hopkins: I think we could make the mistake of arguing from the particular to the general. There may be individual cases which I could quote as well. Nevertheless, I am still not convinced. Have you done a study relating the success of an organisation to the level of salary? There are a lot of comparators that you could use in local government and in the Health Service to do this.

Mr Boreham: I think that fits with the thesis that, I think, a number of us share. The problem is the money has all gone into salary. What we are saying is, if this person is wonderful and is equipped to run this complicated organisation, then an element of that pay should be linked to them delivering what they have promised to deliver, and if the organisation is not achieving the things it is supposed to be achieving, then their variable pay is not delivered; if it achieves more than was expected, then they receive more in variable pay, and that actually deals with the value for money question that you are addressing.

Kelvin Hopkins: I could go on, but I think I have had my share.

Q123 Chairman: Hamish, you have explained, quite well, I think, some of the reasons why we have had what you have called salary inflation. If we were worried about that, if we wanted to do something about that salary inflation, knowing all you know about the market, how would you turn it round?

Mr Davidson: Fundamentally we are here talking about the supply of candidates, and the issues I think you might like to consider in that regard would be the tendency of public sector employers to: write specifications that are far too narrow; that require candidates to, effectively, walk on water and perform miracles several times a day, which automatically means you have got a very narrow group of candidates; and the tendency often of the people creating these specifications, including many head-hunters, I might add, to be pale, male and stale, et cetera, in fact dull and boring too. I recall Sir Gus O'Donnell, before he became Cabinet Secretary, indicating that what he thought the Civil Service needed was more people with pace and passion, and I put the point to him at the time that I am one of the people required to go and deliver people with pace and passion, but do you know what happens? The departments do not appoint them because they are perceived as "too out of the box". So I think the panels need to be ready to take a bit more risk here. The failing with recruitment panels is the tendency to appoint to the lowest common denominator and the tendency to appoint conservatively with minimal risk, which is not something which I can understand. I also think that the recruitment processes probably needs to be less Masonic-like, particularly if you are trying to attract private sector candidates who just do not understand some of the processes and it is not explained to them effectively enough up front. In particular, the speed of a typical public sector recruitment process, which is typically much faster than it is in the private sector, and candidates, as a result, have not emotionally fully engaged to decide whether they do want the job or not. So, getting asked by the panel, "If offered the job, will you accept?", is quite a shock to the poor candidate who has just gone through their interview that day. In terms of dealing with failure issues, I would focus heavily on much more rigor in performance and appraisal, and a lot more ruthlessness, frankly, in dealing with failure altogether. For all of that, I have to say to you that there are serious problems ahead, because, for the first time in a long time, there is an entire generation of chief executives, leaders, and managers in public services who have only ever managed in growth budget situations. From 2011, we may be facing maybe 10 years of radical cuts altogether, and the people are not there. Consequently, I am afraid, as much as it may pain this particular Committee here, I think you are going to see organisations ending up using head-hunters more to find those few people that have got the required skills, because most of them were pensioned off early.

Q124 Chairman: So we have got all the wrong people running these public organisations.

Mr Davidson: No, a lot of people that do not know how to manage in a downturn.

Mr Johnson: I was going to make three more process suggestions about things that could be done which could help contain inflation in public sector pay. I certainly agree with the point that Hamish has just made about the importance of managing performance, and I think the public sector has quite a lot to learn in terms of managing performance rigorously and consistently across a broad population of senior people. Secondly, I think it is very important that the public sector grows talent.

The Civil Service is 500,000 people strong—that is a large organisation, by any stretch of the imagination—and ought to be able to be capable of growing a lot of its own internal talent, but that does imply very careful exposure to different experiences through a career which may be outside as well as inside the public sector. So I put a lot of weight on talent management processes. The third thing I would do is I would give more emphasis towards cash than base pay. I think this was a point that Peter was making. At the moment there is very little pay that is variable and linked to performance in the public sector, and I think if there was more pay linked to performance, with risk as well as upside, so it is not just about a bonus but it is about the real risk of money being held back as well as money given for good performance, that would help a lot in terms of inflation pressures. Then the final thing is, I subscribe to the view that there is a governance issue around this for the public sector, and in the evidence I gave you[2] I attached weight to looking at a pay review body process across the public sector more broadly than it is today. I think it is too bitty. I do think that different parts of the public sector have different needs, so there is something here about focusing on principles of reward for executives rather than specific pay increases for particular groups, I think, and I think there are governance mechanisms put in place around the use of non-executive directors and reporting, and so on; but it frustrated me when I was in the Cabinet Office that we were wanting to draw talent into the Civil Service with great delivery experience from local government, as Hamish indicated earlier, but the pay regimes in local government are different from the Civil Service and got in the way of our ability to attract people into the Civil Service. From a citizen and a taxpayer point of view, that cannot be right. From their perspective, I would have thought, there needs to be more coherence, not to the point of consistency and performance but certainly more quangos.
Chairman: Thank you for that.

Q125 Mr Prentice: Can I come in on that? I want to talk a bit about openness and transparency, which we are all concerned about. Mr Davidson, you talked about these people at the top of organisations who were worried about confidentiality. You mentioned people of calibre just waiting to be approached, and so on. What difference will the regulations make that are currently out for consultation, requiring full disclosure of the pay and perks of local authority chief executives and senior people, and, similarly, in those other areas of the public sector—NHS foundation trusts that we have already spoken about—what difference would openness and full transparency make to the market?
Mr Davidson: The short answer is none whatsoever.

Q126 Mr Prentice: I do not believe that.
Mr Davidson: None whatsoever, if you are talking about detailing remuneration. I think there is no difficulty at all. Personally, I think absolutely philosophically and generally there should be openness about what people get paid in those situations: it is public money fundamentally. The point of confidentiality I was alluding to was about applying for a job and the detail being leaked that you are applying for a job.

Q127 Mr Prentice: The Government is going to bring in these new regulations and full disclosure because the Government believes, ministers believe, it will depress this relentless increase in chief executives' salaries in local government. You are shaking your head, Mr Davidson. I wonder what the rest of you think. Does disclosure tend to depress the increase in salaries?
Mr Evans: I think local government is probably out of kilter with some other parts of the public sector such as the NHS, where there already is transparency. Even foundation trusts, in terms of their annual reports and accounts, would have a remuneration statement that would set out the basic pay, the bonus arrangements, even the pension contributions and the pension pot, effectively, of the chief executive and the executive directors. So there already is disclosure within the NHS and some other parts of the public sector. I am not sure whether that has led to depression.

Q128 Mr Prentice: You are the expert; I am not an expert. In which parts of the public sector is there not full disclosure? We know there is not full disclosure in local government; in which other parts?
Mr Boreham: It is mainly local government. That is the big obvious area where there is not disclosure, but I do not think disclosure will cause pay inflation. The reality is that pay inflation is there. To an extent, if you publish people's salaries, those who are paid lowly will point to those high salaries available elsewhere and will ask for a rise, but the evidence from both the public sector and the private sector is that decision-making is improved where there is full transparency of what the outcomes are.

Q129 Mr Prentice: It is not just salaries, it is pension entitlement, it is perks; it is the whole package.
Mr Boreham: The whole thing, yes.

Q130 Mr Prentice: Life will just continue as before once all this stuff is published. Are you trying to tell me the Taxpayers Alliance, and people like that, are not going to collate that information, bring it together, publish it, campaign on it and write to Members of Parliament?
Mr Boreham: That is my point. If the outcome of remuneration decisions is transparent, then remuneration committees who are making those decisions will have regard to how those decisions are perceived by the public, by voters, by the people who use their services. So, on the whole, I agree with you: the totality of the package is absolutely helpful.
Mr Johnson: And because it opens up accountability more clearly, it will be a cap—not a cap but it will be something that restricts wage inflation.

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Mr Boreham: It is very difficult, if you are a local authority, to go out and set the highest local authority chief executive salary in the country, because that will be immediately picked up on and the remuneration committee will be asked to justify that, so you would have to have a really clear reason for doing that.

Q131 Chairman: You are saying, though, that a perverse effect would be that people would see that other people are getting more than they were getting and then want more.
Mr Boreham: There is definitely an element of that. I am not going to pretend to you that transparency will not cause that to happen, because we have seen that in the private sector, but the reality is that where there is no transparency pay levels tend to be higher. If you look around Europe, the country in Europe that has the highest pay arrangements is Switzerland, and that is because Switzerland only started to publish last year.

Q132 Chairman: Do we have enough transparency for quangos?
Mr Boreham: Quangos, on the whole, make remuneration disclosures. I think they could be strengthened, I think they could quote a figure in thousands rather than a range of 5,000, which is neither here nor there really. They should be clear about perks that are available, and pensions.

Q133 Chairman: So we could have a standard disclosure regime across the public sector?
Mr Boreham: I think that would be helpful. I am not sure I would want to see the 15-page disclosure that you see in the FTSE 100 remuneration reports, but, yes, if we could come up with some baseline transparency that applied for all public funded bodies, I think everybody would be happy about that.

Q134 Mr Prentice: I have got this article in front of me by Clare Fox. She is the woman who runs the Institute of Ideas. She spends all her time thinking!
Mr Davidson: Great thoughts?

Q135 Mr Prentice: She is talking about this and she describes attacking high council salaries as merely feeding the demonisation of ambition, “The anti-fat cat rhetoric inevitably feeds the demonisation of ambition”. What do you think about that thought? Does it? You have not thought about it?
Mr Johnson: No, I think it is close to nonsense actually. In terms of demonisation of ambition, I think that is nonsense. I think evidence of the degree of disclosure in the private sector would confirm that it is nonsense. What I do worry about is that there is demonisation of fat cats—and that is not the right term, obviously—demonisation of senior executives in the public sector, when actually what they are doing, and they are paid to do, is to deliver something that is very important for the country. I worry enormously about that, because I think it discourages really good people from coming into the sector, ie “Why should I put up with that?”

Q136 Mr Prentice: We have got something here about really good people, and I struggle with that, but Polly Toynbee, when she came before us, talked about a maximum pay commission. We have got a minimum pay commission; she was pressing for a maximum pay commission, but it would just be purely advisory. What do you think about the more general point she made about pay ratios: that if you get the chief executive of an organisation getting 100 times, 200 times more, 400 times in the case of the chief executive of Tesco, what the person on the check-out is getting, then the organisation becomes, in a sense, kind of dysfunctional?
Mr Boreham: I think there is a serious point to be made about equality of treatment within organisations. I think the ratios test is absolute nonsense. One of the reasons that Tesco has a very high ratio is because Tesco is large. So the CEO at Tesco gets paid more than the CEO of a smaller retailer, which is exactly what you would expect to happen. You would also expect the ratio to be much higher in an organisation that has large numbers of relatively low-skilled workers, which would be the case in Tesco, than would be the case in an engineering-led company, or a fund management company, or a bank. So I think the ratios test is a completely meaningless and spurious way of assessing this. Similarly, if you have got all your workers in Poland, for good, sound business reasons the ratio would be worse than if they are based in London. So ratios are garbage, but I think it is appropriate that remuneration committees have regard to the way that they treat their people relative to how they treat their bosses.

Q137 Mr Prentice: What about an organisation like the Police Service? We do not have any police officers in Poland. You would say that the same argument applies, that it would be absurd to determine the salary of the Metropolitan Police Commissioner in reference to what the police constable on the beat gets.
Mr Boreham: Yes, because I think you would have to look at the Met and say that this is a particularly large and complicated organisation compared to some other smaller forces. So you would expect the person who is running the Met to be one of the highest paid police officers in the country.

Q138 Mr Prentice: Is that the view of you all, that there is no sense in going down this road of looking at pay ratios within discrete organisations?
Mr Evans: I think it is interesting to crunch the numbers in context, but I think that is all it should be, a background context to inform the discussions. I do not think there should be any fixed rules.
Mr Boreham: You could track the ratio if it is a consistent organisation. If the organisation itself does not change, then tracking the ratio may be useful over time.

Q139 Mr Prentice: For example, the military, or something like that?

Mr Boreham: You could check how the pay of generals moved over time compared to the pay of privates, because you are not going to outsource your privates to Eastern Europe.

Q140 Chairman: If we had a standard disclosure arrangement, one of the things that we could disclose is that ratio of how it changes over time.
Mr Boreham: I think the ratio is fundamentally unhelpful. Polly Toynbee referred to the situation of outsourcing cleaning and catering staff. As soon as my organisation outsources its cleaning and catering staff to Chris's organisation, then my ratio gets better and his gets worse.

Q141 Mr Prentice: I remember the exchange very well. She said that in the public sector 28% of all people are professionals, in the private sector it is something like 8 or 9% because the public sector has been outsourcing all the low-paid jobs to the private sector. I remember that exchange.
Mr Boreham: It does immediately distort the ratio.
Mr Johnson: I do not think it is just because the public sector has been outsourcing some types of work. I think the nature of the role of the public sector means that it needs more professionals proportionally than most private sector organisations do to finish the work.

Q142 Julie Morgan: I wanted to ask about your experience with the public sector organisations you have worked with. You come in and you are paid your thousands and you give your advice.
Mr Boreham: I am sorry; our companies are paid thousands.

Q143 Julie Morgan: I mean your companies, yes. What is your general experience? Is your advice accepted, and do you measure what the results are afterwards?
Mr Johnson: I will start. Certainly in the case of the firms I have worked with over the years, providing advice is a mixture of providing objective, dispassionate advice on the one hand and working through with the client to help the client get to a decision that takes into account the advice that we give. Yes, we are very interested in the effect of that advice, so over the years I have looked at organisations and watched them to see whether they seem to be making progress as a consequence of advice they have taken from firms I have worked with or other firms. It varies from consultancy firm to consultancy firm, but most consultancy firms do some sort of review with the client after the work has been done to take stock of whether the advice was the advice which was required and whether it had the impact that was desired.

Q144 Julie Morgan: So you do review it?
Mr Johnson: Yes.

Q145 Julie Morgan: What are the results generally?
Mr Boreham: Do clients always take our advice? No, and, indeed they should not. It would be an unfortunate situation if we were making decisions for organisations, and I am quite uncomfortable when an organisation wants me to tell them what to do, because it implies that they have not engaged with the task that they are looking for help with. So most of the time, yes, they take our advice, but they do change it, they do ignore it. Sometimes, actually, afterwards, we work out they were quite right to ignore our advice.

Q146 Chairman: You still get the fee, do you not?
Mr Boreham: Absolutely.

Q147 Julie Morgan: What about political involvement in setting pay, for example? What do you think of politicians setting the pay for the chief executives?
Mr Boreham: I think it is very difficult for politicians to set pay, because the politician will immediately look at how this will play when it is disclosed in the newspaper, and that will weigh very heavily on his or her mind, quite understandably, whereas the remuneration committee chairman of an independent organisation will be focused on the needs of that organisation in particular. I think it is difficult for all of you to set pay levels for an external organisation. At the risk of making myself very unpopular, political decisions were taken some time ago to hold down the pay of MPs and to reward in a less transparent way, and I think that is probably something that everyone now regrets. That is an example of a political decision taken to keep the headline level down. The same thing could easily happen if we were trying to have political decisions for pay, for example, of a local authority chief executive.
Mr Davidson: That last point is very prevalent here. I think that there has not been a local authority chief executive appointment, one that I was involved in, where politicians were not involved in setting the pay. The unique thing about a chief executive appointment is that for every other appointment in the authority the chief executive is the client, whereas for the chief executive appointment the politicians are the client, and they are, in my experience, very sensitised to the remuneration issues. Indeed, I think that is vital, because they will, in the end, have to defend this when it becomes public, because there will be an open salary on there. My practical experience has been that I have often given advice in terms of what I think, and sometimes that advice has been accepted and sometimes not. I explain the implications of not doing so and we move forward, but I have never had a problem with politicians having some involvement. More generally, taking the discussion away from pay for a moment, my practical experience over the years, moving right across public services, has been that often the clients do not take advice and particularly advice that has been geared towards opening up the specifications to make them less onerous. The last time I gave evidence to your committee, I made the point about: diverse teams making more informed decisions; the best of talent in any one sector being as good as the best of talent in any other sector; and talent coming in all shapes and sizes, guises, sectors, nationalities,

whatever it may be. I make that point relentlessly to clients in public services. Sadly, they tend to pay lip service to this and then proceed to narrow down the specification dramatically, thereby narrowing the potential pool of candidates, and thereby, I am afraid, back to inflation in remuneration.

Q148 Julie Morgan: I think you talked earlier about the pale, male and stale appointments and a sort of world that is a bit pale, male and stale. I know the appointments you have made have not all been pale, male and stale because I think you have been responsible for some appointments where women have come in and black and minority ethnic candidates, but it does seem as if it is all from a small grouping of known people. I suppose that is my criticism really of the idea of head-hunting. You are complaining about a narrow specification, but head-hunting implies that you go to those that are known, and I think that is really something that does go down quite badly sometimes with the public and people know about how it is done?

Mr Johnson: As a client in that situation, because I have been a client, I have actually been a client to Hamish, my experience is that the client is often pressing—almost the opposite of what Hamish is saying—the recruiter to think more broadly. I can think of a number of instances where we were looking to make sure that we had tapped into potential candidates that were from minority groups and what media could we use to do that and how could we get the recruiter to focus on those parts of the market place. So I do not think it is the case that everybody takes an easy option, recruiting in their own image or recruiting from the people they know. I think there is a serious effort on both the client and the recruiter's side, in my experience, to widen the net and to make sure that we, as we then were, are picking up from a much more diverse group of candidates. I felt quite heartened actually by my own personal experience in that respect.

Mr Davidson: Chris was an enlightened client, frankly, although I have to beg to disagree to some extent here. First of all, I will accept, you will be delighted I say this, I guess, that head-hunters are often part of the problem, not part of the solution. They are part of the problem in that they themselves tend often not to challenge the client sufficiently, they tend often to take the lazy way out, because if, in fact, it turns out that we only have to look at a very small pool, it is less work. They often are themselves made up of male, stale and pale, they often are made up of people who work in that unique sector, so they are minded to think about only that sector as well. So I would be quite critical of many of my colleagues in this environment. However, I am also aware that sometimes, for statistical purposes (and the Cabinet Office were very assiduous at one point in collecting statistics in terms of analysing a break-down of shortlists and such like), yes, there is a pressure to deliver candidates who are not of the norm, but I come back to my point that often those people do not get appointed and they have a bad experience and, as a result of that, they decide, "I am not going to apply for these jobs again." This is what happens. So there is a real conundrum here in terms of delivering that diversity of candidates linked back to this point of inherent conservatism of the appointment process.

Mr Boreham: Can I make a specific point on diversity, which is to do with the recruitment of non-executive roles into public bodies, for example. Non-executive roles in the public sector are actually paid extremely low compared to the private sector; so a discount from private sector to public sector exists at executive level, but at non-executive level it is much larger. This actually causes quite a serious diversity issue, because typically you can only get people of the necessary experience if they have retired on a nice fat pension, so you tend to end up with people in their sixties or their seventies. They are not just male, pale and stale but they are certainly pale, because the reality is that there are not enough black and minority ethnic people in their sixties and seventies with deep business experience and credibility. If you want to get more black and minority ethnic non-executive directors into the public service, you have to recruit people who have got a day job, and the reality is that if they have got a day job, £290 a day is not going to do it. It also raises the question of diversity of outlook: because if all your non-executive directors are portfolio non-executives or people who have retired, you are not getting the perspective of people who are in work at the moment, who are raising families and who are more representative of the population of the UK as a whole.

Mr Davidson: I agree. There is a real dilemma there—with regard to the issue of how we tackle that, particularly the under-representation of youth for example. In the latter case, the typical excuse will be "We cannot hire them as non-executives because they have not had enough life experience and experience generally." How are they ever going to get it? I do not understand why more quangos in particular but all these public bodies too—have not set up shadow boards to draw in the talent to give them practical experience to grow. It tends not to be done. I have made that plea several times. Coming back to your point here in terms of these appointments, to explain the conservatism point here whether it is non-executive or full-time jobs, often the panels will make the logical hire—not the inspired hire. The inspired hire is that person who is a bit different who does not fit the norm and is outwith the people we know about.

Q149 Paul Flynn: The evidence we heard this morning has reinforced the view that essentially your role is parasitic. You have virtually said so. If you disagree with that, where is the proof that your intervention and the vast fees paid to you has resulted in the improvement of the efficiency of the organisations?

Mr Davidson: You ask a direct question and I would be prepared to point directly to examples of organisations I have been involved with over the years.

Q150 Paul Flynn: You just said that often times they do not take your advice and Mr Boreham has said sometimes they are right not to take your advice.
Mr Davidson: I think that is fair.

Q151 Paul Flynn: On balance, where is the advantage in employing you and where is the proof of it?
Mr Davidson: My perspective may be somewhat different. The kind of client base I have had have tended to be the doomed, the dying or the failing type of organisations or the seriously aspirational that do not want boring candidates. They need seriously change focused candidates and those individuals do have to be sought after, particularly where we are trying to recruit for organisations with very poor reputations.
Chairman: You are not talking about the Speaker's Office, are you?

Q152 Paul Flynn: You were responsible for the advising of the Chair, Chief Executive and the 14 Commissioners of the Commission for Equalities and Human Rights.
Mr Davidson: A fascinating exercise.

Q153 Paul Flynn: One of the pinnacles of your career perhaps?
Mr Davidson: No, I think the Chair of the Electoral Commission would be the pinnacle.

Q154 Paul Flynn: The Chair was appointed at £160,000 a year, the Deputy Chair and the Commissioners get a daily allowance of £600 and £400 respectively, so not a lot of equality there. Three senior personnel resigned from the Commission within a week in March: the Chief Executive, the Group Director of Strategy, and one of its Commissioners. Sir Bernard Massie, another Commissioner, also sent a letter, a written warning, to his colleagues expressing concern at the Commissioner's performance. Do you think your advice and the cost of it were justified by the chaos that resulted from those appointments?
Mr Davidson: You are assuming that I gave advice that the particular individuals should be appointed which is not necessarily the case.

Q155 Paul Flynn: There is no need to reveal your involvement. How much was your organisation paid for this and what is your assessment of the result?
Mr Davidson: My understanding is that there is no criticism of the Chief Executive who has resigned, Nicola Brewer. She is a very highly regarded and talented individual. My understanding of the Commissioners who resigned is that it is more to do apparently with the criticism of the Chair and with regard to the Chair appointment. I did not make that appointment.

Q156 Paul Flynn: This is the parasitic nature of it. You go in, you give advice, and if it goes wrong it is nothing at all to do with you but if it goes right I presume you claim the credit. I have not seen any evidence from you yet of why you are necessary. We have seen this enormous explosion in the use of consultants. Where has been the resulting improvement in the efficiency of the bodies that employ the consultants? Is everything more wonderful now in organisations where consultants are used? Are they more efficient and more profitable than before? Where is the evidence?
Mr Davidson: If you want to look at specifics, I would, in local authority terms, point to places like Coventry, Birmingham, the Audit Commission and Camden. For those organisations I could give you evidence. In terms of when an organisation begins to fail, there are very many complicated reasons why that will occur. It may indeed be to do with the relationships between the chair and full-time appointments, just as it is sometimes between politicians and full-time appointments as well. I stand by the point that if we are deemed to have failed we will not be asked back. What is interesting there is that in the main we got asked back. Nonetheless, I take the challenge; it is a fair point to raise.

Q157 Paul Flynn: You corrected one of my colleagues here who said that you are paid thousands and you said no you were not paid thousands, your organisations were paid thousands. You are not doing this work from the goodness of your heart or are volunteers in some way. In the interests of transparency, would you like to tell us what you are paid?
Mr Boreham: I have a copy of my P60, if you would like to see it.
Mr Davidson: I indicated that in the public sector what happens is the fees tend to be a flat rate for recruitment whereas in the private sector it is a percentage, therefore there is no salary inflation in that sense. To answer your question directly, in my last full year I got paid £190,000 so just below the Prime Minister in that particular case.

Q158 Paul Flynn: We know Mr Boreham is paid £126,000.
Mr Johnson: I used to work for a different management consultancy from the one I work with now. My base pay then was £170,000 and my whole earnings were about double that. Then I worked in the Cabinet Office where my base pay was £135,000 and my whole cash earnings were £150,000. Now I am with Mercer and they pay broadly in line with what is transparent.
Mr Evans: I am feeling considerably underpaid.

Q159 Paul Flynn: You are not going to tell us by how much you are underpaid. You do not have to.
Mr Evans: I am paid less than an MP.

Q160 Paul Flynn: Then you are grossly underpaid then. On the question of pay, we have seen the examples quoted of using the Prime Minister, or in Wales the First Minister, as a benchmark. The First Minister of Wales has something like six people working in the Welsh Assembly who are earning more than he does and there are 194 public workers earning more than the Prime Minister. One of the examples of this, what the people blame, are those who were recruiting at inflated salaries looking at the examples of the local authority public sector as well. Has not the whole pyramid of what we regard as being a just and fair pay system been distorted by this?

Mr Boreham: The Prime Minister's salary is a very bad basis on which to set other people's salaries. In reality, the Prime Minister's salary is a political compromise and the main earnings opportunity for a prime minister are not what he or she receives in office but the amount they are able to earn after leaving office from public speaking, directorships, publications and so on. It is an artificially low figure and, therefore, it is a bad basis for looking at other people's salaries. There is a danger that if, for example, were you to say that no-one gets paid more than the Prime Minister—I know that is something they are looking at in the Netherlands—any kind of artificial cap on salaries tends to lead to unintended consequences. Either that money leaks out in other less transparent unfortunate ways or you just cannot get the people to do the job.

Paul Flynn: That is a fascinating answer. I do not know what is the value of former prime ministers if we contrast Tony Blair and John Major in their capacity to earn outside, but we are greatly concerned about people using public office with an eye to future earnings, in particular where we get former ministers who have awarded contracts for billions of pounds who within a year of leaving office take jobs with those particular firms at large amounts of money. Is this a matter of concern?

Q161 Chairman: It may not be our concern.

Mr Boreham: It is outside our pay grade to comment on that.

Mr Johnson: I share Peter's view about the artificiality of using the Prime Minister's salary as a cap. On the other hand, I do think it is reasonable for people to explain and justify significant pay decisions. The Prime Minister is a highly paid individual and pay decisions that are higher than that would warrant clearer justification.

Q162 Paul Flynn: The First Division Association tells us there is no proof that performance-related pay increases the efficiency of an organisation. Quite persuasively they made the point that the de-motivating effect of those who do not get performance-related pay is so damaging that the general level of efficiency would go down. Part of the mythology of people like yourselves is that performance-related pay does work. Would you like to comment?

Mr Boreham: It is about saying if we deliver strong services to the public then it is reasonable that we are paid higher. We justify that high pay in the terms of the value we deliver. If we do not deliver, then we do not deserve those higher levels of pay and therefore our pay is reduced.

Mr Johnson: I have sat across from Jonathan Baume at the FDA many times having exactly this discussion because he represented people that I was responsible for. The reality is that there is evidence that it points in both directions. There is some evidence and research that would support the point that Jonathan is making. There is equally evidence and research that supports the point that well designed performance-related pay regimes do have a positive impact on performance and people inside those regimes have a positive attitude to the way they are managed. One has to be careful about speaking about one piece of research. I think the key is the point that Peter is making which is that there needs to be consequence for performance. If there is going to be consequence for under-performance, which I think is very appropriate, it is also appropriate that there is consequence for delivering expectations and beyond expectations. The issue is how much money to put into that kind of process. I think of the word "gearing". How much gearing do you put on the back of base pay to get that performance message through to the individual? At the moment my view is, having worked both in the public sector and advised it, that the level of gearing is too low. I do not think the level of gearing should be anything like the level of gearing one sees generally in the private sector but it is somewhere in between.

Q163 Paul Flynn: I appreciate what you said about the level of gearing and so on but there still seems to be a lack of any proof of what is the proper level of gearing in this and that the performance pay does work. Does such proof exist? Can you say absolutely categorically if we have a system that is based on performance rather than based on seniority or the job role that that is less effective than performance-related pay?

Mr Johnson: Proof is a difficult word with research but there is research that would point in the direction that well designed performance-related pay is effective in terms of improving performance of organisations.

Mr Boreham: Let me tell you a story. I do some work in Norway. Norway is a much more egalitarian society and executive pay levels are lower. In general, incentives are regarded with a certain amount of suspicion. I was doing some work for a paper company and the manager of one of their paper mills bounded in to see me. I asked him about incentives, because that is one of the things we were looking at for the client, and he said "I love incentives. I adore them." I was surprised because it is a very unionised blue colour environment. He had gone in to manage this paper mill. They had appalling problems with absenteeism. He had used the incentive programme to encourage people to come to work. They now had the second best rate of people coming to work in Norway. He then adjusted the incentive arrangement to encourage other things that needed to happen in terms of improving equality and efficiency and so on. Used in that sophisticated way it worked very well for him as an incentive arrangement. It is one story but it does work, as Chris said, when it is appropriately designed, where the incentives are things that people can impact, and ideally where the users or owners of that organisation can see a benefit flowing through to them.

Q164 Mr Prentice: Was the incentive just paying people a bit more to turn up for work?
Mr Boreham: I do not know exactly how it was organised. There was some kind of annual bonus payment linked to a number of things and one of them was to do with getting people to come to work. It was not just about me being paid to turn up but actually the whole team was paid if I turned up and then you end up with peer pressure and everybody working together.
Chairman: There was an awful row here recently when the CPS paid people for turning up at work during the snowy weather. People said it was outrageous. It is their job to turn up for work.

Q165 Mr Prentice: The Prime Minister wanted us to turn up on a daily basis.
Mr Boreham: The system that was used was in a fairly sophisticated way. There is always a danger of anything crude that you do the crude thing that you are supposed to do and you completely forget about the big picture.

Q166 Paul Flynn: Mr Davidson, I believe you take full credit for the advice that resulted in the appointment by Ken Livingstone of Bob Kiley. His potential salary linked to performance of £2 million over four years was the highest ever paid in the public sector in the UK. Looking back on that and the subsequent career of Bob Kiley, was that something you have any regrets about?
Mr Davidson: Ken Livingstone and his economic adviser negotiated that package directly. I believe I was paid the princely sum of £25,000 to do that recruitment back in those days and all profess themselves very comfortable with that. I recall that the Prime Minister, then Chancellor, refused point black to ever meet Mr Kiley through the entire period of his appointment which may have had some degree of impact on his ability to get the job done. At the time it was viewed as a very positive appointment. Indeed, as I understand it, Ken Livingstone still declares that to have been an appointment that set in train the transformation of London Transport.

Q167 Paul Flynn: I will not go into it or attack Mr Kiley in any way. The new Chair of the Electoral Commission, you were responsible for giving advice there on his salary?
Mr Davidson: I was.

Q168 Paul Flynn: It was subsequently reduced.
Mr Davidson: It was. At the beginning of this meeting here I commented that there were three categories of jobs: the chairs, non-executives and the others. One of the particular features of that appointment was that was a particularly narrow brief. It is the hardest recruitment exercise I have ever undertaken. It is a very high profile job and it is an incredibly important job that the organisation does and the challenges ahead. We had to try and find somebody who would clear three days of time a week to do this, from a very, very narrow pool indeed, and would have to give up in all cases some other work. I indicated that in my opinion in order to do that, if that is what they wanted, they would have to pay a significant sum for the job. It was at an awkward time, as I understand, in the Commons at the time. The appointment was delayed and delayed and then they decided it was indeed changed. My opinion is that they were very lucky indeed that the candidate concerned accepted that cut and still took the job. I think most of the candidates would have declined to take the job because they would have been giving up a lot more money altogether.

Q169 Paul Flynn: Mr Boreham, in answer to a previous question you said that if politicians decide on a level of salary they will decide on what looks good in the press. I presume it is not part of your experience that politicians might behave out of different motives and might decide on a level of salary because it happens to be just, fair and equitable. How do you square your conviction that politicians always go for low salaries with the experience of local government where we have seen an explosion of salaries by chief executives and those decisions were taken by politicians?
Mr Boreham: I am not sure I was suggesting that politicians always set salaries low. I was saying it is difficult for politicians to set salaries high because of the public interest point. I think the closer the politician is to the organisation, the easier it is for them to reconcile the public interest to keeping salaries low with the need to get on board a really high quality chief executive. In local government there is a very close link between the elected members and the chief executive and the operations of the Council which if they are run effectively by the chief executive will tend to lead the elected members being returned so there is an equality of interest. If you have a politician in Westminster who is somewhat distant from the public body then it is harder for them to reconcile those two issues. I would hate to think that the Committee thought that we believed that politicians would always set salaries low. That would be unfair.

Q170 Paul Flynn: You yourself said sometimes you are right and sometimes you are wrong. Sometimes your advice is good and sometimes your advice is bad and that applies to politicians. Do you think the world is any better a place because of your existence and are you not really parasitic?
Mr Boreham: There is a question about what happens if we are not there. If we are not there then it is easier for the chief executive and the executives in the organisation to argue for themselves like shop stewards. It is harder for a remuneration committee or whoever is setting the remuneration to argue against them if they do not have that independent advice and broader perspective. When I have been into organisations that have been advised by other consultants, I normally find a reasonably well ordered set of pay arrangements. When I walk into an organisation for the first time that has not had access to professional advice, I often, not always, find that pay arrangements are quite a long way out of line with what I would normally expect to pay,

sometimes too low but quite often too high, and that is because things have been set in a vacuum without professional advice.

Mr Davidson: I take the question on the chin. I would accept that in many cases head- hunters are parasitic I think it is fair to say. I think that in many cases what head-hunters do is equivalent to moving pieces around the jigsaw board. We solve one person's problem and thereby create a problem elsewhere. I think that is a fair challenge. The response to that then is we and our clients have an equal duty to try and develop new talent and that new talent has to be developed by the appropriate feedback given to the candidates we interview and in all cases try to encourage them to do better next time. What I think is not done sufficiently is the effort to develop the new talent—a point Chris made earlier, particularly within organisations. I think your challenge is fair.

Q171 David Heyes: You have some very complicated ways of answering, you remuneration consultants, a simple question: "How much should I pay my people." I have been making notes as we go along and the kind of mysterious language that you use about reward arrangements, reward propositions, variable compensation and you deploy your reward expertise in giving the advice and so on. It is just a matter of how much should we pay our people and an important part nowadays is pensions. There seems to be a perception that in the public sector pensions are generous, over-generous some people would say, compared with the private sector. I wonder whether that is true and whether that is at odds, for example, with the type of pension that the Fred Goodwins of the world get. Are we really too generous in our pension schemes in the public sector?

Mr Boreham: I think there are a number of factors here. First of all, the Fred Goodwin deal is reasonably common amongst private sector executives who have been around for a long time. If you have joined a FTSE 100 company in the last seven or eight years from the outside you are not going to be in a final salary scheme. You will be in a defined contribution scheme. I think that the public sector pensions for the vast majority of staff are a long way ahead of what those staff could get in the private sector, a very long way ahead, and the gap has widened. At executive level that is not so true because in the private sector executives receive proportionately greater pensions on their already high salaries.

Q172 David Heyes: You have a suggestion to make which is to cap public sector pensions, is that right?

Mr Boreham: That is right. In so far as you are providing somebody with a guaranteed income for life when they retire, I think that is a legitimate strategy but I question whether we need to guarantee somebody half of their salary as a local authority chief executive on maybe £200,000 plus a pension lump sum. It is reasonable to have a much lower guaranteed benefit, for example you cap the pensionable salary at £30,000, and that is an arbitrary figure. Above that level the pension is provided on a defined contribution basis in line with what happens in the private sector. That means you have much less of a guarantee as to what you would be paid but you are guaranteed a basic level of income. It is a mixed system.

Q173 David Heyes: I would like to see what your colleagues think about that suggestion. The thought that comes to my mind is with a cap like that you are going to pay the same sort of pensions to your top managers as the middle and even lower ranking managers and how does that sit with what you call a reward system where a pension is a pension?

Mr Johnson: Peter and I have never spoken about where we think public sector pensions ought to go. I have to say my thinking is very consistent with Peter's. When I was in the public sector I was quite open about where I thought, in the longer term, public sector pensions should go. The way I come at this is that the public sector employers are a large number of relatively low paid people delivering quite difficult and important services. Part of the compact between the country and those individuals can be a defined benefit pension scheme. Seeing that up to a number, whether it is £30,000 or £25,000 you can argue but seeing that defined benefit provision up to a certain salary, is a very reasonable part of that compact. Over and above that then I think the individual both has more income that they can choose to spend in whatever way they choose to spend it. As a consequence, bringing them into a defined contribution pension plan that they can supplement or not as they wish and have more financial freedom to do that feels the equitable way of getting the right balance between an employee who is able to prepare for retirement, on the one hand, and keeping the expense of that under control.

Mr Evans: I echo what Chris said. In a way there is a deal that is done with the public sector that people accept lower pay than they would get elsewhere in return for having a more generous pension arrangement.

Mr Boreham: There is also the pension backdating cost. If you have a long-serving executive who receives a pay rise, the pension cost of backdating that for the whole of their service dwarves the pay rise. If you have somebody who is a senior officer in local government who becomes a chief executive, the pension cost can run into millions.

Mr Johnson: This is a major distortion and does need to be addressed. My experience is when senior pay decisions are made that particular point is not taken fully into account which is problematic. Some of the moves that have taken place in the public sector, for example the Civil Service move into a clear average pension scheme rather than a final salary one, is a very a helpful move because it overcomes the effect that Peter has just described.

Q174 David Heyes: Can I pick up a point from earlier, particularly with David Evans, the performance-related pay bonuses for top managers, particularly in the NHS, is an example. The idea that the top managers can be motivated to deliver in their organisation with a performance package, is that not at odds with the fact that it is a collegiate organisation a hospital or a health trust? It depends on the efforts of all those who work there and not just of the top managers. They set the style and lead and so on but the actual delivery of the quality is in the hands of potentially thousands of people who do not seem to have that kind of incentive. How does that sit? Are there not inbuilt tensions in that around jealousies and so on?

Mr Evans: That is the view of the NHS and that is why compared to other parts of the public sector, and certainly the private sector, very few trust chief executives are actually on performance-related pay. It is probably less than 1 in 5, about 18% of people who are actually on performance-related pay bonuses and the level of bonus is actually quite modest. It would be 5% or 6% of salary and I think that reflects that view. There is even unease amongst some executive directors and some chief executives for precisely the reasons you said. They do not feel that they are solely responsible for the performance of the organisation. It is the culture of the NHS that it is a team effort.

Q175 David Heyes: We heard Peter Boreham say that he is advising remuneration committees of foundation hospitals on how they should have a variable compensation package. I presume by that you mean performance bonus for the top managers.

Mr Boreham: Your point is very well made. The boards we work with would be much happier if they could implement something that works across the organisation. The reality is most of their employees are on national agreements under Agenda for Change so it is much harder to do anything with the broad employee population. You have to bolt it on and put your costs up whereas at executive level they have more freedom to do things with people's remuneration. Most of those I worked with would like to do something broader but national pay setting makes it harder for them to do that. The point about working together is an important one. In the public sector when we think about performance-related pay we tend to think of the performance of the individual. Personally I am much happier if it is about the performance of the organisation. I think about the work we have been doing for a Mental Health Trust on incentives. In reality the director of nursing, the medical director, the director who is responsible for the linkages with the local authority for managing people in the community are all working together and it is difficult to say the nursing director did a great job; it is more about what did the trust as a whole deliver.

Mr Johnson: I subscribe to three points in this area and I have advocated it for many years. It is important that the philosophy, policy, strategy, whatever word you care to choose, around pay, is consistent from top to bottom and embraces the whole of the workforce. The practice will vary for different parts of the workforce but the underlying policy, in my view, should be consistent because the workforce as a whole is engaged in the work of whatever that organisation is. The second point I would make is the move we need to be making with public sector workers is towards variable pay linked to performance for the whole workforce and not just for senior people. I would not draw the conclusion because it does not apply everywhere or we do not do something at the top levels. I would come the other way around and say it is important that we have more linkage to performance of pay for everyone. Peter's observation about how that is done is a vital point. I think for many people, particularly at the front line, it is more about how the organisation has done than how they have done as an individual. The other point I would make is that one of the challenges in public sector pay is the pay structures are based around incremental progression and largely time in the job is determined by how much the individual gets paid. There are two issues here, one is that is deeply inflationary. If you look at the way pay awards are described in the public sector, they are described as being a 2% or 3% increase and then the individual is also getting progression through the pay system so they are probably coming through with 5% or 6%, sometimes 7% increases.

Q176 David Heyes: But they are getting more experience and delivering more quality.

Mr Johnson: There comes a point when the growing experience does not automatically or necessarily deliver better performance. Initially when someone is new in the job experience, and the acquisition of experience, has an important impact on their performance but it tails off, and it tails off quicker than I think the pay systems give credit for. The inflationary drive in the public sector pay systems is something that worries me a lot. The other drive in public sector pay systems about largely rewarding people for having a job rather than rewarding people for doing the job well I think gets in the way of some of the service delivery improvements that we would all like to see.

Q177 David Heyes: What do you mean by that?

Mr Johnson: If I am a junior civil servant working in the Ministry of Defence then no matter how hard I do my job and how effectively I do my job my pay is determined by the pay scale I am in and how long I have been in that pay scale. I do not have any influence as a junior civil servant on my pay because of the performance I deliver on behalf of say the Ministry of Defence. I think that is problematic.

Chairman: Interesting points all of them. We are into the last five minutes.

Q178 Mr Prentice: I think people ought to be paid by the amount of happiness they generate and I want to see happy organisations. When you are talking about performance, just listening to the exchange there I thought what kind of performance is being measured. The Chief Executive in the Staffordshire NHS Trust probably got performance payment for bringing the deficit down and yet we know after everything that happened there that there were not enough matrons and not enough consultants. Perhaps we are rewarding people for the wrong kind of performance. I was very taken by what Mr Davidson said about parallel or shadow remuneration committees. I was interested in what the other three of you thought about that. Mr Davidson said there are not enough young people with a different kind of life experience to go on remuneration committees. Why do we not establish shadow remuneration committees to advise the real remuneration committee? Do you think that is completely fanciful or do you think that is something we ought to give more consideration to?

Mr Boreham: I think we have slightly misrepresented Mr Davidson. What he was talking about is giving people the opportunity to get used to be being non-executive directors. That may include remuneration but it is not going to be the main part of what they are doing. It is giving people the experience and developing a cadre of potential non-executive directors in the future that can be used within the public service. We made a very similar recommendation to a government department we did some work for recently. It was a very useful proposition. Remuneration would be part of that but I do not think we want to be setting up layers and layers of remuneration committees trying to second guess each other's decisions.

Q179 Mr Prentice: Did I misrepresent you?

Mr Davidson: My point was the creation of shadow boards as a whole within which remuneration committees and audit committees might be there too. I would personally advocate shadow boards, and individual shadowing particularly, in all they do.

Q180 Mr Prentice: Who would be on these shadow boards? Could I get on the shadow board of the Royal Bank of Scotland which is a State-owned bank now? I have very firm views about remuneration and banking.

Mr Boreham: I am sure UKFI[3] would be delighted to hear them.

Mr Johnson: I think a shadow process is a good process for giving people exposure, helping them to develop experience and widening mechanisms for doing that but I think you still have to be really clear about where accountability sits. I do not think the shadow board proposition is about somehow fuzzing or sharing accountability. Accountability still sits with the remuneration committee rather than the shadow remuneration committee.

Q181 Kelvin Hopkins: I am worried about this word "performance". My experience, certainly in the Health Service in my region, is that performance is always about money and cost and not about lives and care. We have moved from a world where we were paid a salary and we were expected to work because we were driven by the public service ethos, public responsibility and a sense of pride in what we did. We are now moving towards a world where, if you do it well, you get a bit of extra cash, and if you save a bit in the process you get a bit more cash. This is not the world I want to live in. I may be old fashioned but the world I used to know where you got a salary for the job and we were expected to do it well and had a pride in doing it for that salary seems to have been marginalised.

Mr Boreham: The point is that salaries then were much smaller. If we were paying NHS chief executives £100,000 rather than £200,000 then your argument would have weight. If we are paying them £200,000, I believe some of that should be linked to performance.

Mr Johnson: It is very important to be clear about how one defines performance. The best performance management systems I have seen in both the public and the private sector are much more rounded than you describe in terms of what elements of performance people are being held to account for. It is the quality of delivery as well as the cost of delivery and not just the cost. Secondly, I think the good systems also focus very strongly on the behaviour of executives and how they do their job, not just the performance they deliver but the manner in which they do it and whether they deliver on it and do their jobs in a way that is consistent with the values of the organisation.

Q182 Mr Prentice: That is a key point. In the private sector we are told that people require huge sums of money to deliver shareholder value. What does shareholder value mean? It means regular big dividends to the shareholders but maybe there are other considerations like retaining profit, putting it into research and developing products for the future.

Mr Boreham: Shareholder value should include all of those things. Shareholder value is a forward looking measure. If you have a business that is failing to invest in the future, failing to manage its people properly and develop talent, failing to interact properly with customers then the analysts in the City of London will write down the value of that share, shareholder value will be destroyed and those people will not receive those bonuses.

Q183 Chairman: On your point, people not sharing the values of the organisation and therefore getting marked down in performance terms, who decides that?

Mr Johnson: The senior team of an organisation would work through what the values of the organisation are and then that becomes the requirement. The line manager is an important part of the judgment about whether an individual has delivered to that. If you are talking about the chief executive, then you are looking at the Chair and the board as key players in determining whether the chief executive has not only delivered but has exemplified the values of the organisation.

Mr Boreham: In the private sector, which is where I do most of my work, the key role of the remuneration committee is about performance management of the organisation and the chief executive.

Q184 Chairman: We could do much more in the public sector. We know the Government is taking a lot more interest in these issues at the moment which

[3] UK Financial Investments Limited

is the point about transparency at local government level and so on. It said it is going to do a first-principles review of remuneration packages for NDPB chief executives. In very short terms, is this a good development?

Mr Boreham: Yes, because NDPB chief executives and non-executives' pay is all over the place. If you were trying to look at how it should be, it should be related to how big is this organisation, how complicated, to what level do we need commercial experience in those kinds of roles and to what extent has responsibility been devolved to those bodies but when you track those factors you cannot translate that into the differentials of pay.

Mr Davidson: I would agree with that totally based on the experience of going in and talking to different departments about the organisation's response. There is no coherence of any kind.

Mr Johnson: I fully agree. My only qualification is I would like to see that kind of work done more broadly.

Q185 Chairman: Could I finish by asking that in your memorandum to us[4] you gave us some very helpful recommendations particularly those on governance. I want to see if we have assent to these sorts of things. "An individual review body should advise on the reward principles and provide guidance to national and local government as appropriate for the different parts of the public sector." The proposition is an independent review body to lay down the principles for different areas.

Mr Boreham: If it was principles-based rather than laying down particular salaries, that would be very helpful. In the private sector we have the Association of British Insurers and the National Association of Pension Funds playing exactly that role.

Q186 Chairman: So there is assent to that. "Executive reward decisions, policy and application to individuals should be made through remuneration committees that include independent members and report to ministers or authority members or boards as appropriate to each organisation." That model of remuneration committee of independent members, is that something that people assent to?

[4] Ev 81

Mr Boreham: Yes.

Chairman: I think we have agreed on this already: "Executive rewards should be published in annual reports by analogy with requirements for public companies." We have said yes to that. Is there anything you wanted to say to us?

Q187 Mr Prentice: Did you feel uncomfortable disclosing your salaries to us today?

Mr Johnson: I was quite careful not to say precisely what my salary is from Mercer because I know Mercer prefers that information is between the organisation and the individual.

Q188 Mr Prentice: Do you think it would be better, and this is a point that Polly Toynbee made to us before, if everyone was not so uptight about what they got paid and they just put it into the public arena?

Mr Boreham: I do not think there is a public interest in what we as private employees of private organisations are paid. There is public interest legitimately in people who are running public organisations. There is a legitimate public interest in people who are running listed companies with diverse boards of shareholders. In a privately owned company with private employees, no, I do not think my pay is in the public interest.

Q189 Chairman: Is there anything we have not asked?

Mr Davidson: I would hope that in the eventual report you produce that you will look at the whole supply issue of candidates which I do feel is a significant factor in the reflection on salaries. It may too easily get missed.

Mr Johnson: I endorse that. The recruitment, the development, the management and the retention of talent is the fundamental driver for how the public sector thinks about reward.

Mr Boreham: It is a perceived shortage of talent that drives salaries up in both the public and private sector and some of it, as Hamish has suggested, is perceived rather than real.

Chairman: That is a very important point for us. We have had some vigorous exchange but I am afraid that is what we do. You have responded extremely well. Could I say you have been extremely helpful to us and it is a pleasure to talk to people who actually know what they are talking about. Thank you very much indeed.

Thursday 18 June 2009

Members present

Dr Tony Wright, in the Chair

Mr David Burrowes
Paul Flynn
David Heyes
Kelvin Hopkins
Julie Morgan
Mr Gordon Prentice
Mr Charles Walker

Witnesses: **Ms Millie Banerjee**, Chair, Remuneration Committee, Ofcom, **Mr Tim Melville-Ross**, Chair, Higher Education Funding Council for England and **Dr Anne Wright**, Chair, National Lottery Commission, gave evidence.

Q190 Chairman: Let me welcome our witnesses—can I call you our guests—this morning. It is very nice to see you. We have Millie Banerjee, who is Chair of Ofcom's Remuneration Committee, Tim Melville-Ross, who is Chair of the Higher Education Funding Council and Dr Anne Wright, who is Chair of the National Lottery Commission, amongst the many other things that you all do but that is why we have you here. As you know, the Committee is interested in looking at the whole issue of executive pay in the public sector. Our inquiries eventually brought us to you, because we have not yet got our minds around the whole issue of public bodies and how remuneration takes place there, and you are all centrally involved in that. I do not know if any or all of you would like to say anything just by way of introduction or whether you would like us to ask some questions.
Ms Banerjee: We are happy to go to questions.

Q191 Chairman: Let me ask you in a general sense. One of the things that concerns us is whether there is enough consistency in the way that remuneration is set across the public sector. I particularly want to ask you in terms of your knowledge of a variety of public bodies whether you think it happens in a coherent way or whether it is all a bit of a mess. Who wants to start on that?
Mr Melville-Ross: I think there is a degree of consistency, if I can just say a word or two about the process for determining senior salaries, and I will be very specific about the process for determining the salary of the Chief Executive of the Higher Education Funding Council. The internal process is that there is a small Remuneration Committee, consisting of members of the Board, which I chair, but clearly, there is considerable involvement on the part of the relevant government department in determining the package for the Chief Executive. The work that we do to come up with the right sort of figure is really quite detailed in terms of what you might call the market analysis that we carry out. That market analysis actually runs across both private and public sectors, on the argument that there is a certain amount of interplay between the two. So whilst, bluntly, in the public sector not a lot of importance is attached to the pay of private-sector chief executives, nevertheless, it is part of the process that an external consultancy would go through. There were really two main lines of reasoning that produced the package that is now paid. One was by reference to the public sector as a whole, NDPBs, senior civil servants and so on, with, if you like, a bit of job evaluation going on as part of the process, trying to establish exactly where in, say, a civil service hierarchy the chief executive of a particular NDPB would sit. That was one part of the process. The other part is, given the sectoral specialism, the likelihood—not the certainty but the likelihood—that any CEO of HEFCE[1] would have come from the sector, in other words, would have been or would go on to be a university vice-chancellor, quite clearly, the packages of university vice-chancellors were very much taken into account in determining the package of the individual. Against that background, yes, there is quite a considerable degree of relative judgement made. That maybe sounds a little more scientific than it actually is. Nevertheless, it is a process that we go through and arrive at broadly the right conclusion, which we then, as I say, discuss with the Department.

Q192 Chairman: That is helpful. Can I ask the others to come in.
Ms Banerjee: Our process is somewhat different. We set our own salaries because we are an independent regulator and Parliament set us up to be separate from interference of any kind. Our consistency is derived from looking at a number of inputs. We look at where public sector pay is going because that is one of our inputs, and we are publicly funded to 60% of our funding, 40% being from industry. We also look at what is happening in the sector that we regulate. However, we could never attempt to pay anything like the salaries that are paid in the sector that we regulate but we do need to understand where the packages are going in those sectors so that we know how to recruit the best possible skills. The other point about consistency I think it is important to look at, Chairman, is what are we talking about. Your own terms of reference make it very clear that you are looking not just at pay but at pay and benefits. In comparing salaries sometimes we forget the sort of benefits that go with them. If you look at a defined benefit scheme, the final salary scheme that, for instance, civil servants are paid, which we in Ofcom do not offer and we made it very clear from the beginning that we would not offer to new

[1] Higher Education Funding Council for England

entrants, the value of that final salary scheme is actually quite significant. We have done some work and if you look at buying an equivalent money purchase scheme, it is a significant amount of money which should be seen as a premium or a discount, depending which way you look at it, to the salary we offer. To give you an example, if you are paid £60,000 a year and you have a pension scheme that, say, pays out in 15 years, a money purchase scheme today would cost you £50,000 a year to buy. So when you are looking at salaries, you cannot be looking at £60,000; you have to be looking at £60,000 plus £50,000. So in looking at consistencies, I think we do need to look at the whole package.

Dr Wright: I would also say in my experience there is a good deal of consistency both in relation to what I would call governance—that is, the way remuneration committees work –and also in relation to the kind of advice and guidance that is available to public bodies. As far as the National Lottery Commission is concerned, what I would add to what the others have said in relation to setting the pay of staff is that we do respond on an annual basis to a pay remit, which has to be returned to the sponsor department, so the decisions are always made within that framework, which has the sight of the sponsor department and which we take care is within the budget looking ahead to the forthcoming year. As far as the Chief Executive's salary is concerned, again, the most recent contract provided for the Chief Executive of the Commission was again subject to external review, a study of market data, we looked particularly at the median across a range of public sector, including our particular sector, possibly regulators and so on, and the contract of employment was drawn up in the light of that. So it is both external advice, looking across the piece, and looking at whatever benchmark data is available to us.

Q193 Chairman: So when you read all these stories in the press about what are seen to be stratospheric public sector salaries with lots of noughts on the end, and people say, "How can this be?" your answer is that you look at the sector you are in, you look at the market for the job and that is the outturn?

Dr Wright: Yes, absolutely, and I would add to that in the case of the Lottery Commission, the regulator, in recent years we have had particular regard to the challenges, and I think that is the important thing; the challenges of the job and the challenges of delivery. Most public bodies, in my experience, are concerned with delivery, quite rightly, and looking to results, so the nature of the task is particularly important. For us, for example, over the last four years we have been conducting the competition for the third licence to run the lottery, which finally came into being on 1 February this year, and we have particular challenges and we need particular skills to address that. Overall, I would say also there is consistency but, looking at the stratospheric salaries you have referred to, I think the point that was made about the specialist sectors is really important. As far as we are concerned, the tasks that the Lottery Commission has to undertake are very much concerned with propriety, audit, vetting and so on, a lot of compliance functions, financial and regulatory, and so we are looking to particular skills to carry that out throughout the organisation.

Q194 Chairman: When someone just looks at the figures—and we have this army of researchers who do this for us, of course—and I look at our organisations and the variation in what you are paying your people, the figures for 2007–08 are: Mark Harris, the Chief Executive of the National Lottery Commission, received £106,717 in salary, £27,070 in pension contributions and £16,008 in bonus, which is 15% of salary. If we turn to David Eastwood, who is the Chief Executive of HEFCE, he received £204,771 in salary, including a bonus payment of up to 10% and £26,148 in pension contributions. Finally, if we turn to Ed Richards, the Chief Executive of Ofcom, he received total remuneration of £417,581 including a bonus of 20% of his salary, other benefits and pension contribution. So we have Ed Richards of Ofcom earning twice as much as David Eastwood of HEFCE, who in turn earns twice as much as Mark Harris of the National Lottery. Is this because one is better than the other? Is it because one organisation is more important than the other? Is it because one job, one activity, is more crucial? What is the logic behind this?

Ms Banerjee: First of all, if I can just step back for a moment, when Ofcom was put in place we thought very carefully about what sort of packages we would give. In 2004 there were five regulators which were then collapsed into one. If you add up the salaries of the individual five regulators in 2004, it was £810,000, and two of those people were in a final salary scheme. That is where we started from. Of course, we were never going to pay that much because we were going to consolidate and be a very efficient regulator. Also what we have looked at is this point about final salary schemes. We have not offered a final salary scheme so Ed Richards' basic salary you have to take into account is not linked to a final salary scheme, so there is a premium that we would have had to pay in order to make sure that he does get the appropriate pension contributions. Much more important than that, you do have to look at the job that he is required to do, to build on what my colleague Dr Wright has said. We regulate an industry which is worth £50 billion. It is a very active, ferociously competitive, very litigious environment. Even yesterday you saw the launch of the *Digital Britain* report. Every single chapter of that has some kind of Ofcom involvement. In order to operate in that industry, you need big regulators with very competent people at the top who are able to eyeball the equally competent and ferocious people who lead some of the institutions that we regulate. So you have to have people who are able to deal with it. Having said that, we are not paying private-sector salaries, we are not trying to match the salaries of the people we regulate, but we do have to have a reasonable package to attract the right kind of skills, and also we have to incentivise the people to deliver what they have delivered. So in

Ofcom we have gone from 1,100 people down to 850 people since we were born; our costs are 17% lower than they were when we were born; this is the fifth year we have delivered a less than RPI[2] budget; our reputation is generally good—our stakeholders do not all love us but that is what happens when you regulate people. We do have to reflect that. On top of that, Chairman, what we also have to reflect is our understanding of what is happening out in the marketplace when we are trying to recruit people. Even as I speak, even with the recession, we are trying to recruit a senior person reporting to Ed Richards, and people are falling off the shortlist because we simply cannot afford them. We do not aim to match the sector that we regulate but we do have to have a sensible package to attract the right kind of people to do the job that we are requiring these people to do.

Q195 Chairman: We are simple folk on humble salaries and we find all these figures to be quite starry-eyed. Is it the case that you are saying that you have to pay over £400,000 a year so that someone can, as you say, "eyeball" the private sector and that nobody would do this for £200,000 a year?
Ms Banerjee: Could I just make the point first of all that it is not pay; it is the total package, and the nature of the package is very important because you do need to look at the component that is particularly to do with pension, and the security of a final salary pension is absolutely enormous; anybody who has that realises that and that is a pension for life. So it is not just pay, and yes, I am saying that we need to recruit the right kind of people to do the job that they are required to do. One of the things that is very obvious from our history is that small regulators find it quite difficult to regulate these very large institutions and to have a relationship with them that is businesslike and to deliver what they are required to deliver. When you are a regulator, particularly speaking about Ofcom, it is not enough just to be able to exercise your powers; you have to also be influential, energetic, and intellectually competent to deal with very large companies. We have BSkyB, we regulate part of the BBC, we regulate BT, we regulate Vodafone, we regulator O_2—we have to have people who are able to do that job in the way that it requires to be done.

Q196 Chairman: So you are all paying the minimum amount that you can pay to get the kind of people that you need in the sectors that you operate in—is that the position?
Ms Banerjee: I believe we have to be competitive. People do not come to work in Ofcom because of the pay. They do not. In fact, we have people coming to work in Ofcom, some of our specialist lawyers, for instance, competition lawyers, who we need, who actually take a cut in pay. They do not stay long; they stay about five years but they like to come to an organisation like Ofcom as part of their career development.

Q197 Chairman: This is contradictory now, is it not? You cannot say people do not come to Ofcom because of the pay, having just argued that you have to pay the amount to get the kind of people that you need.
Ms Banerjee: What I was trying to say about that is they would be able to claim more total benefit if they were working outside Ofcom.

Q198 Chairman: Yes, but if they do not come for the pay, why are we paying them these enormous salaries?
Ms Banerjee: No, I think that the benefits we have to give are the minimum that they have to have before we can attract them. People do not just go to work for the benefits they get. You know that. It is the total package: the pay, the pension, the benefits, the environment in which they work, plus the job that they do. A lot of people come to us because they want to work in the public sector for a period in their lives, and we encourage them, and they make their own decisions on that total package but if we did not pay what we pay, I do not think we would get the right kind of people. I have been there for five years and I am very convinced from the data that we collect regularly, as our colleagues have said, we look very carefully at what is happening in the marketplace because we know we cannot match the private-sector salaries.

Q199 Mr Prentice: Although the private sector will pay a premium for people who have worked at Ofcom, inside the regulator, seeing how the machinery works. When they leave Ofcom after two or three years, they will be able to walk into the private sector and get a stratospheric salary.
Ms Banerjee: They do not actually. They are not actually allowed to walk into the private sector. Every one of our senior executives has a contract where we isolate them for varying periods of time, sometimes for a whole 12 months, when they are not allowed to work with any company which has ever had a licence from Ofcom or is about to apply for a licence to Ofcom. Like any other job, anybody who changes jobs takes their experience of the job they have done before to the next job that they do, and we encourage that because it is a healthy change-around of talent between the private sector and the public sector.
Mr Melville-Ross: I just wanted to give you a slightly different angle on this. Clearly, there is an issue implicit in the way you asked your question that all these organisations are similar, and they are not. Clearly, what Ofcom does, what HEFCE does, what the Lottery Commission do are all very different things. Just to illustrate the point, by narrowing the debate down to universities, which is where we by and large, if you like, fish for our chief executive talent, just in what you might think of as a fairly homogenous group, the range of salaries for vice-chancellors is, roughly speaking, the range that you have just described, from just over £100,000 to well over £400,000. You might say, "They are doing the same sort of job so why is there so much difference?" The reality is that universities are very different

[2] Retail Price Index

places. The individual on over £400,000 runs Imperial College, which is a world-class institution, hugely complex, hugely challenging. The point I wanted to drive home is the practical issues that bodies like the board of HEFCE have to address. You talked about David Eastwood just now and his package. David has recently moved on to become the Vice-Chancellor of the University of Birmingham. One of the principal reasons is pay. He was under-remunerated in relation to the market in which he operates and so he left HEFCE and is now at Birmingham on a considerably larger package. When we recruited his replacement, who was the Vice-Chancellor of the University of Dundee, the process of determining his salary was broadly along the lines of what I described earlier but then we ran into the major difficulty that the figure that resulted from that was significantly less than what he was already earning, both in terms of his salary as Vice-Chancellor of Dundee and other non-executive appointments, which obviously you have to take account of: why should someone move for less? You may not like it but that is the way the market is and we have to operate in that market. That is as true of the public sector as it is of the private. Just a little extra colour on how we end up at the figures that we do.

Dr Wright: Could I pick up one of the points you made in relation to that variation in relation to the Lottery Commission? You mentioned the 10% bonus figure and I think it was 20% in that year that you quoted for us. I just wanted to say for the benefit of information of the Committee that in relation to the Lottery Commission—and I cannot speak for others –the only payment that can be made to the Chief Executive on an annual basis once that initial salary is set is technically a bonus payment, of which a part can be consolidated, and that too is solely on the basis of performance, and there is quite strict regime there. The reason for the 20%, I would add, is that when a new contract was put in place in 2005, we took account of the revised guidance from the sponsor department raising the 15% bonus payment to 20% in the year, and we did that very specifically, not just to go to the maximum but because we were mindful of the particular challenges that faced the Commission and our desire for retention, to give the Remuneration Committee a greater discretion in being able to reward performance during those crucial years.

Q200 Mr Prentice: I have this delicious quote from you, Tim, from *The Independent* when you were looking back at your time at the Institute of Directors. You said you regarded it as a personal failure that you did not make more of an issue about the—and I am quoting here—"disproportionately high rewards that go to people who don't deserve them." Then you go on to say, "I'm talking about extremely high reward packages for people running organisations which actually in the overall scheme of things are not that difficult to run." Now, you are the universities man, and you told us that the spectrum goes from £100,000 to £400,000. Do you have a little pecking order of universities in the United Kingdom, the ones that are quite difficult to run—University College—and the ones that are easy to run?

Mr Melville-Ross: Yes, I do but first of all, the comments that you have managed to find that I made some years ago were very much with reference to the private sector.

Q201 Mr Prentice: I am interested in the organisations that are difficult to run. That is the point.

Mr Melville-Ross: Sure, absolutely. Part of the point though was to do with difficulty in terms of creating real wealth, and I have no difficulty—just to talk about the private sector for one moment and then I will come back to universities—with the proposition that if you run huge risks, you create an organisation, you build it in such a way that you transform the lives of many of the people, substantial rewards can flow from that and I am very happy with that. What I am much less happy about is people who have relatively straightforward jobs running relatively straightforward organisations being paid packages which are quite similar to those sometimes which really, truly entrepreneurial individuals rightly enjoy. Now let us make that point with reference to universities. Clearly, there is, on the face of it, a similarity between one university and another but if you look into the difference between the major research-based universities, like Imperial College, Oxford, Cambridge, King's College London, UCL and so on, they are extremely complex, very difficult to run, in terms of having to work in a world-leading research environment, competing with United States institutions for talent, including the Vice-Chancellor of Cambridge, for example, who came directly from one of the Ivy League universities—I forget which.

Q202 Chairman: Yale.

Mr Melville-Ross: Yale, thank you. There is this market point which is very relevant but it is also to do with complexity, with international regard, with being an almost unique individual in a very talented environment, and by no stretch of the imagination would all the universities in the UK aspire to that or claim that level of complexity or international excellence. They do a good job but of a fundamentally different kind, and so the rewards are commensurately lower.

Q203 Mr Prentice: What I take from that is that these huge salaries that are eye-watering—£400,000, £500,000, £600,000, £800,000 a year—go to people running organisations that are inherently quite difficult to run.

Mr Melville-Ross: Yes.

Q204 Mr Prentice: And people should not get these sky-high salaries if they are running an organisation that can comfortably coast along?

Mr Melville-Ross: Fair enough, yes.

Q205 Chairman: You do not see in the job advertisements, do you, "This is a relatively easy organisation to run"? It is always "challenging", so people do not quite get the truth about this.
Mr Melville-Ross: I think they do but I would not be influenced by that kind of advertisement. Essentially, people pretty soon find out just how complex an organisation is to run.

Q206 David Heyes: In this hierarchy then Anne Wright's organisation is very easy to run, yours is quite difficult and Millie's is phenomenally complicated.
Mr Melville-Ross: Since I made the point, I am making one of a number of points which determine how the salaries are set. It is an important point but there are a great many others.

Q207 David Heyes: The reality is that all of your organisations are equally demanding, I would guess. You operate in different sectors, you deliver different functions, but the demands on your chief executives, your top executives, are of a very similar nature.
Ms Banerjee: I do not think I agree with that. I think different organisations are required to do different tasks. Different organisations are at different times in their life cycles and that has to be reflected. I think complexity does vary and your context also varies. As I said earlier, our organisation operates in a very complex context. It is not a stable environment. It is fast-moving, it is changing every day. So I do not think they are the same and if you look at the public sector as a whole, just to broaden the debate, there is a whole range of institutions now in the public sector which are away from central government because in the last 10–12 years lots of tasks have been moved out of the general public sector. I have been around the public sector and my own experience is that there are big differences. I have chaired smaller organisations which have a relatively narrow remit, a small number of staff, a relatively small budget—they are still inherently interesting to run but they are not quite as complex as a much larger organisation.

Q208 David Heyes: Let me pursue that point a little further with you. Would it help in your difficult job of devising salary structures, reward systems, if there were an independent pay review body that could cover senior executives throughout the public sector, including your bodies? Would that be progress?
Ms Banerjee: That is an interesting suggestion. I can see that people would feel that there might be some benefit in that but I would see some practical difficulties. This really goes back to the point I have just made, which is that there is such a range of organisations that you might find that the pay review body ends up making very generalist recommendations which actually do not fit any organisations and become slightly defeating when you get dysfunctional behaviour of trying to find packages around what the review body says to make sure that you can attract the right kind of people. I think that might become very difficult because the public sector is so diverse.
Dr Wright: I do have direct experience of two pay review bodies. I chair the schoolteachers' one and before that for six years I was a member of the Armed Forces pay review body. I would like to say that I admire greatly the good practice of review bodies and I think there is a lot of good practice that perhaps could be learnt and built on across the public sector but on the whole, I probably would agree that a single pay review body across the public sector, or even, let us say, for chief executives of NDPBs, which might be another thing that might be looked at, is probably undesirable and impractical really, too complex. The cycle of decisions is such that it would be a huge amount of work, would probably cost a great deal, and I think there is a value that one has to recognise of governance and remuneration committees which are close to the challenge and close to the market. Having said that, I think that there might well be scope, as I say, for learning lessons from that, particularly in relation to the kind of data and evidence that is provided, which could be helpful, I think, perhaps benchmarking data, something like that, across sectors.
Mr Melville-Ross: I would simply say firstly, I would endorse what my colleagues have said but I would go on to say that, certainly as far as HEFCE is concerned, we do take account of the Senior Salaries Review Board recommendations. You will remember the very first answer I gave when I was talking about the different influences that are brought to bear in determining the kind of package that we come up with.

Q209 David Heyes: The SSRB[3] has a fairly narrow remit, does it not? What I am suggesting is something that would have a much broader scope.
Mr Melville-Ross: The broader it is, the more complex the issues you have to address. We have to recognise that, I am afraid. We may not like it but we are operating, even in the public sector, in a market environment and these influences have to be taken into account. The more you, in a sense, with a small "l", legislate for pay, the more difficult it is to accommodate some of the influences which I referred to earlier.

Q210 David Heyes: Could there be a role for such a body if it were advisory, if it were to do, as you have suggested, the benchmarking, for instance, that would help to bring some more order and more balance to these very disparate decisions that you need to make?
Dr Wright: I would think so. It might not be a body as we know, the pay review bodies at the moment. It might be, for example, the pay review bodies, in my view are very well served by the independent secretariat in the Office of Manpower Economics, which provides a good deal of the data that we use. It might be possible—I do not know—to have something like that or to extend that so that there

[3] Senior Salaries Review Body

was this co-ordinated data available, perhaps in families of bodies. These are different types of bodies, different markets, regulators and so on. Perhaps there might be something there that would help us, to add to the support and advice we have already.
Ms Banerjee: We do take account of data that is available when we set our salaries. One of the pieces of data we look at is what the pay review bodies are saying. This year, for instance, the Civil Service review body is suggesting, I think, a 1.2% rise. Our rise is nil. So yes, we have taken account of what they said but we have decided independently that nobody is going to get a pay rise this year in Ofcom, and that is the decision we have made. But we do take account of the data and we also, of course, look at what is happening in the marketplace that we regulate.

Q211 Mr Walker: Bonuses. I have always been in jobs where the bonus was keeping the job if you performed, but, clearly, I have worked in a different environment to most of you. David Eastwood, Chief Executive of HEFCE, received a bonus payment of up to 10%. Is that a cap of 10%?
Mr Melville-Ross: Yes.

Q212 Mr Walker: How many times have you not paid the bonus?
Mr Melville-Ross: He was paid it twice because he was with the organisation just for two years.

Q213 Mr Walker: What I think we need to establish is, are these real bonuses or are these just part of the salary and they are always paid bonuses? You will always pay the bonus, will you not?
Mr Melville-Ross: No, no, absolutely not. The maximum is 10%, for a start. Secondly, there is a sliding scale of achievement, outstanding achievement, excellent achievement, and so on, down, and a whole series of objectives which I as Chair of the organisation have to evaluate the Chief Executive's performance against. For example, quite a lot of this is inevitably subjective because a lot of his objectives are to do with relationships with government departments, relationships with the sector and so on, but we work as hard as we can to introduce quantified objectives, the organisation's key performance indicators, into the way the bonus is determined and, if those are not achieved, and if there is a judgement that the qualitative elements of the bonus scheme have not been achieved, David would not have got anything like 10%.

Q214 Mr Walker: How long has HEFCE been around for?
Mr Melville-Ross: Since the early 1990s. It was the successor to the University Grants Commission.

Q215 Mr Walker: How long have bonuses been around for?
Mr Melville-Ross: I do not know.

Q216 Mr Walker: I think what would be very helpful is if you could provide the Committee with a note showing for each year what the maximum bonus that could be earned was and how much of that bonus was paid, because then we can ascertain whether it really is a bonus or just part of the salary. Can I ask the same question of you: how many times, in your experience of Ofcom, has the maximum or near-maximum bonus not been achieved?
Ms Banerjee: I cannot tell you offhand but I can certainly give you a note to that effect. My memory is that there were several. We have only been there for five years and there have been times when we have not paid the maximum but, as Tim has said, we have a very robust process on setting the objectives and then reviewing the objectives, and we make an independent decision on whether the bonus is achieved or not and we do not make a payment of the bonus on the basis that it is part of the salary. This year none of our senior team are getting a bonus because they themselves said that they would like to forego their bonus.

Q217 Mr Walker: This year is a special year because we have a recession. I understand that as soon as the leader of my party made a statement on pay, you froze pay at Ofcom. It was shortly after. I am sure it was just a coincidence.
Ms Banerjee: No, we decided that nobody in Ofcom would get a pay rise this year as part of a Remuneration Committee exercise taking into account what was happening in our industry and taking into account affordability and all the other issues that we normally do.

Q218 Mr Walker: I think what we actually need from all three witnesses is the details of your bonus scheme and how it is paid out, because I think there is genuine concern. The public are concerned about lots of things, and we are not in a very strong position as Members of Parliament to be gruelling anyone at the moment but there is concern over bonus payments because many bonus payments look like they are contractual as opposed to genuinely being earned for outstanding performance. Mr Melville-Ross, you have experience of the City—is that right? Do you have a finance/City background or have I got that totally wrong?
Mr Melville-Ross: Go on anyway.

Q219 Mr Walker: We talk about the war for talent and my particular bugbear is the Financial Services Authority. They are stuffed with money, absolutely gorged with money. Hector Sants—and I could be wrong—is on over £600,000, astronomical sums of money, yet he and his senior management team presided over the most monumental disaster imaginable. It was not all their fault but, quite frankly, were they playing croquet for the year before this blew up? What were they doing to earn their salary? We tell the taxpayer you have to pay to get the best people, and we pay £600,000, which is, by anybody's standards, a vast sum of money, and they are AWOL. What is your view on that?
Mr Melville-Ross: I am not quite sure what this has to do with public sector pay.

Q220 Mr Walker: The FSA is public sector.
Mr Melville-Ross: I will give you a response: because the FSA has to operate very much in the private sector. The senior people employed by the FSA are from the banking sector.

Q221 Mr Walker: So does Ofcom, and to Ofcom's credit, you have not had a disaster yet, like the FSA.
Mr Melville-Ross: I suddenly feel as though I am defending the FSA, which I am not here to do. Let me just give you what I hope is a helpful response. You say by anybody's standards £600,000 is a lot of money. By City standards it is not, I have to tell you. The sorts of packages that have been enjoyed by people running banks, who have had even more disastrous experiences than the FSA itself, are vastly greater than that. The FSA does have a monumentally difficult job. I am Chairman of an insurance company, so I have a lot of experience of the FSA, and it is a fiendishly difficult role to perform. I acknowledge that a lot of mistakes were made in many respects, but in response to that the FSA is working hard to improve its capability, and they do need very good people. If you do not employ the best people in the FSA you will—

Q222 Mr Walker: But we clearly have not employed the best people in the FSA. This is the concern. We are told we have to pay these sums of money to employ the best people, as you said to the Chairman, but it is obvious to any outside observer that we have not. We could have had this disaster paying someone £65,000, to be perfectly honest. Where does it end? Shall we pay the next Chief Executive of the FSA £6 million, or £60 million or £3 million? You can see the concerns.
Mr Melville-Ross: I understand your concern. I do not feel that I am in a position to offer a solution, other than to make the point that it is a very complex organisation. For goodness' sake, do not encourage the organisation to pay less for talent right now because it really needs that talent to go through the process of reform that Lord Turner has suggested.

Q223 Mr Walker: A final question: what is the definition of talent? We were told we had very talented people, for example, running the banking sector. This is why they were paid £20 million. Their talent was to ultimately rack up debt, buy duff financial instruments and destroy the financial services sector. So really, there is not a link between remuneration and talent.
Mr Melville-Ross: There probably is not. My definition of talent would be that it has two ingredients: one is intellect—these issues are complex and the individuals concerned really do need to be very bright to understand what is going on.

Q224 Mr Walker: But they did not; they did not understand what was in the packages.
Mr Melville-Ross: Partly that, but partly the wrong judgements were made as well. That is my other ingredient. Everybody around this table knows perfectly well how difficult it is to judge the judgement of another individual, and the past is no necessary guide to the future, although, interestingly, if you look into the research about the most effective ways of identifying the right kind of talent, past experience is the best guide that you will get but clearly, the process we have just been through internationally is an experience that nobody has ever been through before.

Q225 Mr Walker: I am being a bit cheeky here. Boots taking on Mr Hornby of Halifax—is that a good decision, bearing in mind his track record? You said that past performance was a good guide to future performance, so Boots obviously has high ambitions for its shareholders.
Mr Melville-Ross: It must do. They have made a judgement and all I can offer is that people learn from these mistakes. That is what is going on.

Q226 Mr Prentice: I want to ask Millie Banerjee about Royal Mail. You know something about the Royal Mail because you used to be Chair of Postwatch. Adam Crozier gets over £3 million a year, I think, including about £2 million, I read, under the company's long-term incentive plan. I have a cutting from the *Guardian* in front of me from 2008 and you are quoted. You were talking about a particularly difficult period in the Royal Mail when, you told the *Guardian*, "Customer expectations were definitely not exceeded –indeed, were not met." That was you as the Chair of Postwatch. What happened to Adam Crozier's salary and package? Was that poor performance reflected in a reduction in bonuses or any diminution in his salary package? I ask you because you were intimately involved in this and you will be able to tell me.
Ms Banerjee: I am not intimately and I was not intimately involved in setting Mr Crozier's salary or anybody else's salary in Royal Mail and reviewing the package and understanding what they were being paid for, but I was the Chairman of the organisation that was set up to review consumer service in the postal sector. My observation would be that Royal Mail is a very difficult and complex organisation to run. It is very difficult, and the difficulty stems from the fact that it has not invested in transformation of the business for 15 or 20 years, to be honest with you. The nature of the job, to transform the business, is quite special. My observation, which you read out—and I still believe that, having left that organisation—is that the consumers in Royal Mail do not get the best deal that they are likely to get, and that is because of a combination of factors, which are to do with the way the organisation is structured, the lack of investment in the organisation, the fact that there is not really very effective competition in the residential sector, and the whole nature of things. I personally believe that Royal Mail needs to change, if that is the question.

Q227 Mr Prentice: I do not want to take us down a blind alley and the Chairman will not let me but my question is a very simple one. The UCW and the other people would say Crozier has got £700 million from the Government to modernise the Royal Mail and he has been sitting on this money. It has not been spent. The simple question is this: if an organisation is performing inadequately, performing poorly, surely that should be reflected in the remuneration package of the person at the top, and in the case of Royal Mail it has not been reflected?

Ms Banerjee: In principle, that must be true. Taking you back to the Ofcom experience that I have, we look very carefully at how we are performing, not just from our internal results but we look at what our stakeholders say about us and that is taken into account. In principle, you have to be right that an organisation does have to reflect in its salary structure, in its benefit structure, its performance and the way its performance is perceived by the people that it is performing for. In principle, that must be right.

Q228 Julie Morgan: Very quickly, I wanted to ask about pay for board members in the public sector and what you think about the levels of pay that are given and whether that restricts the type of person who actually is on those boards. Tim Melville-Ross, I do not think you take anything, do you, in your role?

Mr Melville-Ross: That is correct, yes.

Q229 Julie Morgan: Could you give me your views swiftly on this, please?

Ms Banerjee: Yes. I do get paid.

Mr Melville-Ross: Sorry, do you mind if I interrupt? I choose not to take a salary. There is a fee of £46,000 payable to the Chair of the Higher Education Funding Council because it is a two-day-a-week role. Because I am well remunerated for many of the other things I do, I choose to give it to charity but you must not infer from that that it is not necessary to pay people to carry out public service like this. My own personal circumstance is such that I am prepared to do that. I used to chair Investors In People, which did not carry a fee. The problem with not paying a fee is that, by definition, you limit the pool of talent in which you can fish. So in principle I do favour board members of NDPBs, public bodies generally, being paid. The difficult question then is at what level. I would certainly not advocate anything like private-sector levels. £46,000 is a great deal less than a private sector chairman of any substantial organisation would receive, and the £5,000 fee which is paid to individual board members is likewise much less than you would see in the private sector. There is that argument about having the opportunity to draw talent from a wider pool. There is also one final point—and I am sorry to interrupt—that I remember as a Chief Executive once my Chair was not paid and that had the effect of discouraging me from making full use of the Chairman, or it might have done; he was not the kind of individual who would be ungenerous with his time but there is a sense that if someone is doing a job over a period of time, they should be paid for it.

Ms Banerjee: I would very much support much of what Tim has said. I think you framed your question around recruitment problems. Our experience in Ofcom is that actually pay has not been a problem. We pay our people adequately. We have a variety of governance structures, not just a board; we have several advisory committees and so on. There is a structure of packages. The main difficulty is around, in our case, because we are a regulator, conflict of interest. We have to find people who understand the environment that we regulate, but we cannot have them coming into Ofcom very soon after they have come out of that industry because we would then have potentially a conflict of interests. That has been our main problem in recruitment, not pay. Most of the people we have on our Board would earn a lot more on a daily rate than what Ofcom is able to pay. I myself earned last year something like £56,000 for two and a bit days in Ofcom but I do other things and I work virtually full-time. Most people do the job because they want to do it as a non-executive in the public sector, not because they are going to get rich from it.

Dr Wright: I have a variety of roles, and this constitutes my main income, apart from a teacher's pension. I have a salary for the Lottery Commission, which I think was just over £60,000 last year. It is important to say that that is calibrated against an equivalent *per diem* rate and it is for 9.5 days input a month. I think that is quite a considerable amount. During the period we have looked at however it was important to be able to give, if necessary, 18 days a month to that because of the nature of the competition. I think that was a good way of looking at that. However, the commissioners are paid on a daily rate, which I think is currently £284 per day. There are differences, not just in the way people are paid, salary or *per diem*, but also in relation to the kind of input. For example, on the pay review bodies the members are paid, I think, £300 per day and Chair £350 per day, and that is in relation to activities, meetings and visits. So there are differences. I have had previous jobs in the past. I was a Board member of English Partnerships, which paid a salary of £12,000 for three days a month. So there is a variety. For me, I would say I think there are two points I have come to a conclusion on over 20 years' experience of these kinds of bodies, some remunerated and some not. I think that where bodies are delivering—and I know we have talked about whether it is an easy job—they have big challenges; we oversee the running of the lottery, the return of money to good causes, £1.2 billion a year, which we account for to the nearest penny, for example. I think it is important for accountability of Chairs that it is recognised that it is a serious job and that it is remunerated appropriately. I think it is important to do that. That is one point. The second point has already been made. We do want greater diversity in our public bodies. I think we are seeing more of that, right across age, background, ethnicity, and so on, and particularly people from small businesses, for example, at an earlier stage in their career. Sometimes it can be very difficult for people to make a contribution as fully as they would like to in public service if there is not an appropriate level of remuneration. So I think it is valuable for those bodies to be remunerated. It is important, of course, to get it right. We would want to bear in mind that for a great many public bodies, for example, across the DCMS which is the sponsor Department for the Lottery Commission, these are trusts and people are not remunerated; they fulfil the role of trustees.

Q230 Julie Morgan: One thing that does strike me is that people tend to collect positions and have more than one in the public sector. I am always a bit curious about that.

Dr Wright: May I answer that? I have had a career as an executive and chief executive and vice-chancellor indeed, and have moved on from that to this next stage of my career. I regard it as a privilege but also I think I can make a contribution to more than one public body, because you can bring some experience across the piece, as we have been talking about this morning. For me, this is something which I take seriously as a role, and indeed chairing a public body I think is a particular privilege and a particular task. One finds that one can bring that experience to bear.

Ms Banerjee: I just wanted to add to what Dr Wright was saying that when I apply for a job, I consider very carefully what skills I can bring and I apply when I think I can make a contribution and transfer my skills. For instance, I have just joined as a board member a primary care trust in Newham in London and, after discussion with them, it seemed to me that I could bring something to them around customer care, consumer care, patient care, how to manage that, how to manage the front end of it. I do it because I think I could bring some skills and, as Anne says, it is a privilege to be able to do that at my age, because I have gone past the executive life and I have a different kind of life now.

Mr Melville-Ross: One very quick point as tailpiece to this discussion. The interesting thing about being involved in several different organisations—and I chair HEFCE, an engineering company, an insurance company and a real estate company—they could not be more different but the issues that come up in the boardroom are very similar, and being able to draw on experience from private and public sector, different industries and so on, I find invaluable, so my colleagues tell me.

Q231 Paul Flynn: We have been given the general impression from this morning's session that all is right with the world, and it is not all right with the world. If somebody is a social worker, they have to take judgements, life or death decisions, on a daily basis, very difficult judgements, but earning £20,000, £25,000 a year, and the gap between their pay and the people you are talking about is getting greater all the time; the gulf between people on average pay and on top pay grows wider. I can understand that Beethoven and Shakespeare are unique. I find it very difficult to have someone sitting behind a desk taking the decisions you describe, Ms Banerjee, eyeballing the public sector and all these other decisions. Do you really believe that someone getting these top salaries is really 20 or 30 times more valuable or doing work that is 20 or 30 times more beneficial than anyone else, or is it just a question that these people who get the top salaries have a special talent for inflating their own salaries?

Mr Melville-Ross: Forgive me. You should not infer from what we have said, and indeed what we have not said, that all is well with the world. I certainly do not think it is and I have not said that. We have to deal with the world as we find it and apply as much logic as we can. You were talking earlier about something I said when I left the IoD,[4] and I am concerned about the level of reward. I think it is disproportionate in the private sector. I am much less worried about the public sector because at least there is a greater degree of rationality. You can argue that it is still not fair but these things are hugely difficult to judge. Please do not attribute the words "all is well with the world" in terms of pay at senior level to me. I do not believe it is.

Ms Banerjee: I would never suggest that all is well with the world. One might need to think about whether social workers are appropriately paid for the risks they take. I am not in a position to comment on that but, in terms of life and death salary, we regulate a £50 billion industry which is absolutely fundamental to the citizens of this country and fundamental to the way the economy is run. Those are important and complex jobs and they have to be remunerated appropriately if we are going to manage to keep the health of the industry in the way we would like to.

Dr Wright: May I answer quickly also, if I may? It is a very important question. We obviously need to consider whether pay levels are right, right across the piece. As far as the Lottery Commission is concerned, we are mainly professional staff. Our lowest paid member of staff is on £20,000 but the average is about £38,000. The Chief Executive, as you heard, is on £106,000, so it is not a huge ratio. In terms of decisions, I can give an example of one decision that the Commission, led by the Chief Executive with ourselves, had to make and that was a decision on the award of a licence to Camelot for the next period and, as we said in public, the outcome of that will be that we estimate that there will be increased returns for good causes of between £60 million and £100 million per annum for the period of the licence at regular sales levels. That is an example where there is a real impact of a decision.

Q232 Chairman: Tim, you talked about the disproportionate levels in the private sector but is it not the truth, and the reason for looking at this kind of issue now, is that what has happened is that the disproportionate private sector salaries have run off into the public sector; there has been this inflation that has carried across into the public sector, for the reasons that Millie gives, because you say in the last 10 years or so much of government has been hived off, has been put into market-facing situations, and in doing that, the argument appears that therefore we have to market-facing salaries.

[4] Institute of Directors

Ms Banerjee: Chairman, I said repeatedly that, certainly in Ofcom's experience, we cannot afford to pay market-facing salaries. We do not pay market-facing salaries.

Q233 Chairman: No, but you say you have to get into that area because of the work that you are doing.
Ms Banerjee: No, we have to take into account what a very talented individual, who has to run an organisation like Ofcom, could actually generate in terms of his package for his lifetime and we have to find a way of making the package attractive to him, and part of it is the benefit package but part of it is that many people come to work in Ofcom because that is where they want to be. They want to make a contribution to the citizens of this country, they want to make a contribution to the public sector, so it is a package. If we were able to pay market salaries, we would be paying a lot more but that is not what we want to do.
Chairman: We have had a good run through the issues. I hope there is nothing you wanted to say to us that you have not had a chance to say. For us, it has given us a good flavour of the kind of context in which organisations like yours, of a varied kind, are having to take these decisions about remuneration. We are very grateful to you for coming along and talking to us about that. Thank you very much indeed.

Witnesses: **Mr Bill Cockburn**, Chairman, **Mr Mike Langley**, Member and **Mr Keith Masson**, Director of Secretariat, Senior Salaries Review Body, gave evidence.

Q234 Chairman: Let us move into the second half and welcome our witnesses, Bill Cockburn, Mike Langley and Keith Masson, all from the Senior Salaries Review Body. We are grateful to you for coming along and helping us with our inquiries. You know what we are about. Do you want to say anything to us by way of introduction?
Mr Cockburn: A couple of points, if I may, Chairman. First of all, the Senior Salaries Review Body has been going for nearly 40 years, and the principal groups that we look at are the Senior Civil Service, the judiciary, the senior military and the senior National Health Service managers, and from time to time we have the joy of looking at MPs' and Lords' remuneration and expenses. We help the devolved assemblies with their salaries, if they invite us to do so. We look at them individually, not as an amorphous mass, and we have sub-committees within the SSRB that look at these various groupings, because they are different, but we can bring that out in discussion.

Q235 Chairman: The key question, which is the one that came up in the previous session, is here we have SSRB doing this work in certain defined areas but not doing it across the wider public sector, and the question, obviously, on the table is would it make sense to have, if not the SSRB, somebody doing a wider exercise, at least at the level of principle and approach across the wider public sector? What would be your take on that?
Mr Cockburn: We represent about 8,000 people across these various groupings that are mentioned, which is a small number in relation to the vast employment in the areas that they represent and the costs that they incur. Generally speaking, we come in when we are invited to do so. Broadly speaking, the groups we represent are not subject to collective pay bargaining, as it is for other people. So, in the absence of pay bargaining, having a body like ours, which is independent of government, which is evidence-based, which is regarded, generally speaking, as fair and objective in the way that we do our things, gives faith to those that rely on us for their remuneration and is fair to employers, who reckon that what we recommend is fairly based. As to whether you extend the system, you could do. For example, taking the most senior National Health Service managers is a recent addition to our group. So we are available and we have the skills to do so, but there are other processes for determining pay elsewhere. I would say, finally, I do not think we would be well placed to be deciding on the pay of individuals, say, like local authority chief executives. We are, I think, better placed to take a group of people and determine pay scales for them.
Mr Langley: I think that is right. Essentially we look after homogenous groups of employees. You heard from the three people who were represented here this morning. They are not only different individuals but they have different skills, and they have different pay markets, and we have, in a sense, homogeneous pay markets across the piece of those.

Q236 Chairman: So if someone came along with a proposition that chief executives across a range of public bodies should have their salaries advised on by the SSRB or a similar body, you would find that a too daunting prospect, would you, because of the complexity of the different markets?
Mr Langley: Yes, I think it would be too difficult, too disparate a field.

Q237 Chairman: How, then, are we to get to grips with the underlying issue of, as it were, what is happening to top pay in the public sector generally? We have got a partial answer through the SSRB system in those areas, but we have not got an answer in this wider sector. Do we say it is too difficult, we cannot do it, or find another mechanism for doing it?
Mr Cockburn: I do not think we would say it is too difficult. We have not been asked to do so. In these other cases they probably have remuneration committees that are set up to do it, whereas for the groups that we represent, generally speaking, there are not remuneration committees. In some cases there are in the Health Service, and they are guided by what we say. I guess it is for the employers to

decide what is best in their circumstances. We are not resistant to this; we are here to respond. For example, the permanent secretaries in Whitehall are subject to a remuneration committee, which I chair, so I chair this and I advise, and Mike is also a member of this now. So we advise the Cabinet Secretary, the Permanent Secretary of the Treasury, the Foreign Office, who form The Troika, but look at the 40 or so permanent secretaries, and we go through the evidence to advise on what pay and bonus would be appropriate in these cases, although, as you know, all the permanent secretaries have waived their bonuses for the last financial year.

Q238 Mr Burrowes: I am sure you do an admirable job, but would you reflect on the fact that, effectively, your job is limited and, in many ways, toothless in terms of your independent recommendations often going the way of a political whim and not being followed through and not being enforced? Firstly, in terms of limited, would you reflect perhaps on those that came to give evidence earlier today that in many ways the role they play, in terms of public pay, is the fox guarding the chicken coop: it is hard to resist not taking the most you can when the gate is wide open? Effectively, that is what many of them are doing as chairmen of their remuneration committees, and the call overseas, as well as perhaps here, is for a ramped up role that you could play with greater authority, almost a public pay Tsar coming before us with a clear mandate to police cost, to contain them and perhaps quite radically to look to reduce costs as well? Would you want to look for a way that you can have much more teeth in terms of the enforcement of your recommendations and, in terms of those recommendations to ministers, when they are not following through a way that they would be much more mandated to accept your recommendations?
Mr Cockburn: I would not accept that we are as toothless as you suggest. It is true that our reports are recommendations to the Government, and it is always up to the Government to decide whether or not to accept our recommendations. However, our reports are public and the Government, if they turn them down (which they do not do very often) then, to Parliament, would explain why it is that they have done this. They tend to be harder on their own pay rather than on the pay elsewhere. If we look over the history, say, since 1997, the Government have only rejected our pay recommendations once, and that was actually the last one in 2009. There are special circumstances, and actually the Government reduced the pay award to below the level that they had recommended to us that we follow. In all other cases through the years, they have either accepted, without question, what we have done or, on occasions, they have staged the awards. They have done that on a number of occasions and they have explained why they have done this, but, generally speaking, there is a pre-disposition to accept what we say.

Q239 Mr Burrowes: Have you ever felt under any political pressure?
Mr Cockburn: No. We are an evidence-based body, so the Government give us economic evidence. All the other consultees give us their evidence in writing and they appear before us, as well, orally. There are 10 of us on the body. We consider all the evidence and we then make our recommendations and publish them, and there is great transparency.

Q240 Mr Burrowes: Those are made in draft form, first of all.
Mr Cockburn: We do not clear the report. We do not negotiate the report with government before it is issued.

Q241 Mr Burrowes: There is no communication that can lead in any way to a change of recommendation.
Mr Cockburn: The only situation is a factual check of some of the things that we have said with officials, not with senior ministers. Ministers have no role in this. The civil servants will check that what we have said in evidence is factually correct but, having said that, our recommendations are our own, they are transparent and we are accountable for them.

Q242 Mr Burrowes: On a separate point, is there not confusion of you being able to make recommendations, for example, in the National Health Service for primary care trust chairmen but not for NHS trust chairmen? Is that not a confusion that needs to be remedied?
Mr Langley: I think the answer to that is, yes. This is a remit we got in September, 24 months ago, to look at the senior managers in the Health Service, but it was a very specific remit. It only covered primary care trusts, ambulance trusts, special health authorities and strategic health authorities, it did not cover foundation trusts or acute trusts, and that, clearly, is a difficulty for us because, particularly when we get evidence from the senior managers themselves, they say, "You are looking after our pay, but what about the pay of people in jobs which we might compete for, or might like to come from, which are not controlled?" We find that a bit of a difficulty, but that is our remit. We were not given the remit by the Government or by the Minister of Health for the other trusts, and we cannot argue about that.

Q243 Mr Prentice: Do you think pay in foundation trusts, those parts of the Health Service that are not regulated or supervised by you, has gone out of kilter? Are chief executives in foundation trusts getting paid too much, as far as you are concerned, and does it have a knock-on effect on the regulated part of the NHS, that people in those areas that you look at are just drifting over to the foundation trusts where salaries are set by their own remuneration bodies?
Mr Langley: I think there is a value judgment in "too much". If you are asking me, "Are they getting paid more?", the answer is, "Yes, they are." Because the pay is set independently by remuneration committees on foundation trusts and they have control of their own budget, therefore their own pay budget, they are able to pay salaries which have been

higher than have typically been paid to National Health Service managers. If the pay is drifting upwards for the foundations trusts, the issue then is how do the bodies that we look after retain, attract and recruit people who might otherwise go into these other jobs? If the pay differential is too much, then we are going to lose them.

Q244 Mr Prentice: Is it too wide at the moment?
Mr Langley: It varies, is the answer, because foundation trusts, coming back to the previous question, are set individually by individual trusts. There is some data, but it depends on the size of them.

Q245 Mr Prentice: You spend your entire life looking at these things. You must be monitoring what is happening in the foundation trust sector.
Mr Cockburn: Mr Prentice, maybe I could add, up to now we have not seen evidence of a great drift from the bodies we represent into the foundation trusts. The Department of Health, of course, look at this and they give us evidence, and they have said to us that they are content to have the foundation trusts outside this and the other bodies with us. There was a worry, in theory, that you would get a tremendous drift, or brain-drain, from one to the other, but that does not appear to have come through in evidence yet. This is something that needs to be kept an eye on, but up to now it has not caused an obstruction, as it were.

Q246 Mr Prentice: Would you like to see all NHS organisations brought under your umbrella, leaving all the politics of foundation trusts and all that to one side, just as a way of regulating things more coherently, I suppose? We are talking about one organisation, the National Health Service, with lots of different families, but it is the same health body. Why cannot they all be under your umbrella? Do you think they should be under your umbrella?
Mr Cockburn: First of all, if you take the groups that we looked at, I can see an argument for saying should all the public sector be under one great body which pontificates on what the rate should be overall.

Q247 Mr Prentice: I am asking about the NHS, not all.
Mr Cockburn: Right. The argument might have some similarity. Taking our groups, even with our groups, which do not represent the whole of the public sector, we have taken the view that it still makes sense to break them up into discrete groups and have sub-committees looking at them, because they are different: the market considerations are different; there are different skills and expertise needed. You have got fundamental differences, like the senior military. As they recruit exclusively from their own ranks, one has to make sure that there is not a distortion in the pay lower down, because you would not be able to resource the generals and the admirals and the air-marshals. So you have to make sure that the pay overall is sufficiently healthy to attract and retain people of the skills and leadership needed to do these extraordinarily difficult jobs. So it is also in the judiciary. That is why we need to look at them. You cannot apply a simplistic, across the board value judgment to them. Equally, in the Health Service, which is colossal, the Health Service is bigger than all the rest put together, therefore, within that there may be, and certainly the health department tell us that there are, differences and you have to fine tune these.

Q248 Mr Prentice: I was not entirely convinced by that answer.
Mr Langley: I think your premise to take the politics out of it is difficult to accept. You cannot. There are politics in deciding whether foundation trusts should sit on their own in terms of determining their own remuneration.

Q249 Mr Prentice: I am just inviting you to get above the politics.
Mr Cockburn: We have the capability to do it.
Mr Langley: If that were possible, it would certainly be, simply because if you look at the rest of the National Health Service, as you imply, they have common base counts and all the agenda for change and the nurses and the doctors.

Q250 Mr Prentice: Where we are, all hospital trusts are on the way to becoming foundation trusts—that is, across the NHS. We are talking about hundreds of thousands of people employed by foundation trusts, and each foundation trust will be able to set the pay of their so-called top people.
Mr Langley: Yes.

Q251 Mr Prentice: The whole pay system in the National Health Service is deliberately being fractured and atomised by the Government as a deliberate act of policy. It is not just one little bit of the Health Service; this is happening across the Health Service. All I am asking you, I suppose, as I asked the people we had before the committee last week, is whether that is a better model than the one that you currently operate. Is it a better model to have each hospital trust setting their pay for the top people, so-called, rather than you?
Mr Cockburn: I think what we say is we have the capability to do that, I believe, and it is not for us to dictate how pay should be determined. We are here and we are open to invitations to do these things, and we apply our skills to doing it. For example, in Northern Ireland they have undertaken a major reorganisation of the Health Service and they have invited us (and they were not obliged to do so) to look at the pay structure of all the top most senior people in the Health Service, and, in fact, we have just completed the assignment, under Mike's chairmanship, and we are about to publish our report. Here is a good example of the Northern Ireland authorities coming to the view that they needed to do this pay review, we were well placed to do it and they invited us to do it. We did not have to force our way in; we were invited because of our reputation, abilities and track record.

Q252 David Heyes: There was a time when we all believed that job evaluation was the solution to these kinds of difficulties. I guess, from what you have said so far, they are still very much central to your approach.
Mr Cockburn: We have a number of evidential sources: the departments, the people that are represented, and we take written evidence, oral evidence, we meet groups of people, so we take their views. We also, on occasion, hire consultants to provide specialist support, whether it is job evaluation, whether it is pension, actuarial expertise if we are doing a review of pensions, as we are doing for MPs right now, and so we do use this. It is not mechanistic. We take it into account and we weigh the arguments along with everybody else. None of that stuff is a precise science, there are different points of view, but it can be quite good guidance to us in forming a view as to the relative importance of some jobs as against others.

Q253 David Heyes: That was a feature of your approach to the NHS review that you conducted recently. It was job evaluation based, was it not?
Mr Langley: What we said in our comments of the NHS senior managers was that there was no correlation between pay and job size. If you look at the structure of how the very senior managers in the National Health Service are paid in their remit group, the directors who report to the chief executive are paid a percentage of his or her salary, and there were some various bands between 55 and 75% attached to job titles, but there was no reference to the size of the job in relation to the job title. The individuals who we took evidence from said, "My job is bigger than that job over there, and yet I am paid the same", and there was no evidence to say whether that was right or wrong. What we said was we thought there ought to be some job sizing within the NHS senior managers to determine whether they were correct or not, and the Department of Health recommended an independent review by a guy called Alan Wright, who accepted that job evaluation, some sort of job sizing, was necessary and the Department of Health accepted that evidence and recommendation and they are going to do that next year.

Q254 David Heyes: That seems to me to be a very sensible approach to these problems, that kind of flexible attitude to it, which brings me back to a point that has been made several times now. Why not possibly broaden the remit of the SSRB or create a similar body that has a wider remit right across the public sector: because it could bring this kind of intelligence and pragmatism to advising each individual foundation trust, in the case of the NHS, on how they should be benchmarking?
Mr Langley: It is actually that, in that if you have a coherent body that deals with pay across the piece, then you are going to have a coherent pay structure. If you are going to have disparate bodies, you are going to have disparate structures, which is back to your point.

Q255 David Heyes: That is a vote in favour. What is it a vote in favour of? Broadening your remit or creating a new body that will address these wider issues?
Mr Cockburn: I just repeat that I think it is a real option. I think you have a body that has got the capabilities and the experience over a long period of time in doing this kind of thing, but I think it is for others to say, given that there are other options, what is the best option for their circumstances.

Q256 David Heyes: You are very cautious about promoting your organisation and what it does. You have given us a very helpful written piece of evidence. It really is interesting and constructive. You are very modest.
Mr Cockburn: We are very modest.

Q257 David Heyes: It is not for the SSRB to judge whether its evidence produced the right results. In several places you say, "It is for others to judge us." Come on, this is your opportunity to promote yourself.
Mr Cockburn: I think our track record is quite good. Maybe I can clarify a point I made earlier about whether our recommendations are recommendations that others can accept. There is one exception to this, and that is on MPs' pay. It has already been decided that our body actually determines what the annual increase in MPs' pay is. A resolution of the House was passed last year. We calculate the increase by reference to 15 other bodies that we look at, and we then notify the Speaker of what the increase is. There is no discussion, there is no debate in Parliament and there is no voting. There is an example, I think, where we can actually be trusted to do something about this. In the first year of a new Parliament we would undertake a more fundamental review of MPs' pay again on the same basis I have just described, and, thereafter, there would be annual up-rating for the remainder of that Parliament. There was a change in the circumstance where it has become, if you like, a little bit more executive than advisory.
Mr Langley: One of our recommendations they did accept.

Q258 Mr Prentice: Were you aware of all the expenses and allowances that MPs were charging?
Mr Cockburn: Indeed, we were, and we have made some feisty recommendations in the past which the House have chosen not to follow. In the past there has been a cherry-picking of some of the things that we have said and a rejection of some of the reforms that we recommended.

Q259 Mr Prentice: This is an issue which is radioactive, if you understand.
Mr Cockburn: Indeed.

Q260 Mr Prentice: But you would like to see a situation where you, or the Kelly Committee, would just look at MPs' remuneration in the round and that MPs should just accept it?

Mr Cockburn: Of course, you have the sovereign power to do anything, so you could always take it back if you were not satisfied, but I think what we have said is that when it comes to remuneration matters, say in determining pay, the pensions (in consultation with the pension trustees), the rate (whatever is the new expenses regime), insofar as maybe from time to time they need to be priced and up-rated, our body would be well placed to do something like that. I think that we are standing ready with some past experience to help constructively with the reforms that we know you are most anxious to have introduced.

Q261 Chairman: Some people are arguing that the allowance issue somehow has to be compressed into the pay issue. Surely the pay issue and the allowance issue are just separate issues?
Mr Cockburn: I think they are separate issues. Yes, they are; absolutely. We have said in the past on MPs' pay (and it is almost politically very difficult to increase it, as we have found over the years), in our view, MPs' pay is 10 to 15% lower than it should be.

Q262 Mr Prentice: Could you repeat that please!
Mr Cockburn: It has been 10 to 15% lower, in our view, and we have said that in our reports. Indeed, in our past two reports we recommended increases of £650 a year on top of the other increases, which the MPs rejected. There is a degree of underpayment, in our view, but it is always going to be difficult to address this under the present arrangement.
Chairman: We want to be nice to you, of course, but let us resist the temptation to go further down that route.

Q263 Julie Morgan: I was interested in your body. It is made up of 10 people, is it?
Mr Cockburn: There are 10 of us who are members.

Q264 Julie Morgan: What sort of range of experience and diversity do those 10 have?
Mr Cockburn: Mike has long experience of senior remuneration management and advice in the private sector. We have professors who are labour economists; we have businessmen, people who have been HR directors in companies. I have been the chief executive in a number of companies. It is a good mix of skills and expertise coming together.

Q265 Julie Morgan: Are there any women?
Mr Cockburn: Actually, we do not have any women currently. We had two, and they came to the end of their term. We have a very open process of recruitment, supervised by a representative of the Office of the Commissioner for Public Appointments, who for the last exercise was a woman. It happened in this case that they were all men who were successful. It was not our choice; that was the way it came out. This is a meritocracy.

Q266 Julie Morgan: In terms of the way you make decisions, do you often have disagreements within the decision-making process where you would strongly disagree about what you are going to recommend?
Mr Langley: We have had robust discussions.
Mr Cockburn: Yes, vigorously. We have not ever had to take it to a vote. We have not had a minority report. We have managed to try to get a consensus, and we work hard to get that. We listen very carefully to all the points that are made and they are different but, in the end, I think there is a general acceptance that what is important is to produce a report at the end of the day which is published, it is a Command Paper laid before Parliament, and really we have a duty to come up with a set of proposals that are soundly based, evidence-based and well argued, and that is what we have tried to do over the years.

Q267 Paul Flynn: There are 194 public workers who receive higher salaries than the Prime Minister. In Wales there are, I believe, six people working in the Welsh Assembly who receive higher salaries than the First Minister there. I had an extraordinary answer from someone sitting here a short while ago about why this should be and was this a reasonable situation to be in. Presumably the Prime Minister would have the highest salary of all. The answer I had back was that being Prime Minister was a springboard for getting a far better retirement salary, which is a very interesting concept. Do you not think this is proof that things have got out of kilter when this pressure is on to raise salaries and the people involved, like the head hunters, are contributing to this and there is a whole process going on which is inevitably leading to the gap between average salaries and top salaries becoming greater, and the example of the Prime Minister's salary is a striking one?
Mr Cockburn: Yes, that is something that, in fact, we have commented on in the past. I think it is fair to say that the political world seems to be subject to its own salary discount by virtue of what you do. For example, we looked at how the Prime Minister's salary and MPs' salaries compare with other countries and we produced this. In fact, you do very well by international comparisons, and when we looked at this, the Prime Minister's pay was second only to the President of the United States. He was paid more than all the other heads of government. The position may have changed since then because of the value of the pound. So that seems to be a feature. Certainly it is the case that if you look at, say, what permanent secretaries get paid, permanent secretaries get paid more than the Prime Minister and other people in the public sector, and in response to the argument, "Should we not use the Prime Minister's salary as the cap, so nobody should get paid more than that?", we think that that would not be a good idea. Besides which, there is the risk that because Prime Ministers are always very parsimonious about their own increases, that could have an adverse effect on others if there was a

linkage, as the Prime Minister's pay is not objectively linked to the value of his job in relation to comparators because there is this political overlay, at the end of the day, in the decision.

Q268 Paul Flynn: This is an argument that goes back to the time of Plato about the guardians. These people who are taking these decisions should have the public interests at heart, but the position now is we have created a situation where people taking jobs as top civil servants, generals, admirals, prime ministers, ministers, are in such a position that their retirement job—their job when they leave the service—is likely to be more attractive to them than the job they are actually doing in what should be the top jobs. There is a grave danger that they can distort their decision-making in order to feather their nest for a future retirement job, and they could be taking the wrong decisions while they are taking those jobs. Does it not distort the whole idea of having people in these top salaries who should be disinterested from their personal salaries and certainly free from any temptation to take decisions that are going to give them rewards for the future?
Mr Langley: The answer to that hypothesis is you should pay them a lot more so they do not need to take those amounts of money when they retire, like Tim Melville-Ross, who said he does not need to be paid as Chairman of his education trust because he has earned lots of money in the private sector.

Q269 Paul Flynn: I know what the position was before, but I think it is unique. There are nearly 200 people who are earning more than the Prime Minister. The Prime Minister's should surely be the top salary.
Mr Langley: Yes, but I think this comes to the heart of one of the issues. It is about pay markets, and what we are looking at is evidence of how you attract and retain people. There is a market for MPs, people in Parliament, which is hierarchical, in terms of salary, starting with an MP and moving up through a committee chairman, minister and then to the Prime Minister, and the issue about MPs' pay is how can you attract the right people to come and do the job? Well, give them the right sort of salary for that. If you look at judges, for example, the pay market for judges: they are senior lawyers, barristers and solicitors, many of whom earn a million pounds a year; so there are different pay markets. The military has its own pay market. As we discussed earlier, the NHS has a disparate pay market.

Q270 Paul Flynn: In the military, the less risk you have the greater your salary. The further you go up the pay scale in the military, the less likely you are to be killed on the battlefield. There does seem to be a distinction there.
Mr Cockburn: Try and tell that to the two and three stars who come before us.

Q271 Paul Flynn: I would be delighted to.
Mr Cockburn: Can I make a general point about our approach to pay? I have explained how we get various sources of evidence and so on but, I think, when it comes to the point, our approach to pay is to pay at the lower end of what would be justified and, in fact, our view is to pay the minimum necessary to get people of the right quality in a sustainable position. Having regard to recruitment and retention, these are the key indicators that we look at in forming a view at the end of the day; so we do not consciously set out to pay a premium. In some cases there are premium payments made where, notwithstanding the pay ranges that we recommend, the Civil Service might go and recruit somebody with particular skills and pay them a much higher salary. For example, in the Olympics, the team that are managing the top Olympics programme are paid well ahead of the going rates, but there is a special case for this because you are looking for people of outstanding ability and expertise to do this. Outside our normal recruitment there is scope for going into the market and paying a premium.

Q272 Paul Flynn: Is there evidence that these stratospheric salaries produce better outcomes in the decisions that they make? We had a striking example in the financial services sector from Charles Walker, and there are many other examples, but is there real proof there that the more you pay the better decisions you will have?
Mr Cockburn: Of course those who employ them have to take that view. If you take the Civil Service (and I will come on to the incentive schemes), there are for these people sometimes very specific objectives and targets that they have to achieve to justify their recruitment for the kind of jobs they are in. We have been quite vocal, in general, about looking carefully at the number of times the Civil Service find the need to go outside the pay systems and recruit more highly paid people. This is a big issue currently, the dual market, if you like, and certainly a lot of civil servants internally, who have come up through the system, are unhappy with the fact that there are other people coming from outside into senior positions who get paid a lot more, and we have challenged this and we have pushed hard to say that this has got to be objectively based, it has got to be evidence-based, it has got to be transparent. In fact we track it and we push the Cabinet Secretary when he comes to see us, and we are very glad to see in the Normington review of the Senior Civil Service there is an acceptance that there has got to be greater rigor and transparency there and there has got to be greater fairness in treating the internal applicant for a job more equally than the external applicant for the same job. In the past it was rather biased. We have been pushing. We are not saying everybody should be paid at the high level, because there has always got to be scope for going to the outside market and paying the premium rates, but in doing so it has got to be fair, transparent and objectively based.
Mr Langley: To answer your question precisely, nobody makes bad decisions because they are badly paid. They leave if they are badly paid.
Chairman: Good point.

Q273 Kelvin Hopkins: My apologies for being late. There is one particular question I am concerned about, and that is on performance-related pay. I hope it has not been covered already. In your paper submitted to us before the meeting *Executive Pay in the Public Sector*, written evidence by SSRB, you question "is the balance right between executive pay and benefits such as bonuses?" Pensions sit on one side but, as regards bonuses and PRP, do you think that balance is right, because, I may say, I am deeply sceptical about PRP?
Mr Cockburn: We are unashamedly in support of incentive performance bonuses. We support it through our own background of having seen it work and, also, the concept of having a higher proportion of variable pay which is performance-based, we think, is a good situation, as a general statement. Having said that, we think that there is considerable scope for improvement in the way things are organised. Bonuses for the senior civil servants, on average last year were 8.6%, and these are awarded according to the appraisals and assessments of the individuals, and they range from nothing to 15%, roughly, which would be a top award, but within the average of the 8.6. We have urged the Cabinet Secretary and his team to make sure that they can improve the quality and rigor of the system that gives rise to these payments, and, indeed, in our last report we did not recommend an increase in the bonus pot for the year ahead, 2009, so it remains at 8.6. Although, in principle, the Government's intention is that that should rise to 10% on average by 2011 but, actually, there was no increase last year. For the permanent secretaries, they have the same bonus scheme of 8.6%, and we make awards on an individual permanent secretary basis according to their performance, and that is backed up by evidence but, as I mentioned earlier, the permanent secretaries this year have waived their bonuses in respect of last year in recognition of the current position that we are in.

Q274 Kelvin Hopkins: There are many areas in the private sector and, indeed, the public sector where there are no bonuses, no PRP: people are paid a salary and expected to do the job, and they do it to the best of their ability, accepting that salary. There is even an argument in some areas, even in the private sector, that PRP is a demoralising factor, and actually in some areas of the private sector they found that productivity went down with PRP instead of up.
Mr Cockburn: People have different points of view, in general. There is a lot of support for this, and certainly it was put to us in evidence and backed up by the Normington Review, that the principle of performance-related pay is a good one and one, in fact, that they want to introduce further. In fact, not only are there the bonus arrangements within the Civil Service, which by private sector standards are quite modest, to be honest the average bonus payments for the Civil Service was something like six and a half thousand, whereas the average in the private sector was 35,000. There is quite a big spread of payments there. That is the reality, but the intention is to make it more rigorous, to make it more meaningful, and not only is the bonus subject to performance but the basic pay itself is performance-based. Just to explain, in the Senior Civil Service there are four categories of performance, and people are allocated to these four categories: the bottom category, which has got five to 10% in it, do not get any pay increase and the higher ends would get more. So even the base pay is related to performance, all within the average pay budget, which we determine overall.

Q275 Kelvin Hopkins: I am afraid it looks to me, and I think to many other people as well, that there are people in the bonus culture environment who are just scratching each other's backs and rewarding each other with bonuses: "We live in the bonus culture, so we will make sure that other people get bonuses as well." Someone with average earnings of £23,000 a year looks at this and feels resentful, because they do not get such bonuses. If there was simply a salary for the job and they had to do the best job possible within their salary, average earners would understand that.
Mr Langley: There are various jobs at that sort of level that get piece rates and get bonuses for productivity, and all sorts of other things like that which are very similar, but I think actually the issue about bonuses is how is the objective setting done? What is the bonus for? What are you trying to achieve with it? If you have a bonus structure, does it actually achieve those things which you are seeking? That comes down to a lot of work needs to be put into objective setting.

Q276 Kelvin Hopkins: One final question. Punching out widgets on a low wage and getting piece work pay for that is one thing. When you are the chief executive of a hospital trust and you are being judged on financial performance, which is, I think, what most of them are judged on these days, the fact that rather large numbers of people are dying in that hospital and getting terrible diseases is sometimes overlooked. There has been a recent glaring example of just this, in this bonus culture driven by financial concerns.
Mr Langley: If the bonus is narrow enough just to look at financial objectives, you are absolutely right.

Q277 Chairman: Have you thought about applying the principle of performance-related pay to Members of Parliament? If you are unashamed enthusiasts for it, why not apply to it MPs as well?
Mr Cockburn: There may be some circumstances where it is not appropriate. For example, if you take the judiciary, there is a strong view and we are persuaded that that would not be an appropriate world to have performance-related pay, simply because, I think, there is a feeling that it might give rise to behaviours that would be inappropriate. Certainly there is a very strong feeling about it. That is not to say that there should not be targets for efficiency in back office activities, and so on, but the

judges themselves, I think, feel very strongly that this is not appropriate. Although we have a general enthusiasm for it, there may be differences.

Q278 Chairman: What about differential pay? A lot of MPs have other jobs as well. Why not have different pay bands: those who are full-time, those who are part-time?
Mr Cockburn: I would agree with you that this is a reasonable thing to do. For example, if you are a Member of Parliament and you are a member of the Northern Ireland Assembly, for example, your Assembly pay is abated by two-thirds, so there is already a principle of abatement if you are in receipt of an MP's pay or Assembly Member's pay. It might be that that sort of concept might have a further potential.

Q279 Mr Prentice: Do the people at the very top of organisations necessarily have the most difficult jobs? I was interested in what you were saying earlier about job sizing. A few years ago, when Andrew Turnbull was Cabinet Secretary and head of the Home Civil Service, I asked him, "What do you run?", and he said, "I do not actually run anything." So presumably he got paid his Cabinet Secretary salary for horizon scanning, and all that kind of stuff, but not actually running things. I am interested in what you mean when you say job sizing: because the number two, or the number three, or the number six in an organisation actually may be doing a more demanding job than the figurehead at the top.
Mr Cockburn: I do not think the Cabinet Secretary is exactly a figurehead, if you look at the range of his job.

Q280 Mr Prentice: I do not think he is a figurehead either.
Mr Cockburn: Quite honestly, whether you have an easy job or whether you have a hard job earlier, people might say to Sir Alex Ferguson, "You have got a really easy job because your team keeps winning", but how often is it the excellent chief executive might make an organisation feel easy and be successful simply because he is brilliant at it? We are more concerned with what is his weight of responsibility, what is his accountability?

Q281 Mr Prentice: I recall John Browne when he was Chair/Chief Executive of BP. He got paid some eye-watering sum of money, and he readily conceded that he did not need the money himself, but he got paid those millions every year because it was necessary, in the salary hierarchy, for him to get that money.
Mr Cockburn: Yes. We have not quite reached that level with our pay review remit yet, but the principle of relating salary to real responsibility, objectively based, and the other considerations that we take into account to set the tone: that individual is a leader of that whole organisation and, if his leadership is not measurable or has any influence whatsoever, he should not be there, quite frankly. That is why you are there: to provide that leadership, the drive and the motivation from all of your team to produce at the end of the day. Our people, 8,000 of them, are responsible for billions of pounds of public expenditure, so it is right that we aim to get the best quality leaders to oversee these vast sums.

Q282 Mr Prentice: We are, theoretically, responsible for some awesome spending, if you go down that road, but can I ask you about private and public sector comparability. I have in front of me a note that we got from Sir John Baker, Chair of the SSRB until 2008, and he said in his note to us that comparability is not necessary for recruitment and retention of good people in the public sector, as witnessed by the huge discrepancy there already is between private/public sector remuneration at the moment, and that is your line, is it not? You pay the most modest amount that you can get away with in order to get those famous good people you talked about a few moments ago?
Mr Cockburn: Yes. I think, in general, that is right. At the end of the day, you have got to make sure you have got people of the right ability. We are not saying you should employ second-class citizens to run the public sector. I think we have got people who, in ability terms, would be a fair match for anybody outside. We are very fortunate that we have people to apply for these jobs who are not solely and exclusively motivated by these high awards, and although you hear of these multi-million packages, very few people actually get them. Even in big private sector organisations, and I used to be a board member of BT, the vast majority of BT's executives were not earning these eye-watering amounts of money the top guys were. Therefore, if you look at the quality of the people that come in, even with the salaries that we offer, which in general terms we are proud of, we do not consciously underpay, but at the top levels there are, undoubtedly, people employed in the public sector who, if they chose, would be very marketable in the private sector.

Q283 Mr Prentice: We constantly hear this.
Mr Cockburn: It is true, and some of them do actually leave to do this. Thankfully, though, we have got a sufficient number that stay and we have got a good flow in each year of talented people. If we do need to pinpoint individual expertise, we will pay a premium rate for doing so, and we do not have to do that too often, but we have the flexibility to do it if we need to in the interests of the taxpayer and public sector performance.

Q284 Mr Prentice: One final point, if I may. You recommended a 2.8% increase for the senior military, and the judges and all the other people were getting 1.5%, something like that.
Mr Cockburn: Although we recommended 2.1.

Q285 Mr Prentice: You did.
Mr Cockburn: But they got 1.5.

Q286 Mr Prentice: Why did you recommend that 2.8% to the military: because they have got nowhere else to go, have they?

Mr Cockburn: It was a particular issue, because there were problems of differential between one star and two star. The one stars and the rest of the Army are subject to their own pay review body and the very senior military are covered by ours. What had happened was there was a compression of differentials and there was a real danger, and we saw evidence of it, that there was no pay incentive for brigadiers to become major generals because the pay difference was so—

Q287 Mr Prentice: That is surely not about pay, is it?
Mr Langley: There are two things about the military. One is that because a lot of the defence contracts have been sent out to tender, some of these top guys and girls are working alongside defence contractors who do similar sorts of job who are actually earning quite a lot of money, and, therefore, there is a secondary market, if you will, for senior military, and that is a very important issue.
Mr Cockburn: That was a wrinkle that we needed to sort out, and that was a way of doing it, but, in general terms, if you look over time, they have not consistently done better than the rest. This was really fixing a problem that you have to do from time to time. In the same way with judges, every few years we do a more fundamental review of judges' pay and, where they have fallen behind, there may be a catching up necessary to do this. In the same way as when we look at MPs each Parliament there is a kind of catching up process once a Parliament.

Q288 Chairman: Your point Mike though, I think, goes back to what we were talking about earlier on. It is the fact that, as you say, we have put bits of the military into market-facing situations. Nobody, when we were doing that, thought about the consequences in terms of having to produce market-facing salaries, but you are saying that is exactly what is produced by it.
Mr Langley: As you quite rightly said, the military in the past thought there was nowhere to go: "I will just carry on until I get to my retirement age and I will have a reasonable pension and, if I am lucky, I can get another job", but now they can see that they can get another job, and at the age of 50, maybe, they think, "Here is a job that I can do quite easily for the next 15 years." The other thing that is very important about the top military is that when they are promoted to the first rung of our remit group they have to accept that they will not necessarily carry on to retirement age, that they are only guaranteed one term.

Q289 Mr Prentice: What is a term?
Mr Langley: Two or three years in the next job, and after that job is finished there may not be another job for them. So the people who are in the rung just below say, "Look, if I take this job with a very modest pay increase, I may have another pip on my shoulder but I may actually be curtailing my potential earnings from 10 years to three years."
Chairman: Okay.

Q290 Kelvin Hopkins: You made a point in your recent answer that there are people in the public service who do not work for money; as long as they are getting paid reasonably they work there because they are committed to public service. Are you not bringing into the public service the values of the private sector, if you like, where it is all about money and profit, and is this not inappropriate? Is it not necessary that we perpetuate this enormously valuable sense of public service? I know many people who want to work in the public sector because they believe in public service. They want decent pay, but they are not there for high salaries and bonuses.
Mr Langley: That is absolutely right, provided the differential between what they are paid in the public sector and what they might potentially earn somewhere else, whether it is in the private sector or the wider public sector, is not too great. I think the people that we talk to when they come to visit us and give evidence are people who really enjoy their jobs. They find them very interesting mostly, some of the senior civil servants we talk to have very, very interesting jobs, they move from one department to another very often and so they have a wide sense of job responsibilities that they can get without moving outside the organisation, and as long as the discount, the pay discount, the benefit discount for doing that job is outweighed by the job interest and the public sector ethos, that is okay, but if it gets out of kilter, if the potential outside becomes too great, then they will go.

Q291 Chairman: Are local authority chief executives a category that you might take under your wing, do you think, properly?
Mr Cockburn: We have not been invited to look at them in the past, but back to an earlier question, if you are saying, "Would it be appropriate?", insofar as they seem to be looked at on an individual basis rather than a collective basis, if we were asked to look at it, obviously, we would look at it.

Q292 Chairman: My question is you are not empire builders, you have not identified other bits of the public sector which you think should probably come within your remit, but you are open to invitation?
Mr Cockburn: Yes.

Q293 Chairman: Finally, transparency. Presumably we are moving to a situation where the presumption should be that all publicly paid people have transparent salaries, are we not?
Mr Cockburn: Yes.

Q294 Chairman: And you are in favour of them?
Mr Cockburn: Yes. In fact, actually permanent secretaries' pay is published, military pay, our pay.
Chairman: Our pay!
Mr Prentice: Our fees are in the public account.
Chairman: Our allowances, unfortunately.

Q295 Mr Prentice: Before you finish with this transparency of pay and so on, do you think there is a ratio, perhaps, between the lowest paid person in

an organisation and the highest paid person in an organisation that would work, or would you not go down that road at all?
Mr Cockburn: I would not. It is very arbitrary. In some cases there may be a good reason why. I think you could have an eye on it. There might be pressure for private sector committees to display such information in their report and accounts each year just to show this up.

Q296 Chairman: Thank you for coming to see us. It is nice to meet the people that set our salaries, more or less, and we have learnt a lot from you.
Mr Cockburn: Ten to 15% is what we recommend.

Q297 Chairman: The problem is, with the best will in the world, if you come forward with a proposition in the next period of time to increase MPs' salaries by 10 or 15%, you will be laughed out of court, will you not?
Mr Cockburn: We have said so, of course, in the past and you have not accepted it.

Q298 Chairman: Thank you very much for this morning.
Mr Cockburn: It was a great pleasure.

Written evidence

Memorandum from the Cabinet Office

Thank you for your letter of 30 March 2009,[1] requesting background information in relation to the Committee's inquiry into Executive Pay in the Public Sector.

Please find attached the answers to your questions, which I hope you will find helpful.

1. *What procedures are in place and what guidance exists for determining remuneration packages for public appointments made by the Crown and by Ministers, including to the boards of public bodies?*

Individual Departments are responsible for determining the levels of remuneration paid to public appointments for which they are responsible.[2] This recognises the fact that public appointments vary greatly in terms of roles, responsibilities, profile and importance. It is important that Departments have flexibility to determine an appropriate level of remuneration based on what can be very particular circumstances.

It is for each Department to put in place internal procedures to assist in the determination of remuneration for public appointments for which the Department is responsible. Some Departments, for example, have issued general guidance to officials, but allow decisions on remuneration to be made on a case by case basis. Some allow flexibility but require senior level oversight and "sign-off". And other Departments have set specific benchmarks or ranges to help inform the levels of remuneration set for all their public appointments. All Departments, however, are bound by the general principles set out in the HM Treasury publication Managing Public Money. This can be downloaded from:

http://www.hm-treasury.gov.uk/psr_mpm_index.htm

This means that each Department must ensure that any remuneration offered to a public appointment for which they are responsible is appropriate, affordable and provides value for money to the taxpayer. The Cabinet Office guidance *Making and Managing Public Appointments* states that Departments should adopt a consistent approach in the levels of remuneration offered to public appointments for which they are responsible.

1A. *What co-ordination role—if any—is played by the Cabinet Office and/or Treasury in setting guidelines, giving advice, and monitoring in this area?*

The Cabinet Office publication *Making and Managing Public Appointments* contains advice and guidance to Departments on the public appointments process. Chapter 15 of *Making and Managing Public Appointments* sets out the policy position on remuneration and provides advice and guidance to Departments on setting remuneration for public appointments. A copy can be downloaded from:

http://beta.civilservice.gov.uk/about/work/public-appointments.aspx

The guidance makes it clear that, in the majority of cases where remuneration is paid, the office-holder should receive a flat fee or rate. Offering performance-related pay or bonuses should be exceptional. Most public appointments can claim reasonable expenses in line with the rules drawn up by the relevant body/ Department. The majority of public appointments are non-pensionable.

The Cabinet Office provides advice to Departments on a case by case basis and works with Departments and other stakeholders to identify and share good practice in all aspects of the public appointment process (including on remuneration-related issues). The Cabinet Office also requires Departments to publish annually in their Public Bodies reports or Annual Report, summary details of all their public appointments. This includes information on the levels of remuneration paid to individual Chairs and Chief Executives of public bodies.

HM Treasury advises and approves remuneration packages for public appointments in the small number of cases where HM Treasury approval is required. HM Treasury also requires executive NDPBs and similar public bodies to publish annual reports and accounts. These will include details of salaries and allowances paid to Chairs and non-executive board members—as well as to senior staff.

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1 Not printed

2 There are a small number of public appointments where the relevant founding statute requires HM Treasury approval. There are also some bodies which are prohibited from providing remuneration to their board members by their founding legislation or by virtue of their charitable status.

2. *What procedures are in place and what guidance exists for determining remuneration packages for non-executive appointments to the boards of Government departments and agencies?*

As with public appointments, each Department and Agency is responsible for determining the levels of remuneration paid to non-executive members on their boards.

The Cabinet Office issues guidance setting out some common principles which underpin the recruitment, selection, appointment and development of non-executive board members on civil service boards. This includes principles which should underpin decisions on remuneration. The guidance makes it clear that there must *not* be a presumption that any remuneration offered is comparable with non-executive directors in the private sector—or in other parts of the public sector—as the responsibilities and liabilities are very different.

3. *What procedures are in place and what guidance exists for determining remuneration packages for senior executives in public bodies?*

3A. *According to paragraph 8.4.4 of Public Bodies: A Guide for Departments, "in general, approval for Chief Executive pay is primarily the responsibility of the sponsor department in consultation with the Treasury". How do sponsor departments exercise this responsibility? What exceptions exist for this process?*

Non Departmental Public Bodies (NDPBs)

Existing guidance

Existing central guidance concerning NDPB Chief Executive pay can be found in the 2009-10 edition of the *Civil Service Pay Guidance* and in *Public Bodies: A Guide for Departments.* This can be downloaded from:

http://www.civilservice.gov.uk/about/work/codes/public-bodies.aspx

New Chief Executives

Sponsor departments discuss proposed remuneration packages for new Chief Executives with HM Treasury which are significant or potentially repercussive. They submit a proposed starting salary and bonus range, along with a business case in support of the proposals. This business case compares the proposals for the new Chief Executive with remuneration arrangements for appropriate comparators, outlining reasons why the proposed remuneration is appropriate. NDPBs and sponsor departments are expected to take into account public sector pay policy when preparing and considering remuneration proposals. As announced in the 2009 Budget (paragraph 6.43), when vacancies from NDBP chief executives arise, NDPBs and sponsor departments must undertake a first principles review of remuneration packages to ensure that these reflect the current labour market conditions. Subject to specific requirements in the NDPB's founding legislation, the sponsor department will approve the final package following discussions with HMT, in line with *Public Bodies: A Guide for Departments.*

Restructuring of existing Chief Executive posts

Sponsor departments also consult HMT on proposals to increase the remuneration of an existing Chief Executive beyond existing uplift arrangements if significant or potentially repercussive. As for new Chief Executives, these proposals are supported by a business case, giving comparative remuneration data and details of the reasons for wishing to change the remuneration, including, for instance, any change in the job responsibilities, or retention issues. Again, public sector pay policy needs to be borne in mind in the preparation and consideration of proposals. The approval arrangements are the same as for new Chief Executives.

Annual remuneration decisions

The process for approving annual pay uplifts and any performance-related pay where relevant is the responsibility of the sponsor department. Details for specific departments should be confirmed with the department itself.

Further guidance has been included in the 2009-10 edition of the *Civil Service Pay Guidance,* to ensure that NDPBs consider the remuneration of their Chief Executives alongside the pay of the rest of their staff, according to the same principles, and consistent with the principles of public sector pay policy. The 2009–10 *Civil Service Pay Guidance* gives details of the kind of information required in business cases put to sponsor departments supporting remuneration proposals.

Remuneration proposals for other executives

HMT also asks to be consulted on remuneration proposals for other executives who are to be paid, the same as, or more than, the Chief Executive, following the same process. On occasion, sponsor departments consult HMT on the remuneration of other executives but this is not a requirement.

HMT is not aware of any exceptions to these arrangements.

Government, through the official led Public Sector Pay Committee, is currently in the process of examining the setting of senior pay in the public sector. The Government shares the objectives of the Public Administration Select Committee to ensure that total remuneration packages are set in a transparent and accountable way, that high quality candidates are recruited to these important positions through evidence based benchmarking of roles and responsibilities, and that outcomes are value for money. Our concern in this matter pre-dates the PASC inquiry and we are in the process of considering future reform. Government looks forward to the Committee's findings as a valuable contribution to such reform.

4. *What procedures are in place and what guidance exists (either from central government or from another co-ordinating source) for determining remuneration packages for senior executives and non-executives to other bodies either generally or sometimes considered to be within the public sector? (for example, local authorities, NHS Trusts, universities, the BBC, Network Rail, UK Financial Investments, British Nuclear Fuels, Partnerships UK).*

PUBLIC CORPORATIONS

Generally Public Corporations are governed in accordance with their constitutional documents.

For those public corporations covered by the publication *Public Bodies: A guide for Departments,* guidance is provided to Government Departments on the approach for establishing and managing bodies. There are also important sections of *Managing Public Money* and the Consolidated Budgeting Guidance that Departments should apply.

NHS

BOARDS

Remuneration rates for Chairs and non-executive board members of NHS bodies (excluding Foundation Trusts) are set by the Department of Health. Foundation Trusts are free to set their own rates.

SENIOR STAFF

Chief Executives and executive directors (and other senior managers with board level responsibility who report to the CEO) working in Strategic and Special Health Authorities, Primary Care Trusts and Ambulance Trusts are subject to a national pay framework—the Very Senior Managers (VSM) Pay Framework—introduced in 2006. Each year the Senior Salaries Review Body makes recommendations to Government on the level of annual uplift and value of the non-consolidated performance pot for staff covered by the VSM Pay Framework.

NHS Acute Trusts, Foundation Trusts and Mental Health Trusts are responsible for their own decisions about executive pay. All have remuneration committees, comprising independent non-executive directors, which make objective decisions about pay and allowance. Foundation Trusts are also subject to the scrutiny of MONITOR—the independent regulator of NHS Foundation Trusts—which ensures that pay decisions are affordable. Acute, Mental Health and Foundation Trusts fully disclose what they pay their executive and other staff in their annual reports.

LOCAL AUTHORITIES

No guidance is issued by Government on senior officers' pay and conditions in Local Authorities. All decisions about pay are taken locally. The Local Government Employers (LGE) is the co-ordinating body for senior pay amongst Local Authorities—and they monitor and advise on remuneration. The LGE, along with the relevant trade unions, negotiates annual pay increases. There is no central Government involvement.

UNIVERSITIES

University are not considered public bodies. They are more generally considered private sector, not-for-profit bodies. The Government has no role in determining the pay of senior staff—or other staff. Pay for senior staff will normally be determined by the University's Governing Body on the basis of market rates.

5. *How are decisions taken on which groups of senior public sector posts to include within the ambit of the Senior Salaries Review Body? (eg the recent inclusion of very senior managers in the NHS).*

The groups which fall within the remit of the Senior Salaries Review Body is largely a matter of history; although Ministers have sometimes added to them. The Review Body on Top Salaries (TSRB) was appointed in May 1971 and renamed the Review Body on Senior Salaries (SSRB) in July 1993. The review body provides independent advice on the remuneration of holders of judicial office; senior civil servants; senior officers of the armed forces and other such public appointments as may from time to time be specified. In 2007, its remit was expanded to include Very Senior NHS managers,[3] following the introduction of a national pay framework for the group.

[3] NHS Very Senior Managers in England are chief executives, executive directors (except medical directors), and other senior managers with board level responsibility who report directly to the chief executive, in: Strategic Health Authorities, Special Health Authorities, Primary Care Trusts and Ambulance Trusts.

The Review Body also advises the Prime Minister from time to time on the pay and pensions of Members of Parliament and their allowances; on Peers' allowances; and on the pay, pensions and allowances of Ministers and others whose pay is determined by the *Ministerial and Other Salaries Act 1975*. If asked to do so by the Presiding Officer and the First Minister of the Scottish Parliament jointly; or by the Speaker of the Northern Ireland Assembly; or by the Presiding Officer of the National Assembly for Wales; or by the Mayor of London and the Chair of the Greater London Assembly jointly; the Review Body also from time to time advises those bodies on the pay, pensions and allowances of their members and office holders.

6. *How (if at all) does central government monitor remuneration at senior levels in the wider public sector? (ie, in those areas outside the ambit of the SSRB)*

NDPBs and Public Corporations

Unless there is a new appointment or restructuring of an existing post, HMT does not currently monitor remuneration of NDPB Chief Executives (or those paid the same or more) and departments establish their own monitoring arrangements. Individual departments should be consulted on these. HMT guidance is that the pay of other executives is to be included in the NDPB's pay remit.

HMT does not ordinarily oversee remuneration of public corporation Chief Executives. Where Government Departments are the shareholder of a public corporation they would be expected to oversee and discuss Board remuneration with the relevant remuneration committees. Departments establish their own monitoring arrangements. Individual departments should be consulted on these.

The Cabinet Office does require all Departments to publish annually summary information on the NDPBs they sponsor. This includes information on the levels of remuneration paid to Chairs and Chief Executives. All executive NDPBs also publish detailed Annual Reports and Accounts containing information on any salaries and allowances paid to Chairs and non-executive board members—as well as to senior staff. In general public corporations will produce Annual Reports and Accounts and those that are bound by the Companies Act will be required to comply with the relevant legislation.

September 2009

Memorandum from Sir John Baker

Summary

1. I am no longer in a position to help the Select Committee in terms of the detailed factual background to their inquiry, but I am happy to provide some comments and opinions based on my 10 years as a member, then Chairman, of the Senior Salaries Review Body (SSRB) and a member of the Senior Heads of Mission Remuneration Committee of the Foreign and Commonwealth Office. In brief, my views on the questions identified by the Select Committee are as follows:

(a) *Are the right arrangements in place?*

In so far as remuneration is dealt with by Pay Review Bodies, the arrangements work well and probably better than any other system. Their work is independent, evidence based, fully transparent, has shown appropriate degrees of flexibility, and broadly produced the right results as between serving the needs of recruitment and retention on the one hand and securing value for money for the taxpayer on the other. At senior levels there is no evidence that the public sector is a pay leader.

(b) *Consistency?*

Consistency should not be a prime consideration. There is of course a significant degree of consistency but greater flexibility is of even more importance.

(c) *Public and Private Sector Comparability?*

Such comparability is not necessary for recruitment and retention of good people to the public sector as witnessed by the huge discrepancies between private and public sector remuneration at senior levels already pertaining.

(d) *Wage Inflation?*

There is no substantive evidence of systematic wage inflation at top levels in the public sector, rather the contrary. There is some anecdotal evidence of some Local Authorities or NHS Trusts, especially those in trouble, bidding up a minority of posts in an effort to secure scarce very able talent, but the consequences are probably trivial given it is necessary to attract the very best talent to where it is most needed and it cannot be conscripted.

(e) *Consultancies?*

The use of consultants both in relation to recruitment of certain individual posts and in the provision of labour market data is necessary to make good deficiencies in public sector capabilities and to keep touch with the market. The key is for the public sector to ensure it has the capacity to manage consultants effectively and secure value for money/the Office of Manpower Economics is a good exemplar.

(f) *Balance in the Remuneration Packages?*

Broadly, within the total remuneration package of base pay, performance pay, and pension rights, public sector senior posts are generous in terms of pension provision but inadequate in respect of reflecting performance in terms of pay progression and bonuses.

(g) *Pay and performance?*

Remuneration can certainly impact performance. More emphasis needs to be given in public sector pay arrangements to better rewarding exceptional or consistently very high level performance. But this has to be done in the context of target setting and monitoring, and high integrity appraisal systems.

(h) *Benchmarks?*

Wholly inappropriate.

(i) *Value of overseas experience?*

Negligible.

DISCUSSION

2. PAY REVIEW BODIES

There is a lot that is right in the determination of the remuneration of top-level public service posts. Taking the Senior Civil Service, Senior Military, the Judiciary and some senior posts in the NHS (the principal remit groups of the SSRB) as examples, it seems to me that the Pay Review Body system is working well in ensuring that remuneration (base pay, performance-related awards, pensions) is just about adequate to recruit and retain quality people whilst also taking account of public sector pay policies, the diversity amongst and differences between different labour markets and pay groups, and the need to ensure that senior public service pay does not become a pay leader, driving up pay elsewhere. I believe this good situation has been reached as a result of the professional capability of the Office of Manpower Economics in providing research and analysis; the fact that the recommendations of Pay Review Bodies are evidence-based and independent of the parties, and not the outcome of horse-trading or government decree; the judicious use of external consultants to provide labour market analysis and comparative pay data; the quality and hard work of pay review body members themselves in understanding the issues and exercising judgement in the formulation of their recommendations; the fact that all the review bodies' reports and the evidence supporting them are published and fully transparent to all the parties and the public; and the continuity of knowledge and expertise that has thereby built up over many decades and is unrivalled elsewhere in public sector pay management. No better way has yet been found to determine the pay of public sector employees.

3. BUT THERE ARE STILL ISSUES

This is not to say that the situation is perfect. If I take the Senior Civil Service as an example there are aspects of the current remuneration arrangements which may need further thought:

— *pay comparability*

At very senior levels, civil service remuneration has not kept pace with private sector executive pay by a large margin. This is not important whilst sufficient people of talent still make themselves available for senior positions in public service. But awareness of what is happening in the private sector is important, as is careful monitoring of the quality of new recruits and retention rates. This argues, however, for retaining diversity in the way different parts of the public sector set pay for senior appointments/a monolithic system would be more likely to lose touch with the various markets for high level talent and be less able to differentiate between the differing needs of differing organisations or sectors in terms of leadership and top management. The consequent lack of uniformity in senior pay levels as between, say, the Senior Civil Service and some Local Authority or NHS Chief Executives is a minor problem measured against the advantages and flexibility of diversity.

— *use of external recruitment*

External recruitment direct to senior posts in the SCS, itself desirable, has led to the emergence of a two-tier pay structure, with externally recruited candidates systematically being appointed at higher pay than internal promotees whose pay is set by the minimum necessary to recruit and retain good people already committed to that type of employment. Whilst this is not wrong in principle, if this practice becomes too widespread and the gulf too wide, it could bring the whole pay system into disrepute with adverse effects on morale and, in time, recruitment and retention. Indeed, it could also expose the system to the risk of litigation on the issue of equal pay. Flexibility is desirable, indeed essential, in attracting talent from outside, but it is essential that those making external appointments and negotiating pay packages, are expert enough to secure value for money. More internal expertise may be required here, not least to question any advice received from external recruitment consultants.

— *performance pay*

Performance related pay is a necessary and fundamental feature in the pay of the SCS, both for base-pay progression and the determination of any bonuses. This is highly desirable in securing the highest levels of performance and value for money. For performance pay systems to be fully effective and motivational, there needs to be an effective and well-disciplined system of target-setting for group and individual performance and monitoring of outcomes, coupled with a realistic, humane but honest appraisal system. The SCS has made real progress in these areas in recent years, but more still needs to be done. However, the best of systems will not be properly effective in rewarding good performance and assisting motivation if the differences in reward from doing an exceptional job and simply performing adequately are small. As a general observation it can be said that the performance-related (especially the bonus element) aspects of SCS pay are as yet too small to be fully effective.

4. Flexibility is Vital

As a generality it can be said that the determination of pay at senior levels in the public sector needs to be flexible to reflect diverse requirements and markets and, at the very top level, often needs to be tailored to very specific needs where skills are scarce and real talent perhaps in short supply. Some top jobs will have an accent on leadership, some on policy analysis and formulation, some on professional expertise, some on change management, some on the delivery of services, some on presentational skills. This will create tension in the face of the normal centralising forces of central government to control things (in general and in detail), to impose one-size-fits-all policies (eg in relation to public sector pay policy), and to avoid taking difficult (ie presentationally difficult) decisions. For example, it has been the increasing tendency of the Government to treat all pay awards in the same draconian way to avoid the problem of the "wrong signals" being sent from one pay group to another. The application of this (misguided) policy to senior appointments partly explains why senior civil service salaries have lost touch with those in the private sector. To members of a pay review body the oppressive weight of government control, which only gets heavier and never lighter, imposes frustrating constraints on finding sound and creative solutions to problems with pay levels and systems that inevitably emerge because labour markets, the nature of demands of the work to be done, the organisation of business, are dynamic. Problems and anomalies tend to build up, creating more and more tension until a crisis breaks. These tensions, which will always exist to a greater or lesser degree, would become more challenging if there were even greater efforts made to bring more and more public sector top appointments and senior pay groups within a yet more centralised and regulated system. It would be a gross mistake to impose greater central control to deal with a handful of high-profile outlying cases. And it is worth noting that, when it comes to the pay of the Cabinet Secretary and Permanent Secretaries, Ministers are already involved on a person by person basis with the appraisal of the individual's performance and that the Prime Minister takes the final decision on the pay progression of each Permanent Secretary. There are also benefits in terms of flexibility in the pay bands for senior civil servants being as wide as they currently are.

5. Benchmarks

I would caution against any concept that there should be a single "benchmark" to set a limit on public sector pay. There already is a degree of homogeneity. For example, it is an accepted policy that the pay of each of the heads of the three great pillars of the state (the Cabinet Secretary, the Chief of the Defence Staff and the Lord Chief Justice) should be broadly similar. The post of Cabinet Secretary is the easiest of the three to evaluate for remuneration purposes by reference to other markets in the public and private sectors for whom data is readily available: the read-across to the other two top posts for which there are no real market comparators is thus helpful in setting their pay and hence that of the rest of the senior military and judiciary. The SSRB has also proposed that the pay of the Prime Minister should, in principle, be at least equal to that of the Cabinet Secretary, and Secretaries of State to that of their Permanent Secretaries, on the basis that the permanent officials are accountable to them. This has found no favour with the Government, however, and ministerial pay lags well behind, ie there is a de facto "political discount". I see no current prospect of any government arguing the logic case for a hike in ministerial pay to a sceptical public, so it is clear that no benchmark derived from, say, the pay of the Prime Minister would be realistic for the wider public sector, which would become totally uncompetitive for top talent if the pay of the most senior posts were held down to a level determined by the pay of the Prime Minister. Equally, the imposition of an arbitrary ceiling based on a particular multiplier of, say, average personal income would also risk severe distortions between public and private and NGO pay over time, and impose inflexibility as to how the various and very divergent organisations within the public sector react to changes in the particular labour market dynamics in their field of activity. It is already arguable that public sector pay policy is over-rigid in the way it works, with national pay scales in education and health care, for example, making posts in London relatively unattractive and those remoter from London and other expensive towns and regions more attractive than required for recruitment and retention. Creation of some benchmark ceiling would in time be likely to lead to further rigidity, limiting room for manoeuvre in adjusting pay to meet the changing requirements of shortages, new skill requirements, organisational change, or the need to bring in outsiders to provide fresh ideas or a new impetus.

6. Overseas Experience

In practice it is very difficult to find useful ways of comparing remuneration in different countries. Circumstances are always different, with different values in different countries being put on the relative value of similar jobs and the merits of public/private sector work, different values put on pay versus prestige, different values put on state control versus market freedom, different skill shortages in different markets, plus, of course, the methodological problem of drawing conclusions when underlying economic conditions are different (eg unemployment levels) and exchange rates are fluctuating.

May 2009

Memorandum from Chartered Institute of Personnel and Development (CIPD)

Background

1. The CIPD's primary purpose is to improve the standard of people management and development across the economy and help our individual members do a better job for themselves and their organisations.

2. As the UK's leading professional body for those involved in the management and development of people, we are ideally placed to contribute to the development of public policy across the spectrum of workplace and employment issues.

3. We are able to draw on the experience and knowledge of our 133,000 members and our wide range of research to provide a pragmatic stance on public policy that is based on solid evidence and the real world.

4. Our membership base is wide, with 59% of our members working in private sector services and manufacturing, 34% working in the public sector and 7% in the not-for-profit sector. In addition 82% of the FTSE 100 companies have CIPD members at director level.

The Committee's Inquiry into Executive Pay in the Public Sector

Good reward practice

5. Although the CIPD feels it cannot comment on the appropriateness of specific arrangements for setting executive pay in the public sector, we can, in our capacity as human resource experts, advise on what constitute good reward practices across all sectors.

6. CIPD encourages all reward practitioners to deliver pay transparency so that employees know why they earn their level of pay, why others earn theirs and what they need to do to achieve a pay rise, bonus award or promotion. This particularly means there should be a clear statement of those behaviours, competences and values that are required by the organisation and how they will be rewarded and recognised.

7. In creating and developing such pay structures and progression mechanisms, reward professionals should try to ensure that an element of pay *at all levels* is linked to organisational and/or individual performance. The CIPD annual *Reward Management Survey* shows that pay is becoming increasingly individualised particularly at senior management levels.[4]

Total Reward

8. We also believe that good reward practice encompasses a "total reward" approach which considers not only the cost and value of base pay or bonuses, but also employee benefits such as share options, healthcare and importantly pension schemes.

9. Unfortunately, this year's CIPD *Reward Management* survey indicates that only 11% of employers in the public sector have adopted a total reward strategy and that few evaluate the impact of their reward practices on the organisation

10. Bearing this in mind, it is unlikely that these public sector employers will have examined what values, attitudes, performances and behaviours are required from their senior executives and articulated how they will reward and recognise these financially and non-financially. Not examining these performances and tying them to pay may mean that people are rewarded indiscriminately.

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[4] The 2009 annual *Reward Management Survey* showed that 92% of organisations used individual performance to manage pay progression for senior managers as compared with 73% in the 2006 survey.

11. Public sector employers that do assess the impact of their reward practices use a wider range of HR and business measures than their private sector counterparts indicating "a balanced scorecard approach" to organisational performance.

12. We believe that such an approach to rewarding and recognising both short and long-term employee contribution could be beneficial to most public sector employers and should be adopted more widely.

CIPD principles for good remuneration practice

13. The CIPD is currently creating a set of principles for good remuneration practice at the board level. The principles are attached to this consultation document as an appendix. Our guidance will be followed up by a report explaining how practitioners should implement the principles.

14. These principles have been developed by reward professionals for reward professionals and are designed to be applicable to all organisations, regardless of economic sector.

15. The purpose of these principles is to help design remuneration packages that act as enablers to support an organisation's talent agenda (eg attraction and retention of talented employees), their business context and to create and deliver long-term value to its shareholders and/or other stakeholders.

Summary

16. To sum up, the CIPD believes that much of the current media and political focus on public or private sector executive pay is misguided. What is just, and potentially, more important than pay levels and pay increases is which performances are being rewarded and why and how they are going to be funded.

17. For a reasoned judgement to be made there must be disclosure not only of the full remuneration package but also what the individual has done and is doing to earn that sum.

18. This principle applies equally across the public, private and voluntary sectors and organisations should remember that there is more to an employees' reward package than just money.

April 2009

APPENDIX

PRINCIPLES FOR GOOD REMUNERATION

The CIPD has developed this set of principles for good remuneration practice at the board level. These principles were developed by reward professionals for reward professionals and are designed to be applicable to all organisations, regardless of economic sector.

The purpose of these principles is to help design remuneration packages that act as enablers to support an organisation's talent agenda (eg attraction and retention of talented employees), their business context and to create and deliver long-term value to its shareholders and/or other stakeholders.

The CIPD considers that to be effective, board level reward packages should be:

1. Context-based

1.1 There is no "one size fits all" solution to executive remuneration. What works in one situation may not be appropriate in another.

1.2 Organisations need to offer remuneration packages that are appropriate for their sector, the business context, the organisation's agenda and other circumstances, eg domestic or foreign owned and where they are in their business cycle.

1.3 The time frames used to assess performance and remuneration will be different between organisations [eg what is considered long-term for an organisation in one industry, such as retail, maybe viewed as short-term by another, such as pharmaceuticals].

2. Competitive

2.1 Remuneration packages for executives should be competitive for their market and sector, in the same way as packages offered to other employees.

2.2 The market and sector should be reviewed regularly (in particular—global, international, local) to ensure the comparators remain appropriate.

3. Commensurate

3.1 Executive remuneration packages should support and be aligned with an organisation's philosophy, market practice, strategy and values.

3.2 The quantum of any award should reflect the value that the executive has created for the organisation over the short and longer-term. The more value that is created or delivered, the greater the reward.

4. Performance Based

4.4 Executive remuneration packages should be linked to value creation over the short and longer-term and there should be clear alignment of interest between the executive, shareholders and other stakeholders.

4.5 Each organisation needs to consider how best to align the interests of its executives to the interests of its shareholders/stakeholders.

4.6 Each organisation needs to decide which of the various performance measures available are most appropriate to an executive in its particular context and at a particular time in the business cycle.

4.7 Judgement will need to be applied in assessing the quantum of an award, including the impact of history and how much of current value creation is a result of the present or past leadership. The reward should be proportionate to the effort of the individual and the impact on the organisation.

4.8 There should be the facility to claim some [or all] of a variable payment back (sometimes referred to as a malus clause) if the performance underpinning such payments subsequently proves to be unjustified.

4.9 An organisation will need to be able to explain and justify the rationale behind the remuneration decisions made to its stakeholder/owners.

4.10 An executive should understand what is expected of them, how they will be rewarded and recognised and what will happen if they do not meet expectations.

5. Balanced

5.1 Components of the remuneration package should recognise and balance internal conflicts, such as between short and long term, individual and collective, what has been achieved and how it has been achieved, etc and should be structured and managed holistically.

6. Transparent

6.1 The design of the remuneration package should be clear and simple enough to be motivational to the executive.

6.2 The process for determining the quantum of an award needs to be clear and understandable both to the executive, shareholders and other stakeholders (including other employees).

6.3 The remuneration package should be fully disclosed to shareholders/stakeholders, such as through the annual accounts.

6.4 However, public disclosure and transparency should not be used as an excuse by employers to copy the remuneration practices of other employers as that will just ratchet up pay.

7. Consistent

7.1 Executives must understand the expected level of performance, attitudes and behaviours, and how these will be recognised and rewarded.

7.2 The achievement of these should result in the consistent application of remuneration processes both for themselves (over time), between themselves and other executives, and between executives and the rest of the workforce.

8. Costed

8.1 The overall remuneration package for executives should be expressed in total remuneration terms such that the executives and shareholders/stakeholders are aware of the value of the total package.

8.2 he overall cost to the organisation of providing each element of the package should be expressed such that stakeholders can judge the return on investment.

9. Integrated

9.1 The remuneration strategy that an organisation adopts for its executives needs to be set in the context of its overall business strategy, HR policies (eg talent management, development, inclusion etc).

9.2 Remuneration committees should ensure that the underlying remuneration philosophy and strategy of the organisation is not contradicted by the way executives are recognised and rewarded.

9.3 Pay approaches in the rest of the organisation is one of the factors that need to be taken into account by remuneration committees in designing executive packages. When developing executive remuneration packages, a Remuneration Committee should have regard to the reward policies and practices across the organisation, seeking to provide alignment on key design features where possible and practical.

10. Independent

10.1 To ensure that shareholders, external stakeholders and staff trust the way that executive packages are determined, it is important that the body making this decision, such as remuneration committees in UK PLCs, have a significant number of members who are independent of the organisation.

10.2 All decision makers should be HR and reward literate and have access to various sources of independent and quality remuneration advice and data.

10.3 Remuneration committees should have regard to appropriate guidelines, eg combined Code on Corporate Governance, NAPF/ABI guidance for UK PLCs or the Charities Act for voluntary sector employers.

Memorandum from the Committee of University Chairs

The Committee of University Chairs (CUC) welcomes the opportunity to contribute to the inquiry into Executive Pay in the Public Sector. CUC is the representative body for the Chairs of UK Universities, encompassing all universities[5] irrespective of their mission or origins. Its purpose is as an enabling body to ensure that its members are well informed of relevant issues, developments, and best practice so that they are better able to discharge their roles effectively. It also acts as an influencing body, engaging in dialogue on policy with ministers and government departments across the UK on a range of strategic issues.

The governing bodies that our members chair are responsible for establishing the remuneration committees which set pay for their institutions' executive heads (the Vice-Chancellor or Principal). The Chair will usually sit on their institution's remuneration committee.

Summary

1. As noted in the inquiry scope, Vice-Chancellors' pay does not fall directly within the Public Administration Select Committee (PASC)'s areas of experience, so the following submission is intended to provide the Committee with some contextual information on the setting of executive pay in the higher education sector.

2. Principally, it is important to note that universities are not-for-profit private institutions. They should not therefore be compared to schools, FE colleges, or indeed any other quasi-public organisation. Their Vice-Chancellors or Principals (the executive heads) are personally responsible for the administration of staff numbers and turnover comparable with medium-sized or large private sector companies and, on average, 40% of university revenue now comes from non-state sources.

3. The executive heads of universities are remunerated in line with what it takes to attract and retain those of the required calibre to lead a unique and complex organisation and bearing in mind the level of risk and responsibility that the role entails. The details of their salary packages are open and transparent and made public on an annual basis.

4. The contextual information below is structured around some of the questions listed in the inquiry's remit. The questions have been taken as they apply to universities, and chosen because of their relevance to the case of university executive pay.

Arrangements for setting and monitoring pay and other benefits for top posts in universities

5. The salaries and conditions of service of Vice-Chancellors and Principals (as well as Pro Vice-Chancellors and some Senior Management Team members) are independently determined by remuneration committees in which the individual concerned plays no part. These committees, which are usually made up of representatives from business and elsewhere, seek to take an objective view of the appropriate remuneration for Vice-Chancellors that is proportionate to the scope and scale of their responsibilities and achievements.

6. Remuneration packages therefore reflect what it takes to attract, retain and reward talented individuals undertaking demanding roles as chief executives of complex, multi-million pound, world-class organisations. The committees ensure the pay is proportionate to the scope and scale of the responsibilities that Vice-Chancellors carry, not only for students and staff, but also as part of their communities. Every university is unique in size, shape, and in the character of its interactions with the business and cultural world in which it is located; the role of every Vice-Chancellor is equally unique, and as well as taking the responsibility for the success of their institutions, they and their institutions also contribute to the infrastructure of their local communities and beyond. Consideration of all these factors is brought to bear on the decisions made by the remuneration committees.

7. Transparency is key to promoting a proper understanding of, and confidence in, remuneration arrangements. The composite pay packages of university executive heads (salary, benefits, bonuses and pensions) are therefore published on an annual basis.

[5] Membership of the Committee is open to the lay chairs of all institutions in the UK which have full university status.

8. With regard to value for money, universities on any measure are successful relative to many parts of the private sector. They produce highly employable graduates with high satisfaction levels (evidenced by the 2008 National Student Survey) and world-class research. As summarised in a recent Higher Education Funding Council for England (HEFCE) report:

> "*UK higher education leads the world in terms of research productivity: its academics produce 16 citations per US dollar, compared with 10 in the United States and four in Japan. With 1% of the global population, it produces 9% of the world's scientific publications and 12% of citations. Universities are also one of the nation's biggest earners of foreign currency, bringing in more than £5.8 billion a year in tuition fees, transnational enterprises and other activities*".[6]

The sector's world-class research success was again borne out by the results of the latest Research Assessment Exercise (RAE 2008). As the strategic decision-makers for their organisations, university Vice-Chancellors play a central role in this success.

Does there need to be consistency regarding these arrangements between different parts of the public sector?

9. Again, universities are not public, but are not-for-profit private, institutions. University remuneration committees are aware of public, private, and sector pay levels when calculating the appropriate pay for the executive head of their specific institution. The relative importance of any such comparisons will differ from university to university, in line with the each institution's particular activity, its unique character, and the candidates it hopes to attract to the role. Because every institution is different, this has proved an appropriate way of attracting the right candidates.

Does there need to be comparability of pay between top posts in the public sector and equivalent posts in the private sector?

10. Private sector pay is certainly a useful guide in setting Vice-Chancellors' pay because the responsibility for strategic decision-making is carried by Vice-Chancellors is comparable with that of a private sector CEO. It would make sense then, that equivalent posts in the private sector might be identified by turnover and staff sizes. At the moment, Vice-Chancellors' pay falls well behind those of CEOs of private sector organisations of a similar size of staff and turnover. Any such comparison will always be limited, however, as it cannot account for the uniqueness of the university and its purpose, and what it takes to attract the right individual to lead it.

Is there evidence of executive wage inflation caused by public sector organisations competing with one another for candidates?

11. Not in the case of Vice Chancellors. Recent increases in executive pay in the higher education sector have been determined by the market, that is, by a rising demand for the best people to lead organisations, not by any artificial factors. There is significant disparity between Vice-Chancellors' salaries, which is strong evidence to suggest that market forces are working and working well through the current system of remuneration committees, and that these committees are effective in ensuring a close link between pay and responsibility.

What impact do the performance or qualities of the people filling top posts in universities have on the performance of the organisations for which they work?

12. Again, the role of a university executive head is essentially that of a private organisation CEO and so has considerable influence over the success or failure of the institution. Vice-Chancellors have a free rein to realise the mission aims of their university as they see fit, through the strategic distribution of resources. These aims will encompass, to varying degrees, student recruitment (international and national), quality and standards in teaching, research excellence and funding, and external links with other sectors of the economy, and so the work of the executive head will have a significant impact on the shape and the health of the institution.

Is there an appropriate benchmark or ceiling for top public sector salaries—eg the salary of the Prime Minister, or a factor of average pay?

13. It does not seem sensible to set a pay ceiling for executive heads in the higher education sector because universities are both varied and evolving organisations. As business-orientated institutions, they should be able, where appropriate, to compete with the private sector in appointing their executive head (that is, to be

[6] HEFCE report, *Higher Education in England: Achievements, challenges and prospects* (2009).

part of the market). All higher education institutions should also have open to them the possibility of becoming more business-orientated in the future, and a pay ceiling could well curtail any such endeavour.

April 2009

Memorandum from Dr Tony Cutler, Centre for Research on Socio-Cultural Change, University of Manchester

SUMMARY

— The submission relates to Key Questions 1 and 8 and examines these questions with reference to research carried out, by the author, on five large executive agencies. The design of this research took account of the central government policy of seeking to apply "corporate governance" approaches to senior management pay into the public sector.

— In the pursuit of a "fair" approach senior management remuneration pay determination was undertaken (in most of the agencies) by pay committees in the sponsoring department.

— Research on large listed companies has questioned the effectiveness of remuneration committees in dealing with conflicts of interest in setting senior management pay. While this issue was not directly researched the overall constraints of the SCS framework considerably limit any scope for "unjustified" pay increases in the agencies.

— Disclosure of details on pay in the agencies was very limited. The general norm was only to disclose aggregate pay levels for senior managers and there was no substantive publicly available information on how the SCS framework was applied to pay determination at agency level.

— Insofar as "value for money" is interpreted (as in "corporate" models) as performance linked pay for the achievement of targets this is constrained by the "forced distribution" approach of the SCS pay framework.

— Insofar as pay inequality (measured by the ratio of chief executive pay to average pay) is deemed a problem and hence a cap on this differential is perceived as appropriate, then pay differentials in large listed companies pose a considerably greater problem than those in executive agencies.

1. The submission is primarily concerned with the Committee's Key Question 1 (particularly sections (a)–(b) and (d)) and Key Question 8. However, before discussing these questions it is necessary to give a brief account of the research on which the evidence is primarily based. It focused on governance aspects of senior management pay in a set of larger executive agencies. Thus it is relevant to the Committee's "focus on civil service posts". Senior managers were defined as board members and the research concentrated on executive managers. The agencies covered were the three largest by full time equivalent (FTE) employment, Jobcentre Plus (JCP), Her Majesty's Prison Service (HMPS) and Her Majesty's Court Service (HMCS). These agencies are principally dependent for their funding on financial allocations from central government. However agencies include "trading funds" which have a substantial income derived from service related fees and the two largest trading funds, by FTE employment, the Driver, Vehicle and Licensing Agency (DVLA) and Her Majesty's Land Registry (HMLR) were included to see if putatively more "commercial" agencies exhibited different governance patterns. Table 1 gives a breakdown of the agencies in employment and expenditure terms, note that the two trading funds had an overall operational surplus.

Table 1

EMPLOYMENT AND EXPENDITURE DATA FOR SELECTED EXECUTIVE AGENCIES 2007–08

Agency	*Sponsoring Department and year of creation*	*Employment*	*Gross Expenditure (£000)*	*Income (£000)*	*Net Expenditure ( )/ Operating Surplus (£000)*
JCP	Department of Work and Pensions (2002)	67,110	3,478,440	18,012	(3,360,426)
HMPS	Ministry of Justice (1993)	49,293	2,314,140	256,169	(2,057.971)
HMCS	Ministry of Justice (1995)	19,345	1,777,436	592,895	(1,184,451)
HMLR	Ministry of Justice (1990)	8,457*	411,355	482,944	71,589
DVLA	Department for Transport (1990)	6,563	541,818	676,116	137,298

Sources: DVLA (2008); HMCS(2008); HMLR (2008); HMPS (2008); JCP(2008)
* HMLR employment data is average numbers employed not FTE.

2. A further prefatory comment is necessary on the prescriptive governance framework adopted for executive agencies. In common with other public sector bodies it has been modelled on "corporate governance" (see for example Treasury, 2005; and for academic discussions of the attempt to transfer corporate governance to a range of public bodies see Clatworthy *et al*, 2000 and Erturk *et al*, 2008). Thus governance practice in agencies aims to simulate corporate sector "best practice" as currently embodied in the Financial Reporting Council's (FRC) Combined Code of Corporate Governance. The current version was issued in June 2008 and outlines recommended governance standards for companies listed on the London Stock Exchange. The research involved three central questions, all related to the appropriateness or otherwise of the putative transfer of "corporate governance" to the public sector. These were: (1) what were the similarities and differences between performance related pay (PRP) for senior managers (strongly endorsed for listed companies in the Combined Code, FRC, 2008: 13) in the corporate sector and the agencies; (2) the Combined Code supports the principle that senior executive managers should not participate in setting their own pay and the recommended method for ensuring that this does not happen is to devolve the decision to a remuneration committee of non-executive directors (ibid 15) thus the second question concerned how such potential conflicts of interest were dealt with in agencies; (3) the final question was concerned with whether there were significant differences between agencies and listed companies with respect to disclosure of the details of senior management pay.

3. The research was undertaken in two stages; firstly agency annual reports for a five year period were analysed; secondly issues arising from this analysis were pursued by contacting (by e-mail) the offices of the Human Resources Directors of the agencies. Responses were received relating to all the agencies, three from sponsoring departments (with respect to DVLA, HMCS, JCP), the other two from agency HR officials.

4. Key Question 1(a): *the "Fairness" of pay setting and monitoring*. "Fairness" is naturally susceptible of a variety of meanings. As was indicated above it has been implicitly regarded as "fair" that senior managers do not play a role in setting their own pay. Two observations are relevant with respect to the agencies researched. The first is that there are mechanisms designed to ensure that conflicts of interest are avoided. These, however, reflect a key difference between agencies and listed companies. Agencies, unlike listed companies, are not pay determination units but report to a sponsoring government department. Thus the principal mechanism for avoiding conflicts of interest is that pay determination decisions for senior managers are taken by committees in the relevant department: in DVLA a Department for Transport remuneration committee; in HMCS and HMPS the Ministry of Justice SCS Pay Committee; and the Department for Work and Pensions SCS pay committee for JCP (communications to the author, HMCS, 2008: 44 and JCP, 2008: 20). In HMLR there is a closer approximation to private sector recommended practice with board level pay determined by a committee of non-executive directors of the agency (communication to the author).

5. Secondly, the private sector corporate governance literature includes significant sceptical commentary regarding the effectiveness of remuneration committees in preventing conflicts of interest. Thus, for example, critics refer to the impact of "community of interest" between executive and non-executive directors on the grounds that the latter are generally active or retired executive directors (Bebchuk and Fried, 2004:33). The research did not investigate the effectiveness of remuneration committee in agencies. However, it is worth noting an important contextual difference with listed companies. Agencies operate within a tightly constrained SCS pay framework regulating pay scales, and setting overall cost constraints. Thus the scope for "unjustified" pay increases is much more limited in agencies.

6. Key Question 1(b): *are arrangements for setting and monitoring pay "transparent"?* Two aspects of the research are relevant to this issue: the extent of disclosure of pay details; and of conditions related to performance related pay. Disclosure of pay details is very limited when contrasted with listed companies. The general pattern was that only *aggregate* pay levels were given in £5,000 pay bands (eg £135–140,000) (see DVLA, 2008: 60; HMCS, 2008: 42; HMLR, 2008: 61; HMPS, 2008: 44; JCP, 2008: 21). Thus no breakdown between changes in performance linked basic pay and in bonuses is presented. There were two exceptions. In DVLA annual reports the salary and bonus of the Chief Executive (CE) is given in each year (DVLA, 2004: 33; 2005: 31; 2006: 55; 2007: 57; 2008: 60). However this breakdown is *not* given for any other board members. In HMPS in 2006–07 and 2007–08 the overall *range* of bonus payments for the board is given but no information is presented on which board members received which bonuses (HMPS, 2007: 54; 2008: 44). Such breakdowns are the norm in listed companies thus allowing for comprehensive salary surveys showing the elements of the senior management pay (eg Income Data Services, 2007). It should also be noted that, while DVLA did publish a breakdown of CE pay and bonus this did not reflect systematic differences between trading funds and the other agencies. Thus, for example, HMLR did not publish such a breakdown.

7. A further significant disclosure issue was the performance conditions attached to PRP. Information on such conditions would require evidence on how committees at departmental or agency level interpreted the SCS framework. The agency reports contained neither information on this issue nor a reference to any publicly available source for reports from these committees. A question posed to each agency was whether such reports were publicly available. All respondents reported that no such reports were publicly available. In HMCS and JCP reference was made to Cabinet Office guidance on how the SCS pay framework should be applied. In the other three cases reference was made to pay strategy documents for the particular agencies (DVLA and HMLR) or, in the case of HMPS, to the Home Office resource accounts (communication to the author). However, these more specific references leave the mode of application of the framework opaque.

For example the HMLR pay strategy states that, in deciding bonus awards, whether "objectives are met" and, where appropriate, "the ease of difficulty in meeting objectives" will be considered. However, no illustrative information is given on how such criteria are applied in the context of the agency. There was also the possibility that the information on the breakdown of senior management pay and performance conditions were included in Senior Salary Review Body reports. However while this source does provide interesting discussions of policy and presents data both are at an *aggregate* level for the SCS as a whole and hence do not provide guidance on individual agencies. If, therefore, a "member of the public" wished to discover (a) the breakdown of the pay of senior agency managers between base pay and bonus and (b) how the SCS pay framework on PRP was applied at agency level for the agencies covered in this submission such information would not (with the exceptions noted on bonus details) be publicly available.

8. Key question 1(d): *Do arrangements for pay setting and monitoring provide "value for money"?* Like "fairness", "value for money" can be interpreted in a variety of ways. However, given the attempt to transfer "corporate governance" noted above it may be worth referring back to a view of pay and performance embodied in the 2008 FRC Combined Code. This (FRC, 2008: 13) is that senior corporate managers should be set targets linked to their pay which embody "shareholder interests". In this respect if the targets are achieved (and if the remuneration committee has fulfilled its function of making them sufficiently "demanding") then the triggering of PRP represents "value for money". There are some respects in which agencies might be seen as exhibiting a similar approach. Thus in reporting year 2007–08 all the agencies used the term "targets" in reports on their "performance" (DVLA, 2008: 16; HMCS, 2008: 24; HMLR, 2008: 16; HMPS, 2008: 16; JCP, 2008: 8). In three cases all key performance targets were quantified and reporting took the form of comparing out-turns with such targets (HMCS, 2008: 24–7); HMPS 2008: 16–19; JCP, 2008: 10–11). In the other two quantitative targets accounted for 75% (DVLA 2008: 16) and 70% (HMLR, 2008: 16) of the set of targets. Furthermore all the annual reports include a commentary by the CE analogous to similar statements in listed company annual reports (see for example DVLA, 2008: 4, HMCS, 2008: 4, HMLR, 2008: 8–9, HMPS, 2008: 6–7, JCP, 2008: 2–3). However, the link to pay does not apply in the same way. The SCS pay framework operates with a "forced distribution" approach where individuals covered compete for a share of a limited funding pool (Cutler and Waine, 2004: 60). Thus, as the SSRB (2008: 24) puts it: "in the private sector . . . conditions for the payment of bonus tend to be fixed in advance so that employees know what targets they have to meet in order to receive a bonus". However, "in the SCS . . . it has been possible for an SCS member to achieve all his or her objectives but not receive a bonus because other colleagues . . . were judged to have performed better" (ibid). This does not mean that the SCS PRP scheme is not delivering "value for money". However, if this term is interpreted as performance linked pay for the achievement of targets then this is not consistent with the prevailing "forced distribution" SCS framework.

9. Key Question 8: *Is there an appropriate benchmark or ceiling for top public sector salaries eg the salary of the Prime Minister or a factor of average pay?* This is a complex issue and the observations made are limited to the conception of using a ratio to average pay as a benchmark. The reference to a "ceiling" can carry the implication that a cap is needed because current "top public sector salaries" are excessive. Table 2 shows CE salary in the four of the agencies as a ratio of average pay in the agencies. As was indicated above, salary is shown in £5,000 bands not as an exact figure so the assumption of a mid point is made and while this is arbitrary it is unlikely to have led to any significant error. HMLR is not included because of the absence of employment figures on an FTE basis. Data for 2006–07 is used for HMCS and DVLA as in both cases there was a change of CE during the year which meant there was no single figure for salary given.

Table 2

RATIO OF CHIEF EXECUTIVE TO AVERAGE PAY
SELECTED AGENCIES 2006–07 AND 2007–08

Agency	*CE: Average Pay Ratio*
JCP, 2007–08	5.9:1
HMPS, 2007–08	5.0:1
HMCS, 2006–07	5.7:1
DVLA, 2006–07	5.5:1

Source: DVLA (2007); HMCS (2007); HMPS (2008); JCP (2008).

CE overall pay at the agencies varied between a range of £135–140,000 per annum (DVLA) to £165–170,000 (HMPS) and the HMLR CE salary fell within this range. It is perhaps interesting to put these figures in a longer term perspective. Froud *et al* (2006: 56) present data on FTSE 100 "survivors" over the period 1978–79 to 2002–03 (ie data for firms who have been constant members of the FTSE 100). The 1978–79 data referred to the highest paid director and the ratio to average pay was 9:1 higher but not wildly out of line with the ratios in the fives shown in Table 2. However, by 2002–03 this ratio (now measured by CE pay: average pay) had risen to 54:1. Thus if the ratio of CE to average pay is treated as a potentially relevant benchmark it is not clear why this should apply purely to the public sector. If it does not then any "problem" of excessive differentials would appear to be focused on large listed companies. Not it should be noted on the private sector per se since, as Froud et al (2006: 57) point out CE pay levels even in large unlisted companies (with turnover up to £500 million per annum) are relatively modest and of a similar order to those found in the agencies covered in the research reported.

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March 2009

Memorandum from Hamish Davidson, Chairman, Davidson & Partners

Introduction

Submissions for other witnesses appear comprehensive and in many respects deliver some consistent themes. Rather than repeat them, I shall merely comment on or add some additional thoughts and perspectives, as well as raise some issues that do not appear to have surfaced as yet and which may be of interest to the Committee.

Culture within the public sector generally is "never take a pay cut, and never take a cut in status"

Christopher Johnson (Mercer) alludes to this in his submission when he talks of it being easier to attract talent from the private sector than from other roles in the public sector—intrinsic value of the work and quality of experience to be gained—whereas candidates from other parts of the public sector already enjoyed intrinsically valuable work.

Within the private sector, it is my experience that candidates will be much more flexible about an "apparent" drop in status as regards literal job title in order to take on a wider role with more responsibility—or a more focused delivery role. They are also more open to being flexible on the make up of the compensation package, which might involve a lower base salary.

Within the public sector, I have found that other than a potential move to the "Not for Profit" or "Third" sector, candidates are almost always unwilling to take a drop in status/title—and most definitely are unwilling to take a drop in salary. The exceptions to this behaviour are, in my experience, rare and exceptional.

This "culture" has had a series of knock-on effects, as I will note below.

The roots of recent salary inflation at Chief Executive (CX) level in local government

There are a number of causes:

(1) *The role of a Local Authority CX has become much more complex*

The net impact of central government policies over the last 20 years means that the role of a Local Government CX (and with a few notable exceptions, I am primarily thinking of unitary, city, metropolitan and counties—rather than districts) has become a larger one and much more demanding in recent years. Rather than presiding over a "steady-state" machine with little in the way of change and a large, top-heavy bureaucracy—the role of today's CX is much more complex, involving ensuring delivery of services through third parties as much as through directly employed staff, via a slimmed down top team and has become much more community and outward facing, and now has very much a shared "leadership" role alongside the elected political Leader of the Council. Actually, the modern role of a CX of a unitary, Met or City authority is probably the broadest in all of public sector. These are tough jobs. The talent required to be successful in this new model CX role is now much greater than was the case in years past, and inevitably then, the pool of such candidates of such calibre is small. Candidates of this calibre are in great demand—and this has contributed to their ability to command higher salaries.

(2) *Much of central government now "rates highly" the best of local government CX's*

When I first began recruiting within the public sector, local authority CX's were, with very rare exceptions, not rated very highly—to such an extent that when conducting a search for a senior civil service appointment, I would generally have been laughed out of court if I had suggested headhunting within the local government community.

Over the last 10 and particularly over the last five years, with the focus on "delivery" local government is today considered one of the few parts of the public sector that actually "gets" delivery, and from where talent that understands how to achieve such in a complex context can be readily sourced. Today, when undertaking a search for a senior civil service or agency role, local government is one of the first areas typically to be considered. The best of local authority CX's now find themselves to be a highly sought after commodity, able to command much higher salaries.

(3) *The unintended impact of CPA*

The Audit Commission alluded to this issue in its report. A perhaps inevitable impact of the CPA regime was the almost desperate need of local authorities to move out of the danger zone of one or no stars—and if at all possible hit four stars. Fair enough. However, what I noticed over the next few years was an emerging trend for elected members, when appointing a new CX, to increasingly veer towards appointing a serving CX who had already made their mistakes elsewhere, would therefore know what to do different, and thus hit the ground running with the barest minimum of learning curve.

It is the impact of this trend that the Committee will want to take note of. Increasingly, there emerged a reluctance to make an internal appointment as CX and to opt for the external. Now, had the internal candidate been appointed, then the salary could typically be set at the lower end of the range. However, given the increasing trend to appoint "externally", and given my point about the prevailing culture within the public sector of never taking a pay cut, the inevitable consequence is ever increasing salary inflation.

(4) *A general reluctance to appoint candidates from outside of local government*

I note with interest that this was a point David Clark of Solace chose not to comment upon in his evidence to the Committee.

My own personal philosophy regarding talent, remains the same as when I last gave evidence to this Committee back in 2003. Specifically:

- — diverse teams tend to make more informed decisions;
- — the best of talent from any one sector is as good as the best of talent in any other sector; and
- — talent comes in all shapes, sizes, guises, genders, accents, nationalities, sectors, etc.

However, for whatever the reason (and perhaps this is another unintended consequence of the CPA regime), local government has continued to be very wary of appointing CX's from outside of the local government family—and very rarely does so, despite more candidates from other sectors (including private) increasingly being drawn to vacancies when they occur, particularly given the more attractive remuneration levels. So whilst one might have thought that increased supply of candidates would take the pressure off the trend of rising salaries, in fact, that potential supply has either tended to be ignored or the specifications for the roles written in such a fashion as to exclude candidates from outside of the sector.

(5) *A general reluctance by head-hunters to challenge restricted personal specifications*

(6) *An increasing tendency "not" to respond to open adverts*

In Europe (but not the US), the UK (and most especially England) is quite unusual with regard to the common practice and extent to which recruitment consultancies/head-hunters are used to recruit to local authority CX roles.

There are a number of reasons for the UK situation:

- — the thinning and reduction of HR capacity leaving organisations less able or confident to undertake occasional, top level recruitment;
- — the increased complexity of the role of CX in local authorities, leaving many less confident about their ability to "grow their own talent";
- — the increased complexity of the role of CX in local authorities has also meant that the candidate pool of candidates perceived able to do the job from within the local government community has declined;
- — an increased trend to bring some "independent assessment" element to the recruitment process;
- — even where there may be potential internal candidates, a growing trend to "test the market";
- — the increased turnover and "mortality" rate of CX's, meaning that local authorities, faced with fishing more frequently in a smaller pool (bearing in mind the general reluctance to "open up" the person specifications to candidates from outside of the local government community) have had little choice but to employ external consultancies (head-hunters) to identify, approach and encourage potential candidates to move jobs; and
- — the desire in some cases to address issues of "diversity" and under-representation, and thus the need to target specific individuals or categories of individuals.

All of the above reasons have served to increase the tendency to use external consultancy assistance (head-hunters) in senior level recruitment. This is a trend that is increasing, steadily.

However, in recent years, the principle reason for the increased use of head-hunters has been a shift in candidate behaviour. 10–20 years ago, candidates typically:

- — will not have been overly concerned about confidentiality regarding their potentially applying for another role;
- — will not have worried too much re the knock-on impact of applying for an external role on their relationship with their Leader, and indeed, likely to have informed their Leader of their action at the outset; and
- — will not have worried too much re the knock-on impact of applying for an external role on the organisation as a whole.

Today, by comparison, we see very different behaviours: Today, the "trend", particularly amongst the strongest and highest profile candidates is for them to be:

- — very concerned indeed about confidentiality;
- — unlikely to wish to "rock the boat" with the Leader unless absolutely necessary, and therefore not tell their Leader that they have applied for another role until they have been short-listed for final panel interview;
- — be very concerned about "leaks" regarding their application, and word getting back to their organisation and potentially "de-stabilising" it;
- — extremely concerned and at times, almost paranoid about seeking promises and guarantees that confidentiality will be maintained and that references will not be taken up until very late in the process:

[It is worth pointing out, here, that public sector is very different from private sector in this regard. Formal current employer references still tend to be taken up prior to panel interview in the public sector, whereas this will almost never happen in the private sector—references only being taken up if the decision has been taken to offer the person the role, and that offer being conditional upon satisfactory references

It is also worth noting that the extent of informal "referencing" (or "checking up on") of candidates for searches conducted for private sector clients tends to be much more extensive than is typically undertaken within the public sector].

— much less willing to "put their hat in the ring" and formally apply for a role where they perceive or think that there may be many other strong candidates applying, and thus the recruitment begins to feel more like a lottery; and

— very nervous about the emotional and physical distraction that preparing an application and going through a full scale interview and assessment process involves unless they think there is a very strong chance they will get the role.

The net consequence of all of the above is that candidates are increasingly:

— sitting on their hands and waiting to be approached and persuaded to apply for senior public sector roles;

— very unwilling to respond directly to job ads;

— assuming that if they are not so approached, then it is highly likely that the employer is not interested in them; and

— unwilling to apply for roles unless they are reassured that their application is likely to be very favourably received, that the effort they will have to put into preparing the application and going through a recruitment process with all the attendant emotional and physical distraction will be worth it and that they are likely to be a "strong contender" to be appointed.

Overall, then, the local government recruitment market (and indeed, at a slightly slower but still inexorable rate, the rest of the senior level public sector recruitment market) is moving towards a more "private sector" model of recruiting, where although, because of the "open and fair competition" tenet, roles are still advertised, the working assumption amongst increasing numbers of employers is that the strongest candidates are likely to be generated through headhunting.

And all this increased having to "tease candidates out of their existing roles" has meant that the balance of power in negotiations has shifted from the employer and more towards the candidate when it comes to talking about remuneration. Thus we have the final key element that has contributed to perceived salary inflation for senior posts within local government.

Polly Toynbee saying "role of head-hunters ought to be looked at in the course of this investigation"[7]

The point that Polly completely missed (and indeed, was incorrect in her evidence) is that, unlike in the private sector, where typically a head-hunter's fee will be based a percentage of their eventual remuneration (their pay), that does *not* apply in the public sector. For the most part and with few exceptions, in the public sector recruitment consultants charge a flat fee, agreed in advance with the client—with the implication that (*and here I am specifically contradicting Polly*), that there is absolutely no incentive (through gaining a higher fee based on a percentage of the final agreed remuneration) for head-hunters to "up the ante" on salaries.

Movement of senior execs between public and private sectors, and vice versa

Lots of people in public sector talk about believing they could do a job in private sector but few do in practice; equally, they keep finding reasons why private sector people would find it hard to do public sector jobs.

"The majority of highly paid senior public sector jobs are not affected by a particular scarcity of suitable candidates"[8] *. . . Taxpayers Alliance*

Candidly, though many of the contributions from the Taxpayers Alliance were interesting and relevant, this particular statement is "utter rubbish".

"More focus on growing talent from within and growing successors . . ." per Chris Johnson

Spot on. This is a massive area of lost opportunity. The extent to which public sector, despite the literal explosion of "leadership development bodies" fails miserably to invest effectively in growing its own talent (especially amongst women and BME communities) is staggering. In this area, the private sector (most particularly within global multinationals) is far ahead of the public sector.

[7] Q 30
[8] EXP 05

To confirm, the supply of suitable candidates for senior roles is hampered and impacted by:

(1) Overly narrow specifications in the person specification.

(2) Those drafting the specifications and making appointments tending to be "pale, male and stale"(and this includes too many of the head hunter advisors).

(3) A tendency to not take perceived risks ("out of the box" candidates—often those from private sector or minority communities and women who may have had what are seen as "unconventional" career tracks) in making appointment and thus appoint "safe" (typically, white, male and more conventional career track) candidates.

(4) "Byzantine" appointments processes that "effectively" un-nerve and often end up discriminating against candidates from outside of the public sector, for whom these processes resemble some archaic, process-driven ritual.

July 2009

Memorandum from FDA

Introduction

The FDA welcomes the decision of the Public Administration Select Committee to launch an inquiry into executive pay in the public sector. The FDA is aware that in the current economic environment there is public concern that relates both to scrutiny of public expenditure and to issues of executive pay across the economy as a whole. As the recession deepens, the public has become more conscious of the increasing inequality in the UK and, while some of the expressions of concern maybe over-heated or irrational, nonetheless valid questions are now being asked about reward in both the public and the private sectors. Moreover, whilst there are significant differences between public and private employment and the issues surrounding executive pay, there are some points of congruence.

Further, in the light of the likely impact of the economic crisis upon public spending, and noting the grim forecast set out in the Budget about the level of government debt, and the major reductions in public expenditure thus anticipated, over the next decade (forecasts which many independent bodies nonetheless regard as optimistic), the public will rightly question all aspects of public expenditure and wish to be satisfied that the tax payer is getting both value for money and "a fair deal".

These concerns are also shared by many public sector employees themselves. Even those holding senior posts in the public services are aware of the wide disparities and the apparent lack of any coherence in pay and reward structures at senior levels across the public sector. This problem is compounded in the public mind by the arguments surrounding the future of public sector pension provision in the context of the collapse of pension provision in the private sector.

This inquiry therefore offers an opportunity to help frame a more meaningful and constructive debate about the executive pay levels since the issue began to be aired widely last year.

In considering the way forward, the FDA sees five underpinning principles:

> Firstly, reward packages and overall pay levels should be seen by the Government, employer and taxpayer as "fair". (There is a concept used in job evaluation of "felt fair" which, whilst not objective, is nevertheless a useful measure).
>
> Secondly, pay levels should be adequate to avoid the public service concerned becoming or appearing to become, an inferior service compared to other parts of the economy. This means that pay levels must have regard to recruitment, retention, morale, motivation and capability.
>
> Thirdly, pay and reward should be transparent. For example, as discussed below, the pay of the most senior staff in the Civil Service is a matter of public record (within a £5,000 band) and levels are set, and the structure determined, by an independent pay Review Body. This is not the case for all senior staff in public sector employment.
>
> Fourthly, there should be a degree of consistency. This not only underpins fairness but assists in movement around the public sector as senior staffs are more obviously transferable without undue salary inflation. The Public Sector Pension Transfer Club which allows people to move across the public sector and transfer pension entitlement without significant loss (and which also applies to MPs who take up office from public sector employment) is a practical example of this approach.
>
> Fifthly, there should be certainty that once a structure or agreement is in place, this will not be constantly changed, particularly for short-term political reasons.

The FDA believes that such principles are best supported by having autonomous and independent pay determination mechanisms, which to a large extent the pay Review Bodies currently offer.

1. *Are the right arrangements in place for setting and monitoring pay and other benefits for top posts in the public sector?*

(a) *Are they fair?*

(b) *Are they transparent?*

(c) *Do they produce the right results?*

(d) *Do they provide value for money?*

(e) *Do they inspire public and political confidence?*

1.1 In considering this question, and subsequent issues raised in this inquiry, there is the difficult matter to consider of what should be understood by the term "public sector". There is no question that one can relatively easily identify the Civil Service, local government and the NHS (although the term "civil servant" is often used to cover senior managers in both local government and the NHS when issues of reward are being argued in the media). We can also add the NDPBs (or quangos) into this framework given that all report through government departments, and HM Treasury has influence over pay levels set (see below). The armed forces and the judiciary (and the UK's parliamentarians) are already covered by the remit of the Senior Salaries Review Body (SSRB) as are doctors and dentists, prison officers, teachers and the police by other pay Review Bodies.

1.2 However, this still leaves substantial room for debate about how wide to extend an inquiry into senior public sector pay given the ambiguous status of universities, the need to consider whether the BBC should be considered within the framework of the public sector or the wider private sector media industry, and public utilities such as Network Rail and the Post Office. There are also organisations such as those delivering the 2012 Olympics which are clearly public sector bodies but for which the Government appears to have explicitly used only the private sector as the comparator in setting salaries. The FDA would welcome debate on how such senior pay in such arms-length publicly funded organisations might be considered.

1.3 As noted above, there is no question that the Senior Salaries Review Body, and the other pay Review Bodies with a remit for senior staff, achieves fairness and transparency in executive pay for those groups for which it is responsible, although the Select Committee will wish to be aware of the anomaly within the NHS where the pay of some Chief Executives, responsible for Primary Care Trusts, is determined by SSRB but other senior NHS managers' pay is determined solely by their Trust within a loose framework set by the NHS.

1.4 A further issue in respect of NHS salaries is that medical consultants are able to receive "merit awards" which relate to the valuable contribution that they make through excellent clinical practice. These graded awards can double a consultant's salary with the highest award and whilst they are restricted in numbers they are held by quite a number of staff. Often, the CEO salary is linked to doctors' pay as it is usually the greater financial award made and it would allow the CEO to keep pace with the general trend. The awards however significantly undermine any concept of parity and appear to remain a closely guarded "perk" that many are unaware exists.

1.5 However, whilst the FDA does not wish to argue that pay for individuals such as Chief Executives of local authorities or of quangos is in any way unfair, there has been relatively little transparency about their pay determination arrangements, and little wider understanding of how decisions are made on overall pay levels or individual reward packages.

1.6 Moreover there is a question not only about simply the mechanisms used for determining reward but also the relationship between the levels of pay across different public sector bodies. Some of the stark differences in pay levels are clearly undermining public and political confidence.

1.7 Evidence of this concern can be seen when, for example, in April 2009 HM Treasury issued its annual "remit guidance" for the use of departments in determining civil service pay and included within this for the first time an obligation upon departments that "the proposal for any pay and bonus arrangements for any NDPB Chief Executives must be submitted to the sponsored department alongside the organisations pay remit. In addition any proposals to re-structure the remuneration package of a Chief Executive must continue to be referred to the Treasury". It is also apparent that Ministers are not confident about pay levels set for local authority Chief Executives in the light of recent statements by John Healey, Minister for Local Government.

1.8 In the Civil Service, the salaries of all Permanent Secretaries and Director Generals (Grade 2s) are published in their department's annual report (given that all these individuals are members of their department's management board). However, local authorities are currently under no obligation to publish the salaries of very senior staff and where they are published there is no immediate explanation of why salaries differ between authorities. Although many London local authorities refuse to publish data on pay, the Chief Executive of Islington earned £152,500 as salary in 2007–08 whilst the Chief Executive of Lambeth earned £193,075 in salary over the same period. There may well be a very straightforward explanation of the differences between those salaries of what are similar local authorities but there is no way of knowing.

1.9 Problems also emerge in comparing pay in the Civil Service. Whilst most civil servants promoted internally have pay levels which, whilst differing, can be assessed and are within the parameters set by the SSRB there are significant differences between the pay of internally promoted members of the Senior Civil

Service and those in comparable SCS jobs appointed from outside, even from the wider public sector. The Select Committee has seen the evidence submitted to SSRB by the FDA and Prospect, and the reports of the SSRB which have highlighted these differences.

1.10 In summary, far too often the Civil Service has focused on recruiting a particular individual and subsequently offering as a starting salary whatever may be required to persuade that individual to take up a civil service post (sometimes at significantly higher levels than the salary earned by the department's Permanent Secretary) rather than, as in most organisations at most levels, setting parameters within which the department is prepared to pay a successful candidate, and ultimately leaving it to the candidate to decide whether to take up an offer of a post at the pre-determined salary. This has been highly wasteful of public expenditure but has also eroded the integrity of the pay arrangements in the SCS and caused significant problems for morale.

2. *Does there need to be consistency regarding these arrangements between different parts of the public sector?*

2.1 It has been noted above that there is no obvious consistency between different parts of the public sector. In the coming period consideration should be given to establishing a more "level playing field" to help to avoid unnecessary salary inflation and facilitate movement across the public sector, as well as helping to allay public concern. This will be however a very difficult task.

2.2 There are two aspects to this issue. Firstly, there is the more straightforward issue of the level of annual increase on whatever salary is in payment. Those public sector staff covered by pay Review Bodies already receive a similar level of annual increase given the framework set by the Government in its annual evidence to individual Review Bodies, and their terms of reference. Using the SSRB as an example, the Government requires them in determining an annual increase to consider factors such as "the need to recruit, retain and motivate suitably able and qualified people to exercise their different responsibilities; regional/local variations in labour markets and their effects on the recruitment and retention of staff; Government policies for improving the public services including the requirement on departments to meet the output targets for the delivery of departmental services; the funds available to departments as set out in the Government's departmental expenditure limits; and the Government's inflation target" (SSRB remit).

2.3 The second, more complicated, aspect is seeking to achieve some degree of relativity between different posts across sectors. In turn, the first step towards this would be greater relativity within individual sectors, in particular in local government where as already noted Chief Executive salaries differ considerably. There would then need to be a gradual realignment of pay levels more widely which would probably need to be underpinned by a process of job evaluation.

2.4 The FDA is not arguing that there should be one pay structure or job evaluation scheme (or a complex of evaluation schemes) operating across the public sector given the many different accountabilities that senior managers and professionals face across the public sector. However, it would be possible for all senior staff in the public sector to be brought within the aegis of a Review Body (which might require establishing new bodies eg for local government, or significantly extended the remit of the SSRB), and through this route it is not inconceivable that a basic system of job weighting could be extended across the main functional areas of the public sector that would enable those responsible for pay setting to determine a framework within witch a pay level could be established. Even without a formal job evaluation mechanism, it is possible to adopt some of the underpinning concepts of job evaluation, such as the size of responsibilities and the degree of autonomy and decision-making, to assist in pay determination.

2.5 Given the considerably greater scrutiny that is likely that is to be brought to bear in the coming decade on public sector reward, such an approach may be the only way of allaying public concern.

3. *Does there need to be comparability of pay between top posts in the public sector and equivalent posts in the private sector?*

(a) *If so, how should equivalent posts in the private sector be identified?*

3.1 An even more difficult question than that of pay relativities across the public sector arises in seeking to determine relativities between the public and private sectors. There is experience of such an approach in the Civil Service. Until 1996, the pay of what is now the core grade of the Senior Civil Service (Assistant Directors or Grade 5's, who were not then under the aegis of the Top Salaries Review Body but instead had their pay determined by collective bargaining between the FDA and HM Treasury) was adjusted every four years on the basis of a "levels survey".

3.2 In summary, the Office of Manpower Economics (which acts as the secretariat to all of the pay Review Bodies) oversaw a process by which consultants designed a job evaluation system for the particular exercise and then compared a range of civil service posts with the pay of private sector posts that appeared to be comparable in function, selected by the consultants. An assessment was then made of the overall reward package of a particular private sector post compared to the reward package for a comparable civil service job. Although time-consuming, this four-yearly exercise did enable civil service posts to maintain a relationship with pay in the private sector that also allowed the Civil Service to compete adequately in a wider market.

3.3 The annual level of any pay increase between the four-yearly "levels exercise" was then determined by an annual pay "movements" index which was based on a basket of increases awarded to private sector workers. This meant that public sector annual pay increases were broadly in line with those in the private sector and seen to be fair across the wider economy. It would be easy to restore such an index.

3.4 Were such an approach to be considered again, it would also be important to look at the reward package on the basis on lifetime earnings (both in work and in retirement) rather than simply at work at that moment. The FDA believes that this would demonstrate that, as far as the Civil Service is concerned, what may appear to be a better pension arrangement does not fully compensate for the difference in salary during the working career.

3.5 Ultimately the Civil Service, or rest of the public sector, cannot isolate itself from the outside labour market pressures completely, nor should it be seen to be chasing short term market movements one way or another. A balance has to be struck between rewarding public servants fairly so they will feel valued and not be constantly looking for opportunities elsewhere, and the need to reflect concern over the use of public money.

4. *Is there evidence of executive wage inflation caused by public sector organisations competing with one another for candidates?*

4.1 The FDA has highlighted the growing gap between the pay of internally promoted Senior Civil Servants and that of other senior public sector staff, as have the SSRB and Civil Service Commissioners. This is one factor in the "dual market" referred to in paragraph 1.9, as the Civil Service has recruited externally and found itself paying higher salaries to new entrants from elsewhere in the public sector. The Government has also referred recently to wage inflation in local government as a "market" has developed for Chief Executives and other senior managers.

5. *What role should consultancies play in the determination of pay for top public sector posts?*

5.1 There would almost certainly have to be a role for consultancies in the determination of pay for public sector posts, just as there is in supporting the existing work of pay Review Bodies. However, this must be seen as a support and technical role for organisations such as pay Review Bodies rather than a delegation of decision making to management consultants. Any other approach is only likely to exacerbate public and political concern.

5.2 Many local authorities currently employ consultants to help set senior pay levels, but there is no obvious transparency.

6. *Is the balance right between executive pay and other benefits? eg bonus, pension*

6.1 Consideration does need to be given to the different elements of public sector reward. The current Government has fostered the extension of performance related pay arrangements for many public sector workers, together with a major extension of the use of bonuses.

6.2 The use of such bonuses has in practice caused considerable reputational damage to senior managers in the public sector, even where such bonus arrangements, as in the SCS, bear no relation either in size or in their framework to bonus arrangements usually operating in the private sector. (The SCS bonus system is simply a method for distributing a percentage of the annual pay increase but in a way that is cheaper to the tax payer because it does not incur "on costs" for the employer such as a pension contribution, and is in reality a form of variable pay).

6.3 Many tax payers fail to understand why someone should be recruited at a salary well above the national average and then receive a bonus for simply doing the job they have been employed to do. As an example, delivering an aspect of the Olympic preparations by July 2012 rather than January 2013 is at the core of the job itself, not a welcome addition. (And it is, as an aside, noticeable that the Government has not proposed the use of either performance related pay or bonuses for Ministers themselves).

6.4 Performance related pay is now common at even the most junior levels of employment, but as with bonuses, the FDA can find no evidence that there is any impact on performance and such forms of pay are often as much a demotivating factor as a boost to morale.

6.5 There are more subtle motivating factors for senior managers and professionals, including the "public sector ethos". Put simply, most senior public servants are very committed to their work, want a fair level of pay and a reasonable pension, and the restoration of professional discretion and autonomy (and less political scapegoating) are far more important than bonuses. A fuller analysis of the problems associated with performance pay and bonuses for the SCS has been set out in the FDA's evidence over recent years to the SSRB which the Select Committee has seen. Further, evidence of the corrupting influence of bonus systems in the finance sector has been all too publicly displayed over the past year.

6.6 The FDA can find no evidence to justify the extension or continuation of such arrangements in the public sector and would welcome their phased withdrawal in the coming years. This has to be in the context of resolving the long term pay issues for the SCS rather than simply abolishing one aspect of the reward mechanism.

6.7 The aspect of reward that has raised the greatest public concern and political debate is pension provision. Whilst all of the public sector pension schemes have been reformed and have reduced costs in recent years, they currently have similar structures even if contribution levels and benefits, together with some other technical aspects of schemes, differ slightly. All are defined benefit schemes and, moreover, pension schemes in the public sector operate in the same way for staff at all levels. For example, a Permanent Secretary is a member of the same pension scheme as an Executive Officer paid a tenth of the Permanent Secretary—only the size of the pension differs, not the quality of benefits. The major change has been the introduction in 2007 of a career average (but still defined benefit) scheme for all new civil servants in place of the final salary scheme.

6.8 Moreover, not only has the cost of public sector pensions if anything reduced in recent years, defined benefit schemes in the private sector are similar in scope and employer cost to those in the public sector. However, the vast majority of private sector workers who are in a pension scheme at all are now in defined contribution schemes which offer considerably poorer benefits than defined benefit schemes, and the closure of many private sector defined benefit schemes, and rapid erosion of pension provision more generally in the private sector, has led to criticism and at times resentment of public sector provision. (It should be noted though that the exception to this rule in the private sector is usually at senior executive level where very generous defined benefits schemes are still often found, as the excesses of Sir Fred Goodwin's pension entitlements at RBS have all too vividly illustrated).

6.9 The FDA believes that the current public sector pension provision is fully justified, and affordable in the long term. Most of the media criticism is economically ill-informed, and the answer to the problems of private sector pension provision should not be a rush to a lowest common pension's denominator, an "equality of misery", but to address the need for better pensions for private sector workers. The pension is also an integral part of the reward package for senior public servants and any attempt to remove or dilute it would inevitably create an inflationary pressure on the other elements of the pay package.

7. *Do the pay levels for top posts in the public sector have a direct impact on the performance or qualities of the people filling those posts?*

(a) *What impact do the performance or qualities of the people filling top posts in the public sector have on the performance of the organisations for which they work?*

7.1 Clearly, high calibre candidates with a proven track record are likely to be able to secure higher pay levels than less experienced or slightly less capable colleagues. Moreover, many of the skills necessary to manage large public sector organisations have a market value in the wider economy, particularly once the economy recovers from the current recession. However, the FDA has not seen any evidence one way or the other that establishes a direct link between the reward package and performance.

7.2 That said, obviously some senior executives have stronger leadership capabilities or, for professionals, greater expertise in their particular field, that can benefit the overall performance of the organisations in which they have a senior role, and the FDA has been supportive of work to enhance leadership and management capabilities in public sector bodies.

8. *Is there an appropriate benchmark or ceiling for top public sector salaries—eg the salary of the Prime Minister, or a factor of average pay?*

8.1 In considering the question of relativities in the public sector (including the possible use of a simple framework of job evaluation), the FDA has focussed on the problem of relativities between different public sector senior managers and professionals. However, we recognise that any such an approach is also likely to have to take account of the remuneration package for elected parliamentarians, although it will be difficult to address this until decisions are taken on the remuneration for MPs more generally in light of the scandal of MPs' expenses.

8.2 However, elected politicians are not in a conventional employment situation and the FDA is wary of trying to establish a straightforward correlation between the reward package for politicians and that for senior public sector executives. There was historically a link between the levels of MPs' pay and that of a certain grade of civil servant (Grade 6/Senior Principal). However, in practice this led to distortions in the civil service pay arrangements as changes felt necessary for the efficiency of the pay system were extremely difficult to implement because of their political implications.

8.3 Successive governments have not helped this discussion by pegging back the levels of the salaries of MPs and Ministers (including the pay of the Prime Minister) in many years as a political gesture, as we now know relying on extensive expenses regime to "cushion the blow". This has over the medium term been a very short-sighted strategy and has left Ministerial pay at a level that is not necessarily comparable to relevant public sector roles.

8.4 It is not obvious therefore that one single benchmark is a sensible mechanism, but rather senior pay should be considered holistically and a better appreciation of fair relativities introduced in line with the principles set out in the introduction.

9. *Can England and the United Kingdom learn from the experience of other countries or the devolved governments in this area?*

9.1 The FDA is not aware of any such experience that would be helpful to this inquiry.

April 2009

Memorandum from the Hay Group

This paper does not attempt to answer all the Select Committee's questions—although we would be happy to do this—but concentrates instead on a few observations and suggestions.

Comments on Executive Pay in the Public Sector

Committee Members, MPs and members of the public are understandably concerned about the value for money they get from public sector pay. We believe that the best way to improve value for money is not to complain about specific salary levels or bonus payments but to look at the market as a whole and concentrate public and regulatory attention on a small number of practicable reforms.

First, therefore, some comments about public sector reward systems:

1. *The Public Sector is not one market*

Public sector organisations occupy a broad spectrum. In practice they operate very differently and it will not help them or the taxpayer to lump them all together. For example, the Senior Civil Service is largely recruited from within the ranks of public servants rather than in the open market. Unsurprisingly, they have the lowest base salary levels of all main public services.

Local government offers higher salaries for jobs of similar weight and challenge, but this is because chief executives, directors and heads of service are recruited in the open market across the UK. In addition, as the Audit Commission has noted, pay has begun to reflect the performance of councils as measured by Comprehensive Performance Assessment and there is a demand for senior managers who have helped to improve local authorities ("Tougher at the Top?", Audit Commission discussion document July 2008).

Universities recruit their Vice Chancellors in the international market—mainly from other higher education institutions—and they select the heads of business schools from among international competitors and the private sector. The pay of university heads has increased significantly in recent years and heads of business schools receive more. In both higher education and business schools, international measurement systems are available which enable recruiters to identify people who are associated with the best performing organisations, just like they can in local government but this time on the international stage.

So even in the public sector, pay levels reflect the openness of the market and the track record of the individual. The point is underlined by experience in the Senior Civil Service, which recruits a minority from the wider market. That minority is paid around 20% more than those who have been promoted within the service (Government Evidence to the Senior Salaries Review Body, December 2008).

2. *The sector includes a wide range of organisations*

Policy towards the public sector in recent years has created a spectrum of organisation types. In part, this spread reflects the level of control from the centre of government, in part the opportunity and responsibility to operate commercially.

For example, central departments and the agencies which they fund are relatively closely controlled and are subject to the standard Senior Civil Service pay arrangements. There are various public bodies which have earned greater autonomy and are more likely to determine their own pay arrangements at executive level such as academy schools, foundation trust hospitals and agencies operating as Trading Funds. Then at one further remove from direct control are public corporations and government owned companies, which determine pay themselves throughout their employment structure. As public sector organisations become more independent and commercial, they are more likely to operate in the open recruitment market and to see a need to match wider market practice in salary level and the configuration of the total employment package.

These differences are reflected in the NHS in England. The directly managed part of the NHS including Strategic Health Authorities, Ambulance Services and Primary Care Trusts—is covered by the national framework for Very Senior Managers, which is reviewed annually by the Senior Salaries Review Body. Provider trusts which do not have foundation status set executive pay locally. Foundation Trusts also set executive pay locally, have further pay freedoms and certainly pay more than the Very Senior Manager system, although their governance arrangements (including for remuneration) are regulated independently by Monitor.

While the position in the NHS is a little confusing, it makes sense to relate autonomy in setting pay to the acquisition of other policy and commercial freedoms.

3. *There is an overreaction against performance related pay in all its forms*

There is a long tradition of hostility in most of the public sector both to linking salary progression to performance and to the use of bonuses. The Senior Civil Service, senior jobs in local government and the commercial public sector are exceptions, but outside these groups it is often argued that linking performance and pay does not suit the work and culture of the public sector.

Suspicion of performance related pay has grown recently as a reaction to the bonus culture in City institutions and certain banks and the combination of high bonus payments and obvious performance failures. However, the investment banking sector is not typical of how performance-related incentives operate in the private sector. Just because a few organisations pay far too much for the wrong things does not make the whole principle bad. In addition, in spite of indications to the contrary from recent publicity, a good system of bonuses and incentives takes care to encourage people to do the basics well and then to achieve more on top. It does not reward them for meeting a few targets while ignoring the main features of the job.

Most important, it is only sensible to relate rewards to performance. The alternative is to pay people the same whether or not they perform—which is not even common sense, let alone good use of public money.

The real difficulty with public sector pay is that it is not sufficiently related to performance. The negotiated pay systems covering the majority of public sector staff, generally up to quite senior levels, are still dominated by incremental pay structures which reward length of service and discourage effective performance management. Some executive pay also bears little relationship either to the performance of the organisation, or the top team or the individual.

The most obvious example is the NHS, where many top salaries are supposedly set based on market rate and little use is made of bonus payments. The approach is exemplified by the Remuneration Report from one of the country's largest Foundation Trusts, which states: "No element of the executive directors' remuneration is performance related". This cannot be right. It is essential to provide a clear definition of good performance, and executives should not continue to receive high salaries and good increases unless they deliver the required performance.

Finally, insofar as public service has operated performance-related, non-consolidated bonuses, these have tended to be focused on individual rather than organisational performance. As such they are much harder to justify to external stakeholders than arrangements related to the value the organisation itself delivers.

4. *Stakeholders should have information but not all public bodies provide it*

There has also been debate about the right of the public to clear information about the pay of executives in the public service.

The clearest rules and practices of disclosure are in the commercial public sector and the NHS, where top team salaries, bonuses and pension entitlements are published—although the salaries are often in bands rather than actual figures. There is also a strong element of disclosure in: the Senior Civil Service (where permanent secretaries' salaries are published and information about the top 5,000 or so civil servants is released each year); police forces, where salaries are set and publicised nationally; and universities, which state the remuneration of the Vice Chancellor and list other senior salaries in bands.

The exception among major organisations is local authorities. They do not generally publish annual accounts in a format which members of the public can obtain and understand, nor do they disclose the remuneration of the top team. Most public information about executive pay in local government comes from press articles and freedom of information requests by individuals and lobby groups.

It is arguable that all organisations funded by the public should have a common duty to disclose executive remuneration at least to the standard required of a PLC. At very least, there should be a duty placed on local councils to make available the remuneration of the chief executive and directors.

Whilst there is some evidence that pay disclosure creates pressure for pay increases from executives, there is also strong evidence (from both the public and private sectors) that transparency improves the decision making of remuneration committees. On balance pay disclosures are of net benefit to the setting of appropriate pay packages, even leaving aside the governance arguments for such disclosures.

5. *Remuneration Committees should consider the terms and conditions of senior executives*

Many public sector bodies have—or are working towards—single sets of terms and conditions that apply across the whole workforce. Whilst "single status" is a useful principle for the wider employee population, it is debatable whether this approach should apply at top executive level. In our view, senior executives should be employed on service contracts with terms and conditions that are appropriate to their roles and which reflect the significant pay they receive. As a specific example, it is inappropriate for senior executives to be eligible for generous redundancy payments.

6. *Pensions are a separate issue*

In recent years, the private sector has moved away from final salary pension schemes because their cost is unsustainable. Whilst a proportion of longer-serving private sector executives are still in final salary schemes, some companies are looking to end even these legacy entitlements—a process that is likely to be accelerated by the changes to pensions taxation set out in the 2009 Budget.

Meanwhile, although there have been changes in entitlements, the major public sector schemes still offer final salary or at least (for new joiners) salary average schemes, with index linking and at modest employee contribution rates. The cost of many schemes has been pushed-up by above inflation salary growth in parts of the public sector and the tendency to target pay increases into consolidated salary. For a long-server the pension costs of any salary increase will far outweigh the value of the salary increase itself.

There has already been public and media comment on the gap between public and private sector pensions and disquiet on this point can be expected to grow. We believe that this point should be separated from concerns about pay and given proper attention in its own right. Public sector pay is not necessarily too high but simply too detached from performance. But the public sector pension bill is extremely high and, sooner or later, the gap between different parts of the economy will have to be reduced.

However, we would note that the pension gap between public and private sector is much less evident at senior levels. This reflects the private sector practice of providing proportionally higher pension benefits to senior executives.

Suggestions on public sector pensions policy go beyond the scope of the Committee's inquiry and we therefore do not include any below. However we would observe that a potential solution that might be acceptable to all stakeholders would be as follows:

— insofar as public sector pension provision continues to be linked to final or average salary, these arrangements should be capped at a given level of salary (say, £30,000); and

— provision on the slice of earnings above this level should be on a defined contribution basis.

Suggestions

Our suggestions are simple:

(a) There should be no attempt at greater intervention in the public sector market, diverse as it is or at capping the salaries of particular groups. This will simply constrain rewards for specific organisations and limit their access to talent.

(b) The regulatory framework for executive pay in the public sector should concentrate on three areas:

  — The requirement for a full and published policy on executive remuneration and a clear process for setting and reviewing it, overseen by a properly constituted, trained and advised Remuneration Committee.

  — A consistent requirement for disclosure of executive remuneration which applies throughout the public sector (ie organisations which are wholly or mainly funded by direct or indirect public grant). This requirement should include local authorities. As part of this requirement, the practice of disclosing salaries in £5,000 bands should be replaced with disclosure to the nearest £1,000 in line with private sector practice.

  — A duty on Remuneration Committees to relate pay to performance (of the organisation, team or individual, as appropriate) and to explain in their policy statement how this link works.

(c) Where public sector executives receive pay and benefits that are competitive in the wider external market, their terms and conditions of employment should also reflect conditions in the external market.

May 2009

Memorandum from the Higher Education Funding Council for England (HEFCE)

Bonus Information

HEFCE's previous Chief Executive, Professor David Eastwood, was employed by HEFCE from 1 September 2006 to 31 March 2009. His entitlement to an annual non-consolidated cash bonus payable in April each year was subject to the following criteria:

Outstanding 10%; Very Good 8%; Good 5%; Acceptable or Weak 0%.

Following appraisal by the HEFCE Remuneration Committee he actually received a 10% non-consolidated bonus on 1 April 2007, 2008 and 2009. The bonus information for HEFCE Chief Executives since we began as a Non-Departmental Public Body on 1 April 1993 is provided in the table below.

CE BONUS

Financial Year	*CE*	*max bonus*	*actual*
2008–09	David Eastwood	10%	10%
2007–08	David Eastwood	10%	10%
2006–07	David Eastwood	10%	10%
2005–06	Sir Howard Newby	9.92%	9.92%
2004–05	Sir Howard Newby	10%	10%
2003–04	Sir Howard Newby	10%	10%
2002–03	Sir Howard Newby	10%	10%
2001–02	Sir Howard Newby	10%	10%
2000–01	Sir Brian Fender	10%	10%
1999–2000	Sir Brian Fender	8%	8%
1998–99	Sir Brian Fender	8%	8%
1997–98	Sir Brian Fender	8%	6%
1996–97	Sir Brian Fender	8%	4%
1995–96	Sir Brian Fender (from October 1995)	£2,250	£2,000
1995–96	Sir Graeme Davis (to September 1995)	0%	0%
1994–95	Sir Graeme Davis	0%	0%

July 2009

Memorandum from the Institute of Directors

About the IoD

The IoD was founded in 1903 and obtained a Royal Charter in 1906. It is an independent, non-party political organisation of approximately 50,000 individual members. Its aim is to serve, support, represent and set standards for directors to enable them to fulfil their leadership responsibilities in creating wealth for the benefit of business and society as a whole. The membership is drawn from right across the business spectrum. 81% of FTSE 100 companies and 73% of FTSE 350 companies have IoD members on their boards, but the majority of members, some 70%, comprise directors of small and medium-sized enterprises (SMEs), ranging from long-established businesses to start-up companies. IoD members are entrepreneurial and resolutely growth orientated. More than two-fifths export. They are at the forefront of good working practices and have embraced the technology of the new economy.

IoD Response to the Inquiry

Our responses to the questions posed by the Committee are followed by further IoD data and recommendations.

Direct Response to Questions

1. *Are the right arrangements in place for setting and monitoring pay and other benefits for top posts in the public sector?*

No.

(a) *Are they fair?*

No.

(b) *Are they transparent?*

No.

(c) *Do they produce the right results?*

No.

(d) *Do they provide value for money?*

No.

(e) *Do they inspire public and political confidence?*

No.

2. *Does there need to be consistency regarding these arrangements between different parts of the public sector?*

Not necessarily, what matters is getting the right people to do good jobs and then being completely transparent about the total remuneration (ie salary, bonus, benefits in kind, employer pension contribution etc) they receive. Transparency is certainly one area where there is a damaging lack of consistency at present. For example, government department accounts list directors' remuneration, but local authority accounts do not. There should be full transparency for all public bodies.

3. *Does there need to be comparability of pay between top posts in the public sector and equivalent posts in the private sector?*

Some sort of comparability may be useful, but only as a guide. There has to be a risk factor included ie the risk of dismissal for poor performance is much greater in the private sector, and so remuneration should be correspondingly higher in the private sector.

(a) *If so, how should equivalent posts in the private sector be identified?*

Not solely from looking at the City of London and the largest UK companies. It is often argued that public sector executives could walk into City jobs. In some cases this may be true but, for executives who have spent their whole careers in the public sector, it is not obvious that this is the case.

4. *Is there evidence of executive wage inflation caused by public sector organisations competing with one another for candidates?*

Yes, although we don't have any systematic evidence. But anecdotally, it is clear that senior civil servants and local authority executives, for example, frequently move from department to department, or from authority to authority, and receive higher remuneration. It is also worth examining reorganisations in, for example, local authorities, which tend to be accompanied by large increases for directors.

5. *What role should consultancies play in the determination of pay for top public sector posts?*

None. Using consultants for this purpose is a waste of taxpayers' money and should be done in-house. There is a genuine risk of a form of cartel if the same consultancy advises a number of different public sector organisations.

6. *Is the balance right between executive pay and other benefits? eg bonus, pension*

What matters is not the relative size of salary, bonus and pension but whether it is sufficiently tied to proper performance measures. It seems that this is far from the case at the moment.

7. *Do the pay levels for top posts in the public sector have a direct impact on the performance or qualities of the people filling those posts?*

Again, it's not about the precise level, but whether pay and conditions are tied to performance, so that good performance is rewarded and poor performance results in dismissal.

(a) *What impact do the performance or qualities of the people filling top posts in the public sector have on the performance of the organisations for which they work?*

As in any organisation, the quality of the leader is crucial to the organisation's success. However, senior civil servants generally operate under greater constraints than private sector executives.

8. *Is there an appropriate benchmark or ceiling for top public sector salaries/eg the salary of the Prime Minister, or a factor of average pay?*

It is difficult to say. The old culture of public service would lead to the conclusion that, yes, there should be a ceiling, and that being paid more than the Prime Minister is excessive. A new model, where executives move in and out of the public and private sectors and are much more accountable for their performance, would suggest that such a ceiling would limit the private sector talent that could be brought in. However, we currently seem to be in the worst of all worlds—a disappearing culture of public service, few executives moving between the public and private sectors, insufficient accountability, and high levels of remuneration.

9. *Can England and the United Kingdom learn from the experience of other countries or the devolved governments in this area?*

There are lessons to be learnt about transparency from the US. In a number of US states, the salaries of all state employees are available online for anyone to see. We would suggest that this could be adopted across the public sector in the UK for those with remuneration of £50,000 or more. The Obama administration has also frozen the pay of White House staff earning more than $100,000. In the middle of a recession, with increasing numbers of private sector firms agreeing pay freezes, this is a measure that could be followed. When recovery begins, there will need to be a severe fiscal tightening to restore the public finances to balance, and so such a measure could be adopted for senior public sector staff in the UK.

1. Existing Data on Executive Pay and Benefits

In addition to our responses to the above questions, the IoD has extensive member survey data on pay and pensions that may be useful when considering the issue. Some sort of comparison can be made with data concerning the public sector.

1.1 Basic pay for an IoD member who is a managing director of a small company (up to £5 million turnover) was £65,000 last year, for a medium-sized company £100,000 and for a large company (£50 million to £500 million turnover) £150,000.[9]

1.2 54% of IoD members who are managing directors of small companies received a bonus or dividend averaging £24,000 last year. For medium-sized companies the average bonus/dividend was £25,000 received by 61% of managing directors and in large companies the average was £42,000 received by 67% of Managing Directors.[10]

1.3 In the public sector, executive pay data is rather patchy. The most comprehensive pieces of research on the subject that we are aware of have been conducted by the TaxPayers' Alliance. The organisation's survey of executive pay in local authorities found over 800 executives receiving total remuneration of more than £100,000, including 14 earning more than the Prime Minister and 132 earning more than Cabinet Ministers.[11] Similarly the organisation found that, among 140 government departments and other public bodies surveyed (excluding local authorities), there were almost 400 people receiving total remuneration of more than £150,000 a year, including 21 people earning more than £500,000 and almost 200 earning more than the Prime Minister.[12] This represents strong evidence that executive remuneration in the public sector is more than comparable with that in the private sector.

1.4 The gap between the public and private sectors with regard to pensions is extremely large. And this applies to executives as well. Almost half (45%) of IoD members (encompassing directors of small, medium and large companies) are not members of an occupational or employer-sponsored pension scheme at all. 12% of directors are members of occupational defined benefit schemes, interestingly, the same proportion as in the private sector as a whole. The remainder of directors are members of occupational defined contribution, group personal pension or employer-sponsored personal and stakeholder pensions.[13]

1.5 By contrast, in the public sector, 90% of employees are members of defined benefit pension schemes.[14] In terms of individual retirement benefits in the public sector, again as far as we know the TaxPayers' Alliance has undertaken the most comprehensive research, estimating that there are over 17,000 retired public sector employees with retirement benefits worth at least £1 million each.[15]

1.6 Large bonuses and "golden parachutes" were once the preserve of the private sector. But the evidence suggests that they are on the increase in the public sector, and are not necessarily rewards for good performance.[16] Indeed, it is clear that rewards for failure are not confined to the banking system.

2. IoD Recommendations

It is reasonable to argue that executive remuneration in the public sector has got out of line, especially when considered alongside performance. The current recession makes the issue all the more important. In addition to our responses to the questions posed, we would offer the following suggestions to improve the situation.

2.1 First, the important measure to consider is not salary, but total remuneration. Total remuneration should cover such items as salary, bonus, benefits in kind, London allowances, relocation allowances, employer pension contributions and redundancy/early retirement payments. Annual increases of total remuneration should be analysed.

2.2 Second, we would suggest that the total remuneration, including a detailed breakdown, of all public sector employees with total remuneration of more than £50,000 (certainly all those with total remuneration of more than £100,000) could be published on a central website accessible to the public. The website could allow name searches, allow browsing by public sector organisation (including local authorities and

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9 IoC/Croner Rewards Survey, November 2008.
10 Ibid.
11 TaxPayers' Alliance, "Town Hall Rich List 2008", March 2008.
12 TaxPayers' Alliance, "Public Sector Rich List 2008", November 2008.
13 IoD survey of approximately 1,000 members, February 2009. In 2007, the latest year for which data is available, there were 2.7 million members of occupational defined benefit pension schemes in the private sector, just under 12% of the 23.4 million private sector workers in that year (sources: Office for National Statistics, "Occupational Pension Schemes Annual Report 2007", September 2008, Table 3.3; Office for National Statistics, "Public Sector Employment Q3 2008", December 2008, Table 5—includes private sector employment data). It is interesting that membership of DB pension schemes follows the same pattern among private sector directors as among their employees.
14 Office for National Statistics, "Occupational Pension Schemes Annual Report 2007", September 2008, Table 3.4; Office for National Statistics, "Public Sector Employment Q3 2008", December 2008, Table 5.
15 TaxPayers' Alliance, "The UK Pensions Crisis", November 2008.
16 To give two examples, in 2007 the former chairman of HMRC, Paul Gray, resigned following the department's loss of millions of child benefit records. He was paid £137,000 for his departure. David Higgins, the chief executive of the Olympic Delivery Authority, was paid a performance-related bonus of £205,000 in 2007–08, despite the budget for the Games rising to over £9 billion (source: TaxPayers' Alliance, "Public Sector Rich List 2008", November 2008).

quangos), and keep historical data so that remuneration increases can be tracked, including for individuals who move between organisations. It is important that people receiving large amounts of taxpayers' money be accountable in this way.

2.3 Third, the level of remuneration should contain a sizeable performance element, although performance should not be simply a box-ticking exercise. This must be accompanied by loss of performance pay or dismissal for poor performance. Too often, bonuses of equal amounts are paid out to the directors of a public sector organisation, which suggests that individual performance is not monitored.

2.4 Fourth, it should be recognised that the risk of dismissal is far lower in the public sector than in the private sector (notwithstanding the above recommendation) and that executive remuneration should therefore be lower in the public sector to compensate for this reduced risk.

2.5 Fifth, the severe fiscal crunch that will be required to restore the pubic finances after the recession is over presents a great opportunity for reform of the current arrangements. Indeed, a performance bonus for permanent secretaries, conditional on the individual's success in reducing administration and overhead costs without cutting frontline services, would be a positive development. Similarly, an incentive to deliver savings on regulatory burdens for businesses would be a very useful aid to economic recovery.

Thank you once again for inviting the Institute of Directors to participate in this inquiry. We hope you find our comments useful. We would be very happy to give oral evidence if required. Should you have any questions, please do not hesitate to contact me.

March 2009

Memorandum from Christopher Johnson

Personal Background

I welcome the opportunity to give evidence to the Committee and to assist with its inquiry in to executive pay in the public sector. For over 20 years, I have worked with leading management consultancies, including Hay, Towers Perrin and currently Mercer, providing reward advice to large organisations in the private and public sectors in the UK, US and other countries in Europe and Asia. Between 2005 and 2008, I was the Director at the Cabinet Office responsible for employee relations and reward across the Civil Service, which included responsibility for senior civil service reward.

Currently, I lead Mercer's human capital business in the UK, which includes provision of advice on executive remuneration and broader workforce planning, performance and reward to a range of clients in the private and public sectors.

My evidence draws on my involvement in public sector reward over more than two decades.

Evidence to the Committee

1. The first part of this evidence is a brief response to each of the Committee's questions. This is followed by observations about possible ways forward for determining and managing executive reward in the public sector.

Response to the Committee's Questions

Are the right arrangements in place for setting and monitoring pay and other benefits for top posts in the public sector?

2. No. Executive reward is set and monitored through different mechanisms—pay review body, remuneration committees (with and without external membership), management process and political decision—there is no coherent approach to or common set of principles for executive pay in the public sector. There is public and political disquiet about executive reward in the public sector. There has not been a debate about the appropriate arrangements for rewarding senior public servants.

(a) *Are they fair?*

3. If "fair" implies reasonable and appropriately consistent, no.

(b) *Are they transparent?*

4. The level of transparency in the public sector varies across the sector; it would be helpful if there was more consistency broadly in line with that adopted in other parts of the economy.

(c) *Do they produce the right results?*

5. No. Overall, executive reward in the public sector is not well managed. It insufficiently supports the acquisition, development, management and retention (and exit) of the talent required to provide leadership of service delivery for and on behalf of citizens and to ensure value for money for the taxpayer.

(d) *Do they provide value for money?*

6. It is unclear. The cost of employing public sector talent is low compared with the private sector. That low cost may result in less competent talent being available to provide leadership of service delivery for and on behalf of citizens and to ensure value for money for the taxpayer; evidence on the calibre of public sector executive talent is unclear.

(e) *Do they inspire public and political confidence?*

7. No. The continued debate suggests that more needs to be done to inspire confidence. There has not been an informed public or political debate about executive reward (or reward for the workforce generally) in the public sector; the Committee's inquiry may provide the basis for building confidence in future arrangements.

Does there need to be consistency regarding these arrangements between different parts of the public sector?

8. The degree of consistency depends to a large extent on the public sector's approach to the acquisition, development, management and retention of the talent.

9. Part of a talent strategy for public sector organisations should be the internal development of senior talent, which would be consistent with best practice in other large organisations. At the same time, it is important for public sector organisations to have access to leading practices, experience from other parts of the service delivery system, innovation and the stimulus of alternative thinking. This implies part of a talent strategy should be the acquisition of proven talent from other parts of the public and private sectors.

10. In my experience in the Civil Service, it proved easier to recruit talent from the private sector to senior roles in the public sector than from other parts of the public sector. Private sector candidates were attracted by the intrinsic value of the work and quality of experience to be gained, and this was a part of the "package" along with reward. However, candidates from other parts of the public sector already enjoyed intrinsically valuable work and had gained quality experience. The gap in pay between the Civil Service and chief executives in local government and senior managers in the NHS, made it difficult to attract candidates from those parts of the public sector.

11. Looking forward, it is reasonable to anticipate greater inter-change across the public sector. This suggests that there will need to be more consistency between different parts of the public sector than today. However, consistency should take the form of principles leaving scope for decisions to reflect local and individual circumstances.

Does there need to be comparability of pay between top posts in the public sector and equivalent posts in the private sector?

12. Comparability is broader than just pay levels. It covers three broad elements of reward:

— Level—the amount of reward available.

  Although actual reward levels for senior civil servants are significantly lower than for comparable roles in the private sector, there is flexibility in the pay structures to offer external candidates reward at more competitive levels, though still below what they earned in the private sector. Most external candidates from the private sector have taken a reduction in pay because they also place value on the professional challenges and public sector ethos.

  However, use of flexibilities to facilitate recruitment is causing problematic internal relativities between external candidates and internal appointments; there is, in effect, a two tier workforce amongst senior civil servants and this situation is unsustainable in the near to medium term.

— Structure—the balance of fixed and variable reward reflecting performance delivered or not, in the short and longer terms.

  Variable performance related pay in the public sector is limited and is significantly lower than both in the private sector and what would be effective recognition for performance delivered. Public sector variable pay should not be as geared as for the private sector, but the risks and rewards of performance accountability should be higher than at present.

  An issue that confuses the debate about performance related pay is the term "bonus": it used pejoratively by commentators to imply *additional* reward. It would be helpful to use language more clearly to mean variable or conditional pay that can be lower or higher depending on the performance delivered.

— Scope—reward is a much broader concept than just pay.

  Some parts of the public sector manage total reward (as do many private sector organisations), which covers pay; benefits including pension; career development and management; and, work life factors. In the debate about executive *pay*, these other factors can be overlooked—see question 16 below.

(a) *If so, how should equivalent posts in the private sector be identified?*

13. The focus should be on relevant organisations and functional roles in those organisations. But it is important not to create an expectation of like for like pay determination. Comparability should be one input in determining pay alongside other factors that enable the public sector to attract and retain the talent it needs, and that take into account affordability.

Is there evidence of executive wage inflation caused by public sector organisations competing with one another for candidates?

14. Anecdotally, yes. The market most often mentioned is for local authority chief executives and chief officers in which local authorities compete with each other to recruit and retain successful talent. Base pay has risen over the last few years at about twice the rate of, for example, the Civil Service. About a third of local authority chief executives are paid at or above the same level as permanent secretaries, which has made it difficult to attract chief executives into the Civil Service.

What role should consultancies play in the determination of pay for top public sector posts?

15. Although there are individual exceptions, the overall competence of reward professionals in the public sector is low; this impacts the effectiveness of reward strategies and pay management. Consultancies play a valuable role providing reward management advice and developing reward management capabilities within the public sector.

Is the balance right between executive pay and other benefits? eg bonus, pension

16. No. There are three areas where a better balance can be struck between the different elements of reward. A better balance should result in more cost-effective reward arrangements measured by employment costs, performance and appropriateness of executive talent. These areas are:

— Balance between base salary and variable pay

  There is limited use of performance related variable pay (paid as non-consolidated, one-off payments) across the public sector. The Civil Service uses variable pay more widely than other parts of the public sector with a budget (or "pot") of 8.5% of base salaries. Although it would not be appropriate to adopt generally the level of variable pay in the private sector for senior executives, there is scope to increase variable pay budgets to 15 or 20% of base salaries: this would give greater emphasis to performance without losing the public service ethos,

— Balance between pay (base and variable pay) and benefits

  Some benefits are competitive with private sector practice, for example, leave arrangements and pension provision, while other elements are below market practice, for example, private health insurance, share plans, car policy.

  Consideration should be given to moving away from defined benefit pension provision (especially linked to final salary) towards some form of base line pension provision alongside more flexible savings programmes in which the executive can choose to take part depending on their judgment of the level of financial planning they need to make. Some parts of the public sector are beginning to provide a range of benefits within which the individual can make choices that better meet their specific needs; this flexibility could make the reward package more attractive to the individual at no extra cost to the employer.

— Balance between tangible reward (pay and benefits) and intangible reward (career and work life)—a total reward approach

  There are good examples of how the public sector makes use of intangible rewards that are attractive to individuals and normally inexpensive to the employer to offer. More can be done actively to manage or optimise the balance between these elements and communicate their value to potential recruits and employees alike.

Do the pay levels for top posts in the public sector have a direct impact on the performance or qualities of the people filling those posts?

17. Pay level is a reward to the individual for undertaking a role; it does not differentiate between different levels of delivered performance and has little direct impact on the individual's performance.

18. Pay level can impact recruitment and retention of talent; the further below the market, the more difficult it is to recruit (and to a lesser extent retain) good talent. There is little hard evidence that the public sector can or can not recruit and retain the talent it needs. The evidence that does exist suggests the public sector has some talent challenges, for example:

— leadership and people management—see civil service capability review findings; and

— small fields of suitable candidates for externally advertised senior vacancies feedback from recruitment agencies.

(a) *What impact does the performance or qualities of the people filling top posts in the public sector have on the performance of the organisations for which they work?*

19. Weak leadership, professional expertise and delivery experience adversely impact the effectiveness of senior management and thereby the performance of organisations they lead. At a time when public expenditure, service delivery expectations and value for money are all under growing pressure, the need for effective talent is greater than ever.

Is there an appropriate benchmark or ceiling for top public sector salaries-eg the salary of the Prime Minister, or a factor of average pay?

20. Adopting the Prime Minister's salary would provide an artificial, absolute limit on salaries that does not reflect labour market circumstances, and therefore could impact the public sector's ability to recruit and retain good talent.

21. An alternative approach suggested in the Government's evidence in 2005 for the Senior Civil Service, to the Senior Salaries Review Body (SSRB) was to link pay levels to a specific percentage of the market median.

Can England and the United Kingdom learn from the experience of other countries or the devolved governments in this area?

22. Practice in other administrations could provide valuable insights about reward policy and governance. However, public and political confidence, as well as that of public sector employees, depends on full debate about the optimal approach to executive reward in the public sector. The inquiry by the Committee is therefore to be welcomed.

Some Observations About the Way Forward

23. Acquisition, development, management and retention of talent, at any level, but especially for executives, takes time and needs a sustainable reward strategy and governance arrangements. The features of these arrangements should include the following.

Reward governance

(a) The public sector is not one sector. Different parts of the public sector compete for executive talent in different markets. For example, government owned companies typically compete with the private sector for business leaders with proven track record; the civil service has grown about $\frac{2}{3}$rds of its executive talent from within and recruited $\frac{1}{3}$rd externally from the public and private sectors.

(b) Public sector reward should be guided by a common set of principles within which different parts of the public sector develop and manage reward specific arrangements.

(c) An independent review body should advise on the reward principles and provide guidance to national and local government, as appropriate, for the different parts of the public sector.

(d) Executive reward decisions—policy and application to individuals—should be made through remuneration committees that include independent members and report to Ministers or authority members or boards, as appropriate, to each organisation.

(e) Executive reward should be published in annual reports by analogy with requirements for public companies.

Reward policy

(f) Executive reward levels (and for all employees too) should be set sufficiently competitive to attract and retain good talent while taking into account the attractiveness of the intrinsic features of making a contribution in the public sector, and the valuable experience that can be gained in the public sector.

(g) All elements of reward should be managed as a whole—a total reward approach and delivered in ways that maximise individual choice to tailor the elements of the reward deal that work best for them.

(h) Executive reward should be linked to performance of the individual and the organisation in the short and longer terms, and should be rewarded through variable pay in which there is both risk and opportunity.

(i) Executive pension provision should be reformed to reflect emerging market practice and affordability through defined contribution arrangements at least for new entrants and possibly for future service.

(j) Executive benefit provision should be extended in scope to include benefits more typically found outside the public sector and employee savings vehicles to facilitate financial planning alongside the new pension arrangements.

(k) Executive reward should be affordable in public expenditure terms and should take account of public sector pay policy.

May 2009

Memorandum from Local Government Association and Local Government Employers

Introduction

The Local Government Association (LGA) represents over 400 local authorities across England and Wales, including all twelve councils which currently have directly-elected mayors. In its role the LGA aims to put councils at the heart of the drive to improve public services and to work with government to ensure that the policy, legislative and financial context in which they operate, supports that objective.

Summary

1. We would like to thank the Committee for this opportunity to present some considered thoughts on the subject of executive pay in the public sector. Like all bodies with some responsibility for executive remuneration, we recognise that there is real political and public concern about both the level of top remuneration and growth in packages and also about how well the mechanisms for setting top pay are operating. For us, this concern predates the current economic downturn but has undoubtedly been exacerbated by it.

2. Our evidence is written from the perspective of our role in agreeing annual basic pay increases and some core terms and conditions for Chief Executives and Chief Officers but we hope that our observations will help in developing a more general picture.

3. Our key observations are as follows:

— Local Government operates a system in which the main decisions on executive remuneration are taken by individual councils as employers. This is very important in ensuring that local politicians can be held to account for the decisions they make. It also enables councils to operate flexibly in the markets they need to recruit in.

— This approach has served the local government sector very well in recruiting leadership teams capable of running very complex organisations. No other parts of the public sector and few if any parts of the private sector operate such a wide range of critical services with such large budgets as local authorities. No hospital chief executive, for example has to manage education, public safety, housing and highways services on top of social care. Added to this is the unique political environment of being responsible to local elected members as well as having to interact with the national government.

— The salaries and rewards agreed by local determination sometimes reflect a better economic climate and local priorities in recruitment that may no longer be sustainable in the current economic downturn. Councils need talented people in top management positions; however they must take steps to be more accountable in setting top pay and rewards and balance this with the need, in a tight financial situation, for all salaries to be demonstrably reasonable.

— We have long recognised that the perception of the system and its apparent fairness is very important and that councils must take decisions about pay for senior executives in an accountable way. The LGA Group has recommended that councils should establish independent remuneration committees and this advice is now set out in the national terms and conditions for chief executives.

— We will shortly be issuing guidance to the sector advising councils to review their own remuneration strategies and setting out some recommendations for strengthening the use of remuneration committees and on how councils can manage growth in top pay more rigorously.

— We believe that councils must be completely open and transparent about the full range of pay and benefits in top reward packages. We therefore support the Government's decision to require public disclosure of remuneration information in local government in a way that is equivalent to the current requirements in the Civil Service. We look forward to the forthcoming consultation on detailed proposals.

— We are sure that it is appropriate for different parts of the public sector to develop remuneration strategies that suit their very different responsibilities and methods of operation, though of course there are some important common principles about accountability.

— We do think it is important to encourage the shared development of leaders across the public sector to promote a partnership approach, so common training and enhanced chances to work across sectors will be important developments.

The Role and Impact of Chief Executives in Local Government

4. Local authority Chief Executives have always had complex roles and the level of complexity is increasing. They have overall responsibility for budgets of £370 million on average and well over £1 billion in a number of cases. They are responsible for nearly 5,500 staff on average—over 48,000 in the biggest council. They oversee dozens of statutory services including the whole vital range of services for children, public protection, highways and so on. It is estimated that upper tier local authorities have over 700 different occupations. In recent years, Chief Executives have had to lead the development of new responsibilities working in partnership with the Health Service, Police and others on community issues. Councils also have wide and growing responsibilities for economic and community development, which is central to national recovery. One example of new responsibilities that will be devolved next year is responsibility for brokering training and skills development for all 14–19 year olds. All this has to happen in the context of democratic politics.

5. The impact that a strong Chief Executive and management team can have in practice is considerable. A council that is well managed both politically and managerially can have a strong impact on local communities. The whole team is responsible for running some very large business units.

6. An exhaustive listing of responsibilities is not possible here but the point is well made that the top leadership team overseeing this range of core responsibilities requires exceptional capabilities. The reward package has to reflect this need as well as the need to provide demonstrable value in the use of taxpayers' money. All these observations apply proportionately to Chief Officers, such as Directors of Children's Services, as well.

Reward Structure for Top Executives in Local Government

7. The main responsibility for setting pay and rewards for Chief Executives—and indeed all staff—in local government lies with individual councils as employers. There is a voluntary arrangement whereby all but around 10% of councils take part in national negotiations through Joint Councils involving the recognised Trade Unions. The JNC is a collective bargaining mechanism that agrees a national annual basic pay increase and some other core terms and conditions—particularly the disciplinary process for Chief Executives.

8. The individual salary level to which any national increase is applied is set entirely at local level, based on an assessment of the size of the job and relevant market comparators. The way in which pay is adjusted each year is also a matter for local discretion. In practise, around 64% of Chief Executives are paid on an incremental pay range and 36% have a "spot salary", which is reassessed periodically.

9. On top of this, some councils offer various additional payments and, to a lesser extent, performance related pay. Additional payments include things like regional allowances, long-service supplements, fees for administering regional bodies etc. Around 49% of Chief Executives receive additional payments and 6% are known to receive some performance related pay.

10. All the various elements of remuneration packages produced an average actual payment of £128,922 (not including pension entitlements) to Chief Executives according to the latest LGE survey in 2008. The survey found that the overall average (mean) annual basic salary for chief executives excluding additions was £124,784. The corresponding figure was £90,965 for 1st tier officers, £69,528 for 2nd tier officers, £58,575 for 3rd tier officers and £53,877 for other executive officers.

11. The evidence from last year's report on chief executive pay by the Audit Commission, "Tougher at the top?" was that basic salary levels for single tier and county council chief executives increased by 34% between 2003–04 and 2007–08, whereas the total pay of private sector chief executives increased by 78% from 2002–03 to 2006–07. Part of the increase in the pay of council chief executives was related to growing turnover, which increased from 11% in 1998 to 17% in 2007 for single tier and county councils. The Audit Commission's research observed an emerging consensus that effective political and managerial leadership are fundamental in creating high performing local authorities, and a perception that the appointment of an existing chief executive with a good track record is the best way to improve performance.

12. The range of individual salaries is quite wide though salaries at the upper end are the exception to the rule. In our most recent survey the distribution was as follows:

Salary Range	*No in receipt*	*%*
£200,000–£225,000	7	2
£180,000–£199,999	24	6
£160,000–£179,999	46	11
£140,000–£159,999	52	13
£120,000–£139,999	46	11
£100,000–£119,000	123	31
£80,000–£99,999	91	23
Less than £79,999	14	3

13. The salary range is not out of line with the rest of the public sector, however, in common with the public sector as a whole, we need to ensure that further growth in reward packages is carefully managed in order to ensure that executive reward reflects current economic circumstances.

The Balance of Reward Packages

14. Additional financial benefits and bonuses are not as significant a component of pay as they are in the private sector. However, work is being done to establish a full picture of additional payments, so that recommendations can be developed about how best to control them.

15. The pension scheme is an important additional part of the overall reward package. It is a funded scheme with contributions from individual employees, as well as from employers. Employer contributions can add around 20% on average to individual reward packages. The pension scheme has recently been reformed to introduce banded payments so that higher earners pay more, with rule changes to make the scheme more affordable. This will need to be kept under review, to ensure that the scheme continues to take account of longer-term economic and demographic factors.

Ensuring Public Accountability

16. We believe that local government needs to balance the benefits of local decision-making with complete clarity and openness about the reward packages given to top executives.

17. Councils take their fiduciary duty in accounting for top executive remuneration very seriously. There is already a high level of public disclosure of salary levels and we support government moves to extend these. Councils also produce extensive audit material according to the requirements of the Audit Commission and CIPFA. The sector is also unique in its signed commitment to completing equal pay audits across the workforce.

18. LGE and LGA do believe, however, that local government must take careful note of concern about top salary levels. We intend to recommend that councils should review their local remuneration strategies, improve accountability through appointment of remuneration committees with members from outside the council and examine ways to demonstrate that annual growth in pay is reasonable and justified.

19. The LGA Group has advised councils to set up independent remuneration committees to oversee the process of setting top pay and reward packages. Advice on setting up committees—preferably with representatives from outside the council—is contained in the national terms and conditions for chief executives. Such committees can provide powerful oversight of the mechanisms for setting pay and the advice and information taken into account. We have now expanded our advice to recommend that councils should take steps to ensure that top pay growth does not move out of line with general pay growth in the economy, unless changes can be fully justified by exceptional performance.

Benchmarking Across Sectors

20. The question of providing an appropriate benchmark for salaries across the public sector has been raised. We think it is important to understand what this would entail. We have already outlined the particular specialist roles of top executives in local government. We feel sure that other sectors should highlight their own specialist roles as well. If any attempt is to be made to develop good comparable benchmark salaries for the public sector, the exercise will need to involve the entire public sector and take account of detailed differences in job roles beyond simple job titles, in order to create an accurate analysis.

21. We believe that it is increasingly important to develop a cadre of multiskilled leaders who can work increasingly across and between different parts of the public sector delivering services in partnership. We believe that it is important to enhance the scope for common development and learning as well as for sharing experience via secondment from government departments to local authorities.

22. It is also very important for councils working alone and in partnerships to do more to develop their most talented employees to take up leadership positions in the future. This will increase the supply of potential leaders.

International Comparisons

23. We have not made a close study of systems in other countries but we do believe that it is valuable to note that in Scotland, where a more highly centralized form of pay setting for Chief Executives has been retained, there is some intense discussions about growing problems. In particular there is some disagreement about finding appropriate benchmark comparators for Chief Executives because the old comparators of civil servants and head-teachers are regarded as inadequate.

24. Also, we are aware that some years ago the Republic of Ireland attempted to conduct a wide-scale salary benchmarking exercise across the whole public sector, which resulted in significant anomalies and disagreements.

25. Our conclusion is that the best approach is for individual sectors to have flexibility to operate within their own requirements and relevant markets, although this flexibility must be used responsibly and accountably.

April 2009

Memorandum from Managers in Partnership (MiP)

Managers in Partnership (MiP) welcomes the opportunity to give the Committee a short submission about executive pay in the NHS.

MiP is the trade union organisation for over 5,300 senior healthcare managers, including more than 300 NHS chief executives. MiP gives evidence to the Senior Salaries Review Body (SSRB) for its board-level members in primary care trusts, strategic health authorities, special health authorities and ambulance trusts. Our most recent evidence to the SSRB is attached to this submission.[17]

1. *Are the right arrangements in place for setting and monitoring pay and other benefits for top posts in the public sector?*

(a) *Are they fair?*

(b) *Are they transparent?*

(c) *Do they produce the right results?*

(d) *Do they provide value for money?*

(e) *Do they inspire public and political confidence?*

Our members in receipt of Very Senior Managers Pay in the NHS have made it clear that they do not think the current arrangements for pay are the right ones. They are not fair or transparent and there are many examples of their failure to produce the right results, either for the responsibilities of the post or in relation to other posts within the NHS and in other public and private bodies. Moreover, it is our view that the current arrangements leave organisations vulnerable to challenge under equal pay legislation. We would therefore argue that they do not provide value for money and cannot inspire confidence. Our evidence to the SSRB provides a more detailed critique.

2. *Does there need to be consistency regarding these arrangements between different parts of the public sector?*

We are not against the principle of consistency between different parts of the public sector, but some key questions include whether the market factors for pay levels for senior managers are broadly the same in all public services and therefore whether a common approach is possible.

We would certainly like to see greater consistency within the NHS. We argue that consistency can only be realistically achieved by giving all NHS remuneration committees the same powers to appoint and remunerate directors as applies to foundation trusts.

3. *Does there need to be comparability of pay between top posts in the public sector and equivalent posts in the private sector? If so, how should equivalent posts in the private sector be identified?*

Yes. There are job markets that cross the sectors. The finance duty in the NHS is a good example. Salaries below board-level compare well with the private sector, but directors of finance in the NHS are paid much less than their counterparts on private sector boards.

Most NHS boards mirror the corporate governance of most private sector boards. On the face of it comparators are available. However, the question will be how we can ensure that we are comparing the boardroom posts of comparable organisations. There is, of course, also a private healthcare sector in the UK from which to draw potential comparators.

4. *Is there evidence of executive wage inflation caused by public sector organisations competing with one another for candidates?*

The latest IDS report on NHS boardroom pay suggested that salary rises are driven by starting pay rather than pay rises to existing postholders. We have no evidence about the factors considered by remuneration committees, but anecdotal evidence suggests that NHS foundation trusts and local authorities use their greater pay freedoms to outbid the rest of the NHS for the best managers.

The Committee might like to note that MiP's advice to our members is, where possible, to maximise starting salary in pre-appointment negotiations, in order to counter (1) the absence of pay progression after appointment and (2) the likelihood of relatively short tenure in post.

[17] Not printed.

5. *What role should consultancies play in the determination of pay for top public sector posts?*

Consultancies have a role to play in ensuring boards make informed decisions about market rates and job evaluation. The commercial terms on which such consultancies are engaged should be open to scrutiny.

6. *Is the balance right between executive pay and other benefits? eg bonus, pension*

The bonus arrangements for NHS managers covered by the SSRB are modest. The current arrangements for those on VSM are criticised in our evidence to the SSRB.

The pension scheme, especially for those managers with long service, is a valuable benefit.

The balance with risk, however, is completely wrong. Tenure is seen as short, with senior executives held to account by a system that is often arbitrary, subjective and amateurish. Good HR practice, which is a benefit of any employment, is normally non existent. Many organisations have struggled to appoint key people, in circumstances where pay is not the only factor. In our evidence to the SSRB this year we intend to explore the views of many assistant directors that directorships are not worth the candle. They don't see the relatively small increase in pay compensates for the career risks and exposure of working at board-level.

7. *Do the pay levels for top posts in the public sector have a direct impact on the performance or qualities of the people filling those posts? What impact does the performance or qualities of the people filling top posts in the public sector have on the performance of the organisations for which they work?*

We don't believe that, in the short to medium term, pay levels have a direct impact on the performance of people filling top posts. Vocational rewards drive many managers. For example, our members in primary care trusts are highly motivated by the commissioning agenda, despite feeling hard done by compared to their colleagues in trusts and foundation trusts. For the reasons given in the answer to question 6, we believe pay does prevent the best managers seeking directorships.

When things go wrong in the NHS, politicians and regulators blame managers. This is the negative side of the coin. The other side is that managers are very important for the performance of NHS organisations.

8. *Is there an appropriate benchmark or ceiling for top public sector salaries—eg the salary of the Prime Minister or a factor of average pay?*

No. Pay in the NHS tends to be viewed hierarchically, ie the highest salaries should be in the Department of Health, then the strategic health authorities, and then trusts. Why should this automatically be the case? If the politically acceptable salary at the top of the tree is set too low, then salaries lower down are artificially depressed. This is the experience of our members in Scotland. Salaries ought to be compared using commonly recognised principles of executive remuneration and job evaluation. These would provide a degree of benchmarking.

The elephant in the room is, of course, the pay of top doctors.

9. *Can England and the United Kingdom learn from the experience of other countries or the devolved governments in this area?*

It may be useful to review the arrangements for remuneration in other countries, ensuring the review covers a cross-section of models of healthcare provision. Please note our comment in the answer to question 8 above about the problems with the arrangements in Scotland.

In conclusion, MiP welcomes this inquiry into executive pay in the public sector, and we would be happy to elaborate on any of the answers provided.

June 2009

Memorandum from Dr Anne Wright CBE, National Lottery Commission

INQUIRY INTO EXECUTIVE PAY IN THE PUBLIC SECTOR—18 JUNE 2009

As requested by the Committee, please find attached the details of our Chief Executive's maximum bonus levels and actual award made each year since the National Lottery Commission was set up in 1999.

The Chief Executive's current contract, which dates from 2005, is open-ended. It provides for an annual review by the Remuneration Committee, on the basis of appraisal of performance against targets for the year. The Remuneration Committee has discretion to determine a bonus payment of up to 20%, of which up to 5% can be consolidated in salary. There is no other provision for salary increase ie the Chief Executive does not receive the NLC staff pay award.

In determining the bonus payment, the Remuneration Committee has regard to the wider economic context, and available guidance including the HM Treasury affordability guidance, and pay advice from the sponsor department, within the overall framework of the Chief Executive's contract.

You will note that this year the Chief Executive has decided to forgo a part of the bonus payment awarded by the Remuneration Committee, and also requested that the consolidated bonus be limited to the amount of the NLC staff pay award of 1.5%.

CHIEF EXECUTIVE REMUNERATION DETAILS

Year	*Salary*	*Non-Consolidated Bonus*	*Non-Consolidated Bonus*	*Conslidated Bonus* (1)	*Conslidated Bonus*	*Total Bonus*	*Total Bonus*	*Note*
	£	£	%	£	%	£	%	
1999–2000	75,000.00	7,325.00	9.77	2,175.00	2.90	9,500.00	12.67	
2000–01	77,175.00	3,472.88	4.50	2,315.25	3.00	5,788.13	7.50	
2001–02	79,490.00	8,012.00	10.08	1,988.00	2.50	10,000.00	12.58	
2002–03	81,477.00	10,250.00	12.58	0.00	0.00	10,250.00	12.58	(2)
2003–04	83,514.00	11,750.00	14.07	0.00	0.00	11,750.00	14.07	(2)
2004–05	85,180.00	12,300.00	14.44	0.00	0.00	12,300.00	14.44	(3)
2005–06	97,000.00	11,640.00	12.00	4,850.00	5.00	16,490.00	17.00	
2006–07	101,850.00	14,407.00	14.15	5,093.00	5.00	19,500.00	19.15	
2007–08	106,943.00	16,041.00	15.00	5,347.00	5.00	21,388.00	20.00	
2008–09	112,290.00	5,614.50	5.00	1,684.35	1.50	7,298.85	6.50	(4)
2009–10	113,974.00							

Notes

(1) Consolidated bonus represents the element of bonus which is consolidated as a cost of living increase.

(2) Uplift does not form part of total bonus amount as these were one year contracts of employment.

(3) Uplift does not form part of total bonus amount as this was first year of a new contract of employment.

(4) The Chief Executive's bonus can be up to 20% of his annual salary, subject to performance. The bonus is non-pensionable and non-conslidated, although up to 5% may be consolidated (as a pay increase). The bonus, and any consolidated increase is set by the Commission's Remuneration Committee, who review the Chief Executive's performance against the objectives set at the start of the year. The Remuneration Committee and Commission have considered the Chief Executive's performance for the 2008–09 year which included the successful delivery of a transition to the third licence. Having regard also to the economic climate and to available guidance, including current HM Treasury affordability guidance, the Remuneration Committee and Commission determined a total bonus payment of 9%. The Chief Executive has waived part of his bonus and accepted only a non-consolidated payment of 5% and a pay increase of 1.5%.

Memorandum from NHS Employers

Summary

- The NHS employs in the region of 3000 posts at Chief Executive and Executive Director level across 400 organisations in England.
- There are two approaches to remuneration of senior appointees, according to organisational type.
- Around two thirds are enabled by statute to set executive pay locally by remuneration committee.
- The remaining third is required to operate the "pay framework for Very Senior Mangers" specified by the Department of Health—this framework is currently under revision.

Background

1. There are in the region of 1.3 million staff employed by the NHS in England in 400 organisations. Of these around 3,000 are Chief Executives or Executive Directors. The arrangements for executive pay vary according to the type of organisation and are explained below. However, other aspects of the reward package are common across the NHS.

2. NHS staff below director level are either employed on specific national agreements for doctors and dentists, or (over 1.2 million) on a national pay system based on a job evaluation framework, entitled "Agenda for Change", which was introduced in 2004. The Agenda for Change arrangements include a NHS Staff Handbook[18] which details terms and conditions of service such as leave and redundancy arrangements. These terms (but not the accompanying pay system) are generally extended to all in the executive group and should be referenced in individual contracts.

3. There are pension schemes, Ill Health Retirement and Injury Benefit Scheme for the NHS in England and Wales and these also apply to the executive group. Since 1 April 2008, employees with higher earnings have paid an increased pension contribution (7.5% of pensionable pay between £63,417 and £99,999, rising to 8.5% of pensionable pay of £100,000 or above.

Executive Pay in NHS Trusts and Foundation Trusts

4. Since 1991, when NHS trusts came into being, they have been able to use local pay setting machinery in the form of a remuneration committee. This will be chaired by a non-executive director and report to the Trust Board. The introduction of Foundation Trusts in 2004 provided a different legal basis for NHS organisations and further cemented their right to set remuneration independently. There is no mechanism for central intervention in determining executive roles or payment.

5. This system appears to work well with little complaint by organisations which operate it. They have the flexibility to design director roles to suit the organisation and to set pay appropriately. It is good practice for Remuneration Committees to benchmark their pay against market and industry levels using independent advice. As with most senior roles there is little evidence of pay scales in use at this level with a spot rate being determined on appointment. Some drift has been noted by independent reviewers Capita and Incomes Data Services who have undertaken longitudinal surveys of NHS boardroom pay. This is understood to be caused by increased pay offered on appointment rather than annual rises above the median in any one year.

6. Transparency is obtained by the requirement of NHS organisations to publish the detail of board remuneration in the trust accounts. Variable pay forms a very small part of the package overall, and is not used by the majority of organisations. There is no common form of contract documentation.

7. The Department of Health pay circular advising on annual pay uplift described below for very senior managers indicates that the uplift applies to NHS trusts also (even though they are not part of the national pay framework). This is the only extent to which the two systems can be said to interact. However, the circular has no direct effect for Foundation Trusts.

Pay Framework for Very Senior Managers

8. The Department of Health has determined that pay for executives in Primary Care Trusts (151), Ambulance Trusts (11), Strategic Health Authorities (10) and Special Health Authorities (10). The framework was introduced in 2006 and since 2008 has been under the auspices of the Senior Salaries Review Body (SSRB). Salaries for Chief Executives are set in bands according to organisational type and those for supporting directors are set as a percentage of the Chief Executive salary. There are allowances for certain additional responsibilities. There is also a model form of contract to accompany the framework.

9. In 2009, the Department of Health rejected a recommendation of a 2.4% uplift by the SSRB. The Department's circular[19] advised instead that in light of the economic climate and the need to show leadership and pay restraint, the uplift would be 1.5% for 2009/10 and the bonus pot would remain at 5% of the VSM pay bill.

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[18] See: http://www.nhsemployers.org/SiteCollectionDocuments/afc_service_handbook_aw_010708.pdf
[19] http://www.dh.gov.uk/en/Publicationsandstatistics/Lettersandcirculars/Dearcolleagueletters/DH_097394

10. The VSM Pay Framework was independently reviewed in 2008. The "Wright review" and the Department of Health response to it formed the Department of Health's evidence to the SSRB in 2008.[20]

11. Employers subject to the VSM pay framework have long argued for change and have, on two occasions, submitted evidence to the SSRB seeking more flexibility and local control. The ability to design board level roles, attract the best candidates, enable movement between sectors and give local remuneration committees freedom to act rather than to rubber stamp the use of a framework, has been the main thrust of the submissions.[21] As a programme of work is underway at the Department of Health to revise the framework the arguments are not pursued further here. However, your Inquiry sought an opinion on the interaction of the systems and a view on whether there should be centrally controlled or devolved arrangements across the public sector.

12. From our engagement with employers, the general view is that it would be preferable if NHS organisations were all able to manage their own senior pay arrangements. The VSM framework does not have the confidence of the organisations which are obliged to implement it. It is not "felt fair".

13. Fully devolved arrangements would facilitate recruitment of the best candidate for a role in any organisation and encourage movement between organisational types. It would remove barriers to recruitment in "hard to fill posts" and enable organisations to incentivise challenging assignments. Currently, there is a strong disincentive for a successful manager of an NHS Trust or Foundation trust to move to a post in an organisation operating the Very Senior Mangers pay framework. This is potentially restricting the candidate pools for the "world class commissioning" of patient care.

14. There is no indication that executive pay in the NHS is out of line with reward in other sectors where the management challenge is of a similar order of complexity, or that NHS pay requires any form of cap. The averages are well below the benchmark of the Prime Minister's pay referred to in your reference document. Examples for Chief Executives and Directors of Finance from the most recently available aggregated statistics are included in the table below.

15. Each organisation is required to publish details of the remuneration package of its senior officers in its annual report.

16. Finally, we are an organisation representing England only so have not commented on practice in Devolved Administrations or international public sector comparisons.

INCOMES DATA SERVICES NHS BOARDROOM PAY REPORT 2009 EDITION

Chief Executive average basic salaries (£)

PCTs	133,294
Provider trusts	141,408
FTs	157,878

Director of Finance average basic salaries (£)

PCTs	100,911
Provider Trusts	105,997
FTs	118,512

June 2009

Memorandum from Ofcom

During Millie Banerjee's oral evidence session with the Committee, Charles Walker requested a note on the maximum bonus that can be earned and how much of that bonus is paid out.

> **Q216 Mr Walker:** *I think what would be very helpful is if you could provide the Committee with a note showing for each year what the maximum bonus that could be earned was and how much of that bonus was paid, because then we can ascertain whether it really is a bonus or just part of the salary.*

Ofcom's Bonus Policy

Ofcom offers a limited annual bonus payment, awarded for good performance. Performance is measured against objectives set in line with the annual plan and agreed at the start of the financial year. Colleagues who are rated as unsatisfactory are not eligible for consideration. Each individual's performance is reviewed before determining the actual bonus amount. In the case of the Chief Executive and current Executive Committee the selected amount cannot exceed the contractual maximum of 20% of base salary and these bonus proposals must be agreed by the Ofcom Remuneration Committee.

20 http://www.dh.gov.uk/en/Publicationsandstatistics/Publications/PublicationsPolicyAndGuidance/DH_090068
21 http://www.nhsemployers.org/PayAndContracts/AnnualPayReview/SSRB/Pages/SeniorSalariesReviewBodyEvidence.aspx

Ofcom Bonuses 2008–09

In light of the current economic circumstances, Ofcom froze pay for this financial year, and halved the amount to be allocated for bonuses. Members of Ofcom's Executive Committee were not considered for a bonus. Any bonuses awarded were weighted to more junior pay grades.

Chief Executive and Executive Committee Bonuses

Mr Walker expressed particular interest in the Chief Executive's salary and bonus.

Ofcom was established in 2003 and during this first year, the Chief Executive's maximum bonus potential was 12%. In 2004, this maximum bonus potential was increased to 20%. The bonuses awarded to both Ofcom Chief Executives reflected the high quality of leadership they have provided for the organisation. A bonus is not a guaranteed part of his salary and the Chief Executive has not always received the full amount.

The variable award of bonuses applies throughout the organisation and is reflected in the bonuses awarded to members of the Executive Committee (ExCo). ExCo is the senior executive team responsible for overseeing the management of Ofcom. Its core focus is on setting direction for the organisation, financial and administrative decision-taking and monitoring. Its policy-making responsibilities are limited to management policy only.

The colleagues listed in Table 1 have all sat on ExCo. When Ed Richards became Chief Executive ExCo was restructured and is currently made up of Ed Richards (CEO), Jill Ainscough (COO), Peter Phillips (Partner), Stewart Purvis (Partner) and Stuart McIntosh (Partner). In addition, Christopher Woolard was appointed to ExCo as Partner in July 2009 and there is vacant position for which Ofcom is recruiting.

BONUS AWARDS FOR CHIEF EXECUTIVE AND MEMBERS OF THE OFCOM EXECUTIVE COMMITTEE—2003–09[1]

Blank boxes indicate a year during which the individual was not Chief Executive or serving on ExCo

		Bonus CAP	*2003–04*[2]	*2004–05*	*2005–06*	*2006–07*[3]	*2007–08*[4]	*2008–09*
Robin Foster	Partner, Strategy Team	20%	6%	19%	0%			
Peter Phillips	Partner, Strategy and Market Developments	20%			0%	16%	20%	0%
Graham Howell	Secretary to the Corporation	20%	0%	8%	10%	10%	7%	
Peter Ingram	Chief Technology Officer	25%[6]	0%	24%	19%	23%	5%	
Sandra Jenner	Director, Human Resources	20%	11%	20%	18%			
Janet Campbell	Director, Human Resources	20%				10%	14%	
Tony Stoller	External Relations Director	20%	10%	10%	10%			
Dominic Morris	Director of the CEO's Office	20%			18%	8%	7%	
Kate Stross	Commercial Director	20%	7%					
Rona Chester	Finance Director	25%[6]		7%	20%	23%	0%	
Philip Rutnam	Partner, Competition and Strategic Resources	20%		14%	20%	20%		0%
Sean Williams	Partner, Competition and Investigations	20%		20%				
Jill Ainscough	Chief Operating Officer	20%					20%	0%
Stuart McIntosh	Partner, Competition	20%					0%	0%
Ian Hargreaves	Partner, International, Nations and Regions	20%						0%
Stewart Purvis	Partner, Content and Standards	20%						0%
Ed Richards	Chief Executive	20%				16%[5]	20%	0%
Stephen Carter	Chief Executive	20%	11%	20%	20%	0%		

Notes to Table

1 The colleagues listed below have all sat on the ExCo and their salary and bonus were published in the annual report. The annual reports give the pro-rated salary for the time on ExCo but the bonus for the full year, including any time when they were not a member. In order to accurately reflect the relationship between their published salary for their work as a member of ExCo and the bonus they received, the percentages here have been calculated by annualising the salary figures published.

The records of some former Ofcom employees are stored off site. The figures in this table have been calculated using information readily available and should be taken as a strong indication of the bonus award.

2 Prior to Ofcom's vesting at the end of 2003, a number of colleagues were working for Ofcom and one of our legacy regulators. The figures given are based upon the salary and bonus awarded for their time working for Ofcom.

3 In the 2006–07 financial year, the performance assessment period was changed from calendar to fiscal year. In the annual report the salary figures were for a 12 month period and the bonus for a 15 month period. The bonus has been pro-rated to match the salary period.

4 In 2007–08 ExCo was restructured.

5 Ed Richards was appointed Chief Executive in 2006. This bonus figure reflects his time as Chief Executive in that year.

6 The individual packages negotiated with Peter Ingram and Rona Chester when they joined Ofcom included a 25% maximum bonus. Rona Chester has now left Ofcom, Peter Ingram is no longer a member of ExCo and bonuses have been standardised.

July 2009

Memorandum from the Public and Commercial Services Union (PCS)

Introduction

PCS welcomes the opportunity to make a written submission to the Public Administration Select Committee. PCS—a union representing over 300,000 members, the majority of whom work in government departments, agencies and public bodies—also welcomes the invitation to give oral evidence as the inquiry topics are issues that are of concern to our union.

Executive Pay in the Public Sector

It seems right that pay and benefit for top posts across all parts of the Public Sector should be determined in a reasonably consistent way, whilst making due allowance for specialised/technical nature of some posts. Also we would support a proper and comprehensive basis of comparability, being developed to enable these posts and equivalent post in the private sector to be analysed. It must, of course, be recognised that the basis of determining salaries and packages for private sector positions, usually decided by management boards or remuneration committees, does not always lend itself to a feasible comparison in all respects.

This aspect would need to be considered in much further detail. For PCS, there should also be a similar read across in terms of comparability for civil service posts below the Senior Civil service, as these are very often the "feeder grades/career paths" for the more senior posts.

PCS recognises that the question of performance pay and bonuses is currently controversial arising from the concerns expressed about bonuses payments in banking and other commercial entities. However, there is a serious question beyond the understandable skepticism and criticism about bonuses in parts of private industry, about whether performance pay constitutes value for money. Frankly, there is little evidence that performance pay systems contribute to, or assist organisations in reaching targets or objectives. Also, there is a lack of any mechanisms for achieving assurance where output or performance improves or deteriorates, that this is related (even partly) to the existence of performance pay arrangements.

Thus, the justification for use of performance pay and bonuses can be extremely thin, whilst there is evidence in OECD reports and elsewhere of bonuses having a de-motivating effect on staff and managers. PCS has long held the view that performance pay is generally a bad way of spending money, as there is continuing evidence of potential discrimination in pay systems particularly on the basis of race/ethnicity, disability and working patterns (to the disadvantage of many women).

PCS has not gathered evidence of such a trend or effect at the level of Senior Civil Service posts, but there are many experiences among the separate bargaining units across civil service organisations (over 200 of these) of a very real internal job market, applying particularly at recruitment levels. This is based on wide pay differences of 25% or more (for the same grade/job weight) in different civil service organisations. There has been considerable movement of individuals between lower paying and higher paying organisations and this has involved considerable cost for Government Departments. It is a recognised feature especially in London and other major cities.

Individuals can literally shop around for better salaries in the same high street. PCS believes that this is a very wasteful situation, and that much more coherence and commonality of pay systems and pay rates is needed.

March 2009

Memorandum from the Senior Salaries Review Board (SSRB)

Introduction

1. The Review Body on Senior Salaries (SSRB) is an independent body established in 1971 (as the Top Salaries Review Body) to advise the Government on the pay of various groups ("remit groups") of senior public sector workers. Currently the SSRB reports annually to the Prime Minister and the relevant Secretaries of State on the pay of:

- salaried holders of judicial office throughout the United Kingdom;
- senior military officers[22] throughout the United Kingdom;
- senior civil servants in England, Scotland and Wales; and
- senior managers (other than those on medical contracts) in English Primary Care Trusts, Ambulance Trusts, Strategic Health Authorities and Special Health Authorities.

In addition the SSRB reports when requested on the pay, pensions and allowances of Members of both Houses of Parliament, Members of the Devolved Parliament and Assemblies and of the Mayor of London and Members of the London Assembly. The SSRB has also carried out ad hoc reviews, for example of the remuneration of tribunals' judiciary and senior NHS managers in Northern Ireland. The SSRB's full terms of reference are at Appendix A.

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22 Senior military officers are those of the ranks of Rear Admiral, Major-General and Air Vice-Marshal and above.

2. The SSRB's reports are normally published as command documents and since 2001 have been made available on the website of the Office of Manpower Economics (OME), together with reports of research commissioned by the SSRB.

3. The SSRB has 10 members, appointed following advertisement and a selection procedure supervised by the Office of the Commissioner for Public Appointments. The current membership is listed at Appendix B. Members have a wide range of skills and backgrounds, including business and HR, and two are specialist labour market economists. The secretariat is provided by the Office of Manpower Economics which is staffed by civil servants.

Responses to Questions posed by the PASC

1. *Are the right arrangements in place for setting and monitoring pay and other benefits for top posts in the public sector?*

(a) *Are they fair?*

(b) *Are they transparent?*

(c) *Do they produce the right results?*

(d) *Do they provide value for money?*

(e) *Do they inspire public and political confidence?*

4. Pay review bodies exist to provide independent advice on the pay of groups of public sector workers for whom the state is the sole or major employer (eg the armed forces, judiciary, school teachers, doctors and dentists, prison officers) and especially for those such as the armed forces who are prohibited from joining trade unions and taking industrial action.

5. The SSRB can comment only on the pay arrangements for its own remit groups. Broadly the SSRB is satisfied that it is able to obtain sufficient evidence from the Government and other parties, including members of the remit groups themselves, to make well-founded, balanced recommendations on the pay of those groups, taking account of the matters set out in our terms of reference. In most years the Government accepts and implements those recommendations although this year it reduced the SSRB's proposed pay awards for the judiciary, senior civil service and senior NHS managers to below the levels the Government had proposed in its own evidence to the SSRB.

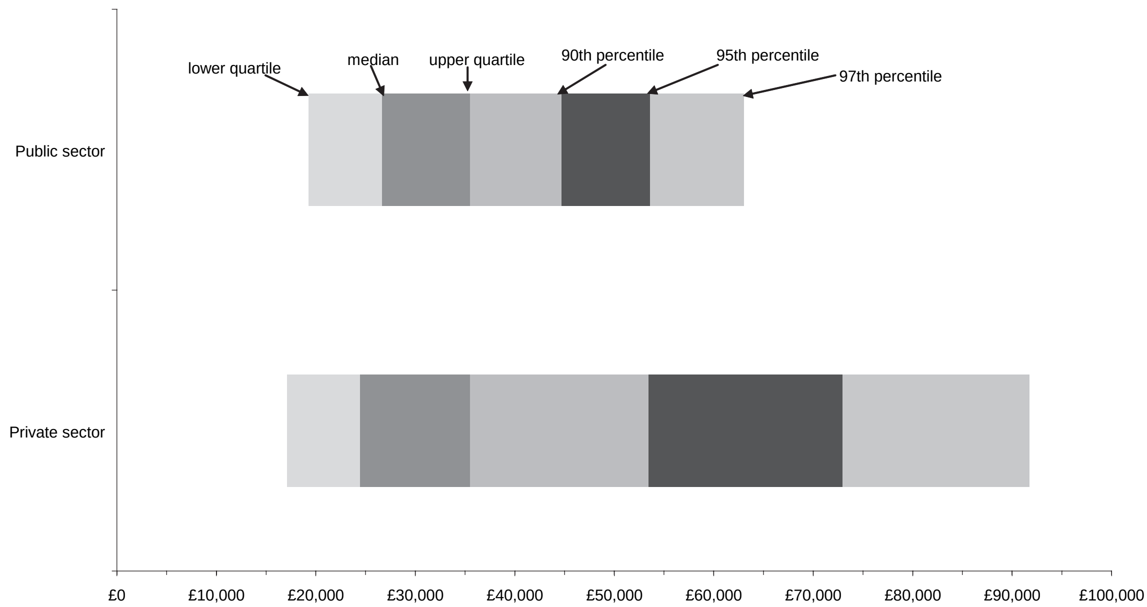
6. However, there is a particular problem with the pay for political posts where successive governments have declined to follow the SSRB's recommendations on many occasions. The result has been that pay of Ministers and Members of Parliament is now lower than is justified, in the SSRB's view, by the responsibilities of those posts. Thus the Prime Minister is currently paid £194,250,[23] Cabinet Ministers in the Commons receive £141,866 while Members of Parliament are now paid £64,766. These rates, especially for the Prime Minister and Ministers, are not commensurate with their levels of responsibility. This has led to a number of public sector workers being paid more than the politicians whom they serve. This might indicate that the intangible benefits of political office are significant and higher than elsewhere in the public sector. Moreover, pay for political posts in the UK is not out of line with that in most other European countries. In our report of our Review of parliamentary pay, pensions and allowances[24] we provided comparisons of the pay of Members of Parliament and Prime Ministers in selected countries, using Purchasing Power Parities to convert currencies. At that time British MPs were paid more than most of the other countries we looked at, with the exception of Canada, Italy, the Netherlands and the USA. Looking at Heads of Government using the same methodology, only the US President (who is also Head of State) was paid more than the British Prime Minister. It appears, therefore, that a substantial "political discount" operates in most countries.

[23] The Prime Minister and other Ministers who are Members of the House of Commons receive an MP's salary plus a ministerial supplement. The figures quoted here are the sum of the two.

[24] Report No 64, Cm 7270.

7. At higher responsibility levels, public sector pay in the UK is significantly lower than that in the private sector, as is shown by the following chart.

NATIONAL PAY DISTRIBUTION IN 2008



Source: Office for National Statistics (Annual Survey of Hours and Earnings)

Note: Basic pay for all public and private sector employees at April 2008.

We believe that pay levels for our remit groups, other than MPs and Ministers, are set broadly at the minimum necessary to recruit, retain and motivate suitable people.

8. Our arrangements are transparent. We are recruited by open competition. We consider evidence from all the parties and indeed from anyone who wishes to submit evidence to us. That evidence is normally published by the parties and we publish on the OME website any research we commission to assist us in making recommendations. We submit our reports to Government and they are normally published as command papers.

9. It is not for SSRB to judge whether its efforts produce the right results. For the most part the Government accepts our recommendations but occasionally it stages them (as in 2007) or abates them (as this year), at least in part. In the introduction to our Thirtieth Report[25] we argued against treating this small group of leaders and senior managers (our main remit groups total fewer than 8,000 people) in the same way, for pay purposes, as all other public sector workers. We suggested that the Government did so out of "fear that higher awards for our remit groups will lead to irresistible pressure from other, larger groups of public sector workers. In this view of the world 'signalling' becomes the dominant consideration."

10. As to whether the SSRB represents value for money, again that is not for us to judge. Currently the Chairman of the SSRB is paid £350 per day or part of a day when on SSRB business, plus travel expenses. Other members are paid £300 a day plus travel expenses. Our secretariat currently comprises some four full-time equivalent civil servants (including one person working exclusively on the review of MPs' pensions). The approximate total cost of operating the SSRB for the last financial year was £440,000. We cannot say whether our work inspires public confidence—it is doubtful whether much of the public is aware of what we do—but the arrangements have now been in place for nearly 40 years. The SSRB continues to attract high quality members and new groups have been added to our remit: most recently the senior NHS managers. We try to meet as many members of our remit groups as possible through annual visit programmes during which we both listen to the views and concerns of members of our remit groups and explain to them how we work. We believe the arrangements of which we are a part have served the country well, helping to avoid disputes and to balance the interests of our remit groups and taxpayers.

2. *Does there need to be consistency regarding these arrangements between different parts of the public sector?*

11. Pay varies across the public sector in part because of specific conditions or circumstances. The public sector is not a single market. Different public sector workers have different earnings potential. The demand for their skills and knowledge varies. For example, it is clear that most senior barristers or solicitors who might become High Court judges are able to earn much more in the private sector than on the bench. On balance we believe it is better to allow flexibility across the public sector to respond to differing labour market

[25] Thirtieth Report on Senior Salaries 2008, Cm 7388.

needs. Moreover, it may be necessary on occasions to recruit individuals with specialist skills, sometimes for a fixed term, for example to manage large construction contracts in connection with the 2012 Olympics, and to pay significantly above the normal rates for such posts in order to secure the services of people with skills and experience not otherwise available in the public sector. Too rigid a pay system could make it impossible to recruit specialists of the necessary calibre and would run counter to the policies of successive recent governments to encourage recruitment from the private sector into the public sector at senior levels. The current broad pay band system for the Senior Civil Service provides the necessary flexibility to fill exceptional posts.

12. On the other hand, there are undoubtedly tensions caused by the fact that pay levels differ between different parts of the public sector and we have, for example, heard complaints from senior civil servants who tell us that they deal with and do much the same work as people in other public sector bodies, eg regulatory bodies, local authorities, while being paid appreciably less than those people.

3. *Does there need to be comparability of pay between top posts in the public sector and equivalent posts in the private sector?*

(a) *If so, how should equivalent posts in the private sector be identified?*

13. In SSRB's view it is neither necessary nor justified as a general principle for the public sector to seek to match the pay of top posts in the private sector. Experience suggests that there is no difficulty in obtaining high quality people to work in the public sector. It seems clear that there are many factors which together can compensate for lower pay in the public sector: job interest, job security, pension, less competitive pressure, better work/life balance etc.

4. *Is there evidence of executive wage inflation caused by public sector organisations competing with one another for candidates?*

14. SSRB has heard anecdotal evidence that this may be the case, for example where poorly performing local authorities, schools or NHS Trusts compete to recruit chief executives, heads or other senior managers with successful records of improving organisational performance. However, we are not aware that this is a problem with the SSRB's own remit groups which have clearly defined pay systems. Nevertheless, as noted in paragraph 12, members of our remit groups increasingly point to other parts of the public sector where pay appears to be higher for no obvious reason.

5. *What role should consultancies play in the determination of pay for top public sector posts?*

15. It is normal for government departments seeking to fill specific senior posts to use recruitment consultants who will advise, among other things, on the appropriate salaries for posts. There is a danger that it is in the consultants' interest to set such salaries higher than strictly necessary in order to make posts easier to fill, and even because in some cases the consultants' remuneration may be linked to the salary on appointment. The SSRB has expressed concerns in the past, as have the Civil Service Commissioners, about departments' practices when recruiting externally. For example, in our Thirtieth Report we recommended that the Government urgently review the practices of allowing successful external candidates in recruitment competitions to negotiate salaries substantially above those advertised and of forcing existing civil servants successful in open competitions to accept salaries substantially below those available to similarly qualified external candidates. We are pleased to note that our concerns were echoed in the Normington report on Senior Civil Service Workforce and Reward Strategy, and that the Government appears to be acting on them, for example by providing better guidance to departments on recruitment practice.

16. The SSRB uses consultants to carry out job evaluation of posts from time to time to ensure that pay levels are broadly correct within organisations (internal relativity) and to check levels against the wider market. However, in SSRB's view job evaluation is not a precise science and should not be the only tool used to set pay levels. As noted in paragraph 13 above, there are often benefits other than pay from working in the public sector.

6. *Is the balance right between executive pay and other benefits, eg bonus, pension?*

17. The SSRB believes that a significant element of pay should be performance-related. Those who perform better should be paid more. We have therefore encouraged and supported the introduction and development of performance-related pay for the SCS and senior military. The judiciary argue strongly that performance-related pay is not appropriate for them. We recognise that there are some difficulties in designing and applying performance pay systems in parts of the public sector, notably for policy work, where outputs are difficult to measure. We believe there is scope to improve and extend the existing performance management and pay systems for our remit groups but we remain attached to the principle.

18. We are fully aware of the value of public sector pensions. We have commissioned work by specialist consultants to quantify the benefit of our remit groups' pensions and we take full account of total reward when making our pay recommendations.

7. *Do the pay levels for top posts in the public sector have a direct impact on the performance or qualities of the people filling those posts?*

(a) *What impact do the performance or qualities of the people filling top posts in the public sector have on the performance of the organisations for which they work?*

19. In our Thirtieth Report on Senior Salaries (2008) we wrote:

> "The groups of people whose remuneration is our concern are the leaders of several pillars on which British society is built: the law; the armed forces; the Civil Service, and (now added) the NHS. They command billions of pounds of national resource (of which their own pay is a tiny fraction) and the work of millions of people. Their quality, efficiency and motivation can improve our public services and save the taxpayer millions of pounds. The nation rightly expects these people to perform at the very highest level of their capability and that incompetent performance should not be tolerated or rewarded. These hugely dedicated people do not expect to receive the financial rewards of comparable leaders and senior managers in the private sector in return for this vital work, but they do expect recognition of the value of what they do, respect for their commitment to public service and fair pay."

8. *Is there an appropriate benchmark or ceiling for top public sector salaries—eg the salary of the Prime Minister, or a factor of average pay?*

20. We do not think there is an appropriate benchmark or ceiling because the public sector is not a single labour market. It needs to recruit and retain people with many different skills and abilities. There are different markets for eg finance directors, IT managers and HR specialists. Moreover, those markets can change over time. There are also sectoral variations, as noted in paragraph 11, above and regional differences. This makes it impossible in our view to set rigid pay rates for many public sector jobs. Moreover, as noted in paragraph 6, politicians have held down their own pay for political reasons. If the Prime Minister's salary were to constitute the ceiling for public sector pay, then either that salary would have to be increased substantially or there would be very serious difficulties in recruiting and retaining good quality senior staff in the public sector.

9. *Can England and the United Kingdom learn from the experience of other countries or the devolved governments in this area?*

21. As noted in paragraph 1 above, some of SSRB's remit groups are UK- wide while others are limited to parts of the UK. SSRB and its secretariat has frequent contact with pay-setting bodies in other countries. We are always willing to learn from other countries but on the whole we find that pay systems and levels (linked as they are to tax, social security, pensions and the cost of living) are highly specific to local circumstances.

May 2009

APPENDIX A

REVIEW BODY ON SENIOR SALARIES—TERMS OF REFERENCE

The Review Body on Top Salaries (TSRB) was appointed in May 1971 and renamed the Review Body on Senior Salaries (SSRB) in July 1993, with revised terms of reference. The terms of reference were revised again in 1998 as a consequence of the Government's Comprehensive Spending Review, in 2001 to allow the devolved bodies direct access to the Review Body's advice and in 2007 to add certain NHS managers to the remit.

The terms of reference are:

> The Review Body on Senior Salaries provides independent advice to the Prime Minister, the Lord Chancellor, the Secretary of State for Defence and the Secretary of State for Health on the remuneration of holders of judicial office; senior civil servants; senior officers of the armed forces; very senior managers in the NHS;[26] and other such public appointments as may from time to time be specified.
>
> The Review Body also advises the Prime Minister from time to time on the pay and pensions of Members of Parliament and their allowances; on Peers' allowances; and on the pay, pensions and allowances of Ministers and others whose pay is determined by the Ministerial and Other Salaries Act 1975. If asked to do so by the Presiding Officer and the First Minister of the Scottish Parliament jointly; or by the Speaker of the Northern Ireland Assembly; or by the Presiding Officer

[26] NHS Very Senior Managers in England are chief executives, executive directors (except medical directors), and other senior managers with board level responsibility who report directly to the chief executive, in: Strategic Health Authorities, Special Health Authorities, Primary Care Trusts and Ambulance Trusts.

of the National Assembly for Wales; or by the Mayor of London and the Chair of the Greater London Assembly jointly; the Review Body also from time to time advises those bodies on the pay, pensions and allowances of their members and office holders.

In reaching its recommendations, the Review Body is to have regard to the following considerations:

> the need to recruit, retain and motivate suitably able and qualified people to exercise their different responsibilities;
>
> regional/local variations in labour markets and their effects on the recruitment and retention of staff;
>
> Government policies for improving the public services including the requirement on departments to meet the output targets for the delivery of departmental services;
>
> the funds available to departments as set out in the Government's departmental expenditure limits; and
>
> the Government's inflation target.

In making recommendations, the Review Body shall consider any factors that the Government and other witnesses may draw to its attention. In particular it shall have regard to:

> differences in terms and conditions of employment between the public and private sector and between the remit groups, taking account of relative job security and the value of benefits in kind;
>
> changes in national pay systems, including flexibility and the reward of success; and job weight in differentiating the remuneration of particular posts;
>
> the need to maintain broad linkage between the remuneration of the three main remit groups, while allowing sufficient flexibility to take account of the circumstances of each group; and
>
> the relevant legal obligations, including anti-discrimination legislation regarding age, gender, race, sexual orientation, religion and belief and disability.

The Review Body may make other recommendations as it sees fit:

> to ensure that, as appropriate, the remuneration of the remit groups relates coherently to that of their subordinates, encourages efficiency and effectiveness, and takes account of the different management and organisational structures that may be in place from time to time;
>
> to relate reward to performance where appropriate;
>
> to maintain the confidence of those covered by the Review Body's remit that its recommendations have been properly and fairly determined; and
>
> to ensure that the remuneration of those covered by the remit is consistent with the Government's equal opportunities policy.

The Review Body will take account of the evidence it receives about wider economic considerations and the affordability of its recommendations.

APPENDIX B

Senior Salaries Review Body

Bill Cockburn CBE TD

Professor David Greenaway

Michael Langley

Sir Peter North, CBE QC

Paul Williams

David Metcalf

Richard Disney

Martin Fish

Christopher Stephens

Bruce Warman

Memorandum from the TaxPayers' Alliance

Summary

- The current levels of executive pay in the public sector are a matter of serious concern. The escalating costs of senior managers and executives over the past decade, without parallel improvements in services or efficiency, have done much to undermine the public's faith in taxpayer funded bodies. Furthermore, a lack of transparency over pay in some parts of the public sector has weakened already minimal levels of accountability.
- It was with the aim of throwing light on public sector executive pay that the TaxPayers' Alliance (TPA) instigated the annual Town Hall and Public Sector Rich Lists, the impact of which is noted in the Committee's call for evidence. These two documents have exposed the rewards for failure, excessive wage inflation, and frequent over-promotion which are now all too common in the public sector.
- It should be noted that increased transparency and rigour in the setting and monitoring of executive level public sector pay does not have to mean an end to appropriate financial rewards. Many senior public sector jobs are not only difficult but critically important, requiring a level of professional skill or a past career of service that needs to be remunerated accordingly. This will sometimes necessitate pay and conditions sufficient to compete with private sector employers.

The real abuses in senior public sector pay take place away from the very few high profile positions that demand valuable qualification or experience. The majority of highly paid senior public sector jobs are not affected by a particular scarcity of suitable candidates and the key consideration in the setting and monitoring of executive pay must be value for money; "what is the lowest amount we can pay while securing a suitable candidate".

At the moment taxpayers are not getting value for money. Most top posts are not filled by individuals with a history of well remunerated private sector work, and there is little chance that senior managers will leave for better paid work elsewhere. The Chief Executives of England's Regional Development Agencies for instance, are universally career public servants, whose prospects in the private sector are far fewer than they would suggest. Pay must reflect these realities (including benefits, job security and accountability) not just faux-comparisons with private sector executives in charge of equivalent budgets or staff numbers. It must also be completely transparent to the general public, allowing them, through "shareholder activism", to monitor and assess whether top public sector remuneration is fair and well earned. The fact that such practices are not always obvious in the private sector should not inhibit the public sector from embracing them; the public sector has the opportunity to lead the way.

Response to Key Questions

1. *Are the right arrangements in place for setting and monitoring pay and other benefits for top posts in the public sector?*

No. At best public sector bodies and authorities are covered by central government guidance on pay, but most are free to set pay and conditions entirely independently. The system of "remuneration panels" and "remuneration boards", in which most public sector executive pay is set are inadequate; ordinary taxpayers are rarely represented. As currently set up, those responsible for setting and monitoring pay and benefits are likely to gain directly from salary increases and improved benefits, eliciting a clear conflict of interest.

(a) *Are they fair?*

No. Current arrangements will seem fair to public sector executives, but they are unfair to taxpayers. For instance the generous rewarding of public sector executives after serious management failures are an abhorrent abuse of resources, particularly as they are awarded to executives who enjoyed massive salaries, prior to their dismissal, for being "excellent managers" when clearly they were not. We understand that current contractual agreements often necessitate pay-outs and compensation. That does not excuse them however. In the future public sector executive employment contracts must contain clauses that exclude the possibility of payouts or compensation for loss of office should the individual be made to resign for reasons of proven poor performance.

(b) Are they transparent?

No. It is extraordinarily difficult for the public to establish the exact pay and conditions of public sector executives, let alone the details of how such remuneration packages were agreed. Often it is only at the termination of contracts that we find out what pay and benefits individuals received. All minutes, agreements and memos pertaining to the setting of pay and conditions for board level and £100,000 plus earning members of public sector bodies should be available online, and a clear remuneration report (containing details of all board level and £100,000 plus earning employees) should be made a mandatory part of every public sector body's annual publications.

(c) *Do they produce the right results?*

No, as the many cases of unwarranted and egregious pay and benefit settlements evidence. For example, despite multiple independent reports concluding that the outbreak of MRSA at Maidstone and Tunbridge Wells NHS Trust came about from a tragic failure in hospital management, Rose Gibb, the Trust's Chief Executive, left with a generous compensation package. The public was rightly outraged.

Similarly, Parliamentary Committees, the NAO and the Financial Services Authority's own investigation all concluded that the FSA's management had been asleep at the wheel in the run up to collapse of Northern Rock and subsequent financial crises, but Clive Briault (Managing Director of Retail Markets at the FSA) still received a compensation package in excess of half a million pounds on his dismissal.

(d) *Do they provide value for money?*

No. Current arrangements do not provide value for money, allowing as they have the explosion of over-generous salaries, enormous pay-offs and excessive benefits.

(e) *Do they inspire public and political confidence?*

No. As stories such as those outlined in answer C become ever more common, the public loses confidence in the current arrangements. Note the commitment of all three main political parties to reforming aspects of top level public sector pay.

2. *Does there need to be consistency regarding these arrangements between different parts of the public sector?*

Not necessarily. The public sector is vast, encompassing a huge variety of professions. Arrangements to set executive pay will need to reflect this. However there should be consistency across the public sector regarding transparency. All individuals employed at executive level positions, in organisations funded by the taxpayer or controlled by Government (whether central or local) should have their total remuneration details published each year. The "total remuneration" shown must include salary, bonus, benefits in kind, employer pension contributions, compensation for loss of office, relevant termination payment, etc.

This level of transparency is already found in certain parts of the public sector, but it should be mandatory for all of it.

3. *Does there need to be comparability of pay between top posts in the public sector and equivalent posts in the private sector?*

Only for a select few senior posts in the public sector is comparability necessary or desirable, and even then the comparative private sector job should be used only as a reference, not a benchmark. If nothing else it is very difficult to find comparable jobs between the private and public sectors, beyond crude comparisons on organisational size and budget. These crude comparisons ignore the fact that private sector chief executives have different sets of priorities (profit maximisation) and pressures (competition), and thus different risks to public sector top posts.

One obvious difference is job security; the risk to one's job is higher in the private sector, as poor performance is far more likely to lead to dismissal. Additionally, poor performance of an executive in the private sector can mean many other workers lose their jobs; this is rarely the case in the public sector. Remuneration in the private sector should therefore be higher to reflect these risks.

(a) *If so, how should equivalent posts in the private sector be identified?*

Most top public sector jobs do not have a comparator in the private sector; with a virtual monopoly on healthcare, NHS managers cannot bench their pay to some private sector equivalent when private sector healthcare is almost exclusively a high value niche. The same applies to Council Chief Executives, whose closest comparator would be a central government permanent secretary (whose pay is far less than most Council Chief Executives). Comparisons with positions in the City of London or FTSE 100 companies are particularly distorting and should be avoided; the claim that public sector executives, who have worked in the Civil Service or public sector all their lives, could walk into higher paid private sector jobs is often not very credible. Again, the primary factor in determining the correct level of pay must be an assessment of the availability of suitable candidates and value for money.

4. *Is there evidence of executive wage inflation caused by public sector organisations competing with one another for candidates?*

Yes, but largely anecdotal. Competition between councils over Local Authority Chief Executives is a common occurrence, as is competition between NHS Trusts. In central government, senior civil servants now move between departments regularly, often receiving higher remuneration packages with each move. Among non-departmental public bodies, in some areas the sector is so entirely dominated by taxpayer funded bodies (most obviously in health, but also with the near total monopolisation of green and environmental issues by DEFRA, the Department for Energy and Climate Change, the Environment Agency, Carbon Trust, WRAP, Energy Savings Trust, Encams and various taxpayer funded NGOs) that job competition is almost entirely constrained to that between public sector (or publicly funded) organisations.

5. *What role should consultancies play in the determination of pay for top public sector posts?*

None; the use of consultancies to advise on pay does little to encourage public confidence in the system or deliver value for money, often acting as little more than an expensive rubber stamp. Some consultancies are little more than employee groups designed to push up pay. Local councils in particular have been guilty of relying too heavily on the services provided by companies such as Solace Enterprises, a company owned by the Society of Local Authority Chief Executives and Senior Managers, the professional body for senior Local Government employees and thus a directly interested party. Note too that recent sharp rises in public sector executive pay is concomitant with the increased use of consultancies.

6. *Is the balance right between executive pay and other benefits? Eg. bonus, pension*

The issue is more complex than simply getting the relative amounts right. For one, the generous employer contributed pensions linked to most top posts in the public sector must be understood as significant additional pay awarded each year. The fact that such pension schemes very occasionally exist in the private sector does not make them excusable for the public sector. Such arrangements are—as the Institute of Directors have shown—incredibly rare in the private sector, where most executives do not enjoy anything like the benefits enjoyed by retired senior public sector workers.

Secondly, the methodology behind the awarding of performance related bonuses or pay is unclear. Does the "performance" relate to the individuals or the organisation? If performance is measured on the organisation as a whole (and public sector bodies are almost always found to be performing "well") top posts will be constantly rewarded. But this does not tell us anything substantive about the performance of the individuals or the organisation as a whole, and it does not form an appropriate basis for a bonus. Performance related pay must be linked to proper measures of performance (of the individual and the organisation as a whole), clearly stated and explicable.

Importantly, the debate over public sector bonuses and benefits must not be hijacked by discussions about activities associated with the relatively small and unique parts of the private sector, in particular the City of London. Such practices are applied to very few individuals, and are highly unrepresentative of how pay and conditions are set for the vast majority of those who work in the private sector.

7. *Do the pay levels for top posts in the public sector have a direct impact on the performance or qualities of the people filling these posts?*

Top posts in the public sector are very well remunerated, by any standard or measure. Moreover, if individuals in top posts do not perform to the best of their abilities at all times, regardless of pay, then they are not suitable for the job. Public sector workers often stress that they do their jobs, in part, out of sense of duty; this attitude must be reintroduced into the top levels of the public sector.

(a) *What impact does the performance or qualities of the people filling top posts in the public sector have on the performance of the organisations for which they work?*

Leadership can have a considerable influence on the performance of an organisation. The qualities and performance of the senior members of public sector bodies will no doubt have a significant impact, as we have too often seen when over-promoted officials take on top posts, leading to unfortunate results.

Improving the quality and motivation of staff in the public sector is not just, or even primarily, a matter of money. Giving staff real autonomy, the freedom to make decisions and the chance to take responsibility for the results (good or bad) will improve staff satisfaction, motivation and performance, much more than increased pay.

8. *Is there an appropriate benchmark or ceiling for top public sector salaries—eg the salary of the Prime Minister, or a factor of average pay?*

Most public sector employees should not earn more than the Prime Minister, who is quite well paid compared to senior managers in all but the largest private sector companies. However, if we want to see good managerial talent come in from the private sector, taking over public sector organisations, than we may (in a few, very special circumstances) have to accept pay at levels higher than the PM. It is important to accept that hard rules and simplistic benchmarks are no substitute for transparency and controlling pay on the basis of a democratic judgement about the level of pay that is acceptable.

9. *Can England and the UK learn from the experience of other countries or the devolved governments in this area?*

The United States has pioneered transparency in public sector pay. Easily accessible databases with positions and pay scales are available in many states, with some going further still, detailing the exact pay and perks of every state employee by name. Such a level of transparency should be imposed on all senior management positions in the UK public sector.

In terms of the levels of executive pay, President Obama acknowledged the need for action (for both political and economic reasons) and froze the pay of any White House Staff earning over $100,000 on his first day in office. A similar move should be replicated here, with the pay of all senior public sector staff frozen immediately to reflect the recession and falling pay in the private sector.

April 2009

Memorandum from Stephen Taylor, Director of Taylor Haig

A few quick thoughts which may run against the underlying implication of some of the questions:

- it is highly desirable that managers at many levels, including the top, are able to move reasonably easily between the public and private sector. Each sector would be much the poorer without the mutual understanding which this movement enables. The loss of that understanding in return for a little money saved from senior public sector salaries would be a very bad bargain indeed. So I am afraid you cannot insulate the public sector remuneration debate from the private sector one;
- the skills, demands, accountability, exposure and insecurity of running, say, a £500 million council are absolutely not of a different order from those of running a £500 million business (I know, I've dealt with lots of both over the last 30 years). The pay of the latter—your remuneration consultants will give you the correct answer—is probably at least four times the former;
- the pay of local government chief executives should be determined by local politicians. If the local populace don't think they get value they can vote for a new lot;
- in general we get extraordinarily good value for money from the roughly 1000 people at the top of our public services; more than we deserve given the small-minded abuse they get;
- you cannot deal with this subject without dealing also with both performance pay and pensions; the mix of salary + performance pay + pension (never mind the total) is very different in public and private sector. The answer is a much larger performance element and the end of index-linked pensions for the public sector;
- history shows that holding down top pay does no more than that, ie it does not hold down pay at lower levels. All that happens is differentials are squeezed and then fewer people strive for the top jobs. That is already the case in the Civil Service; and
- senior public servants don't have the tax planning/avoidance opportunities of the private sector. In other words, they pay the full marginal rate on all their earnings.

The only thought I'd add is that while in principle "the market" should determine top salaries, it is as we know highly imperfect. So we need some additional mechanism, but not please national control on the grounds of "consistency", "fairness" or some other nonsensical rationale for centralisation. I'm attracted to the idea of a ratio, eg that we wouldn't expect the top salary in a public sector organisation to be much more (or indeed much less) than X times its average salary and would look for justification if it was. We can then debate what X is, and perhaps it changes over time. I think it's about 8.

I'd also, by the way, be interested in the ratio of chief executive salary to the level immediately below. Needs to be at least 1.3:1.

Re your question 7, my main learning about pay after 30 years is that people don't in fact think about it very much provided they don't feel unfairly treated, that the greatest source of feeling unfairly treated is not the absolute but relative level, and that relativities near to home (eg if I'm a university vice-chancellor then other vice-chancellors, not company marketing directors) are what matter.

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