IS ‘SAY-ON-PAY’ THE MOST REASONED APPROACH TO EXECUTIVE REMUNERATION ACCOUNTABILITY?: AN ASSESSMENT OF THE MEANINGFULNESS OF UK AND US ‘SAY-ON-PAY’ FRAMEWORKS

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A. INTRODUCTION
B. CONTEXTUALIZING THE LEGAL LANDSCAPE OF SAY-ON-PAY
C. A REVIEW OF THE WISDOMS OF SAY-ON-PAY
D. THE SHORTCOMINGS AND POTENTIAL IRRELEVANCE OF SAY-ON-PAY
E. ARE THE CURRENT SAY-ON-PAY FRAMEWORKS THE END ALL BE ALL SOLUTION FOR EXCESSIVE REMUNERATION?

A. INTRODUCTION

The issue of excessive executive remuneration is no stranger to scrutiny in numerous countries over the recent times.[1] The prominence of this debate, now more than ever, is largely attributable to the rise in shareholder activism, financial populism and the renewal of the public interest, particularly due to the most recent financial crisis, for ‘exacerbat[ing]’ income inequality.[2] Even though there is no standard definition for what exactly falls within the scope of ‘excessive’ compensation,[3] the contentiousness of this issue as the most ‘egregious corporate governance failure’ is well-founded, primarily considering that the ratio of CEO pay to average worker pay has increased from 20 or 30 to 1 in the 1960-70s to 200 or 300 to 1 in the past few years.[4] As a response, ‘say-on-pay’ legislation was introduced with the purpose of granting shareholders an advisory vote on the executive remuneration put forward by the board of directors. The pioneering legislator of this mandate is the UK in 2002, purportedly with the intention of promoting corporate governance efficiency within the corporation and increase the degree of accountability of the board to their shareholders.[5] Say-on-pay has grown increasingly common, with other states following the UK’s steps, however the periodicity and the nature of the voting inevitably differ due to the varying degrees of ‘concentration of ownership,…institutional ownership,…social tolerance toward income inequality, and certain political influences’.[6]

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[1] Thomas A Hemphill and Wadeeha Lillevik, 'US "Say-on-Pay" Legislation: Is it Corporate Governance Overreach?' [2009] 51(2) International Journal of Law and Management 105-117, 107.

[2] Dean Baker, Josh Bivens, et al, 'Reining in CEO compensation and curbing the rise of inequality' (Economic Policy Institute, 4th June) <https://www.epi.org/publication/reining-in-ceo-compensation-and-curbing-the-rise-of-inequality/> accessed 19 December 2023; Thomas Picketty, *Capital in the Twenty-First Century* (1st edn, Harvard University Press 2014), 290.

[3] Stephani A Mason, et al, 'Say-on-Pay: Is Anybody Listening?' [2017] 20(4) Multinational Finance Journal 273–322, 281.

[4] Baker, Bivens et al (n 2); Picketty (n 2), 290.

[5] MJ Conyon and G Sadler, 'Shareholder Voting and Directors’ Remuneration Report Legislation: Say on Pay in the UK' [2010] 18(4) Corporate Governance: An International Review 296-312, 297.

[6] Konstantinos Stathopolous and Georgios Voulgaris, 'The Importance of Shareholder Activism: The Case of Say-on-Pay' [2016] 24(3) Corporate Governance: An International Review 359-370, 362.

The nature of say-on-pay later evolved into a dual-vote – an advisory vote on the annual remuneration report and a binding vote on the remuneration policy.[7] Having considered that, whether the growing political support for advisory say-on-pay on the remuneration report is rightly placed is a question that has been subjected to considerable academic debate.[8] Given how the US is known for its traditionally unwavering emphasis on 'business-friendly corporate laws', their introduction of say-on-pay is fairly monumental,[9] and it is certainly worthwhile to consider the legal developments and implications taking place there in comparison to the UK.

Therefore, this essay aims to contribute to the ongoing debate on the meaningfulness of 'say-on-pay' on the remuneration report as a corporate governance mechanism that aims to limit excessive executive remuneration and the harmfulness manifested by it in the UK and US. This will be achieved by contending that while this development in corporate governance has the potential to reduce the level of overly-exaggerated compensation packages, a greater emphasis needs to be placed on striking a balance between income fairness and aligning the interests of managers with shareholders to reduce overall agency costs. This argument will be made on the grounds that the current say-on-pay frameworks in the UK and the US are not only ineffectively designed, but also ineffectively utilized, given the observed low levels of voting dissent on remuneration policy.[10]

This essay will first examine the legal landscape of say-on-pay in the UK and US in section II, and then consider the benefits and shortcomings of say-on-pay in sections III and IV in relation to both jurisdictions. Lastly it will assess whether say-on-pay can be considered as the most reasoned approached to executive remuneration accountability by drawing on other mechanisms that could conceivably decrease excessive executive remuneration in section V.

B. CONTEXTUALIZING THE LEGAL LANDSCAPE OF SAY-ON-PAY

The controversy of the suggested 70% increase in the remuneration package of the CEO of British Gas Plc in 1994 triggered the enactment of the Directors' Remuneration Report Regulations in 2002 by virtue of s.257 of the Companies Act 1985.[11] It mandated the disclosure of executive compensation in an annual report submitted at the Annual General Meeting at an unprecedented degree of detail and granted shareholders an advisory vote

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[7] Companies Act 2006, s. 439A(7)(a).
[8] Stephen M Bainbridge, 'Is 'Say on Pay' Justified?' (2009) UCLA School of Law, Law-Econ Research Paper No. 09-19/2009 < https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1452761> accessed 19 December, 2023.
[9] Martin Petrin, 'Executive Compensation in the UK: Past, Present, and Future' [2015] 36(7) The Company Lawyer 196-204, 196.
[10] Ibid, 199.
[11] The Directors' Remuneration Report Regulations 2002; Lee Roach, 'The Directors' Remuneration Report Regulations 2002 and the Disclosure of Executive Remuneration' [2004] 25(141) The Company Lawyer 1-13, 1.

to provide their assent or dissent of the remuneration report.[12] The effectiveness of this was bounded by shareholder apathy more often than not, as less than 10% abstain or voted against remuneration reports resolution.[13] It was speculated that the reason for this was either 'efficient monitoring, entrenchment issues or other firm related determinants'.[14] Meanwhile, the CEO pay in the UK grew a multiple of 47 times the average worker to 120 times between 1998 and 2010. The continuous concern regarding the disparity between the two and the aim of the legislation is justified when considering their repercussions on the productivity and incentives of employees and the broader impact on society at large through issues of fairness and distributive justice.[15]

Nevertheless, it is fair to deduce that the non-binding nature of the remuneration report vote is the reason for the lack of desired change and growth of executive pay as concluded by Ferri and Maber's comparative study which considered firms between 2000 to 2002 and 2003 and 2005.[16] However, this overlooks that directors will have to face 'shareholder outrage' in case they proceeded with a compensation proposal that was largely voted against, of which can cause reputational harm and additional costs.[17] The circularity of this is amplified when considering that the majority of shareholders in the UK tend to be institutional investors who possess short-term goals and are not known for being engaged as stewards partaking in shareholder-activism.[18] The early and fragmented success of say-on-pay as an advisory vote is evident with the link established between the performance of a firm with executive remuneration, which in turn reduced executive rewards for failure.[19] It cannot be implied from this link that the legislation had any significant impact on the alignment of pay with performance.[20] The introduction of the say-on-pay framework in the UK was partly praised on the basis of the assumption that there is 'no doubt' that companies and their shareholders agree that it 'improved communication between boards and shareholders'.[21] Regardless, the 2002 say-on-pay was not without fault, as this success remains 'questionable'.[22] This is because relying on an integrated system of mandatory disclosure, an advisory vote, along with remuneration committees has not effectively lowered rising remuneration levels.[23] Furthermore, a wider

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[12] Ibid, Sch.7A; ibid, 5.
[13] Conyon and Sadler (n 5), 297.
[14] Stathopolous and Voulgaris (n 6), 366.
[15] Petrin (n 9), 197.
[16] Fabrizio Ferri and David A Maber, 'Say on Pay Vote and CEO Compensation: Evidence from the UK' [2011] 17(2) European Finance Review 527-563, 554.
[17] Lucian Ayre Bebchuk and Jesse M Fried, 'Executive Compensation as an Agency Problem' [2003] 17(3) Journal of Economic Perspectives 71-92, 75.
[18] Brian R Cheffins, 'The Stewardship Code's Achilles' Heel' [2010] 73(6) The Modern Law Review 1004-1025, 1004.
[19] Ferri and Maber (n 16), 554.
[20] Petrin (n 9), 199.
[21] Andrew Clark, 'US research backs Britain's 'say on pay'' (*The Guardian*, 5 March 2008) <https://www.theguardian.com/business/2008/mar/05/executivesalaries.useconomy> accessed 21 December 2023.
[22] Petrin (n 9), 199.
[23] Ibid, 199.

scope of disclosure had an adverse impact in some instances, which could make the impact of say-on-pay redundant.[24]

The 2008 recession made shareholders, the public and the Government more 'acutely aware' of the excessive levels of executive remuneration.[25] As a result, shareholders' voices were strengthened with the introduction of additional disclosure regulations that were accompanied by the enactment of reforms in the Enterprise Regulatory Reform Act 2013.[26] This reform granted shareholders with a three-yearly binding vote on their company's remuneration policy every three years.[27] It also provided an advisory vote on the annual report on remuneration, which lays out the payments and benefits given to directors every financial year.[28] This change was perceived as 'over-engineered' and 'unlikely' to curb rising executive pay levels. This perception was validated, to some degree, by initial findings that reported that average CEO pay of FTSE 100 increased by 5% between the years 2012 and 2013.[29] While some caveats apply to the empirical data such as change in CEOs, the figures still provide valuable insight on the initial impact, or lack thereof, of complementing the advisory remuneration report vote with a binding say-on-pay vote.[30]

An advisory say-on-pay framework was set in the US through the Dodd-Frank Wall Street Reform and Environmental Protection Act 2010 to counterbalance the 'substantially greater powers' that UK shareholders held prior to its introduction.[31] The troublesome nature of executive compensation was also being recognized at a wider scale in the US, with 61% of corporate directors believing that the current compensation models are problematic in 2007.[32] The premise of this non-binding vote on both remuneration reports and policies was to handle the way in which remuneration arrangements 'often fail' to give executives the appropriate incentives to fulfill their fiduciary duty to maximize shareholder wealth and align both of their interests.[33] As this

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[24] Alan Dingam, 'Remuneration and Riots: Rethinking Corporate Governance Reform in the Age of Entitlement' [2013] 66(1) Current Legal Problems 401–441, 410.

[25] The Department for Business, Innovation and Skills, 'Executive Remuneration: Discussion Paper' (gov.uk, September 2011), 4 <https://assets.publishing.service.gov.uk/media/5a78cab040f0b6324769a335/11-1287-executive-remuneration-discussion-paper.pdf> accessed 21 December 2023.

[26] Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013; Charlotte Villiers, 'Executive Pay: A Socially-Oriented Distributive Justice Framework ' [2016] 37(5) Company Lawyer 139-154, 139.

[27] Enterprise Regulatory Reform Act 2013, s.79.

[28] Carsten Gerner-Beuerle and Tom Kirchmaier, 'Say on Pay: Do Shareholders Care?' (2018) The European Corporate Governance Institute Finance Working Paper 579/2018, 2 <https://www.ecgi.global/sites/default/files/working_papers/documents/finalgerner-beuerlekirchmaier.pdf> accessed 21 December 2023.

[29] High Pay Centre, 'High Pay Centre Briefing: The Effect of Executive Pay Reforms' (*High Pay Centre*, 2 June 2014) <https://highpaycentre.org/high-pay-centre-briefing-the-effect-of-executive-pay-reforms/> accessed 21 December 2023.

[30] Ibid.

[31] Stathopolous and Voulgaris (n 6), 363; The Dodd-Frank Wall Street Reform and Environmental Protection Act 2010; The Securities Exchange Act 1934, s.14A.

[32] Sandeep Gopalan, 'Say on Pay, and the SEC Disclosure Rules: Expressive Law and CEO Compensation' [2007] 35(2) Pepperdine Law Review 101-163, 102.

[33] Bainbridge (n 8), 43.

reform was modeled after the then-existing UK's say-on-pay, it provided shareholders with a three-yearly non-binding vote, a say on the frequency of the vote and the right to vote on executive severance packages.[34] However, it was met with stronger criticism than it did in the UK. It was argued that it would increase agency costs and would cause a 'federalization' of corporate governance legislation, which would in turn have harmful consequences on the way the capital market operates in the US.[35] Beyond such issues, it was also expected to cause a 'major overreach' to the available provisions that gave the board the authority to manage the pay-setting process.[36] Though, upon its application, boards were found to be reactive to negative say-on-pay votes by lowering excessive remuneration.[37] On the other hand, it was also reported that, like the UK, the number of dissatisfied shareholders with executive packages is generally low as negative says never exceeded 3% and has even dropped to 1.7% in 2016.[38] Additionally, say-on-pay did not 'significantly reduce' CEO remuneration as intended.[39] The reasoning for this will be further examined in sections III and IV.

C. A REVIEW OF THE WISDOMS OF SAY-ON-PAY

The underpinning of say-on-pay is to 'correct social harms' caused by excessive executive pay. Such harms are manifested by denying shareholders, employees and other contributing stakeholders of the portion of the benefits that executives tend to reap for themselves.[40] As a result of this denial, the political economy generating society's wealth may be endangered by 'diffused mistrust, resentment and anger'.[41] On the other hand, Walker suggests, the cost of excessive remuneration may be recognized as one that is 'borne solely' by the shareholders,[42] as they are the residual claimants of the remaining profits of the corporation.[43] Within this risk that they bear, shareholders expect managers to maximize the company's value, thereby maximizing their dividends.[44] This, however, tends not to be the case when managers prioritize the maximization of their own remunerations.[45] Therefore, the assumed advantage of using a shareholder-centric

[34] Jill E Fisch, Dairius Palia, et al. 'Is Say on Pay All About Pay? The Impact of Firm Performance' [2018] 8 Harvard Business Law Review 101-129, 105.
[35] Bainbridge (n 8), 45.
[36] Hemphill and Lillevik (n 1), 114.
[37] Paul Hodgson, 'Surprise surprise: Say on Pay appears to be working' (Fortune, 8 July 2015)<https://fortune.com/2015/07/08/say-on-pay-ceos/> accessed 21 December 2023.
[38] Semler Brossy, '2016 Say on Pay Results: End of Year Report ' (*Semler Brossy*, 1 February 2017) <http://www.semlerbrossy.com/sayonpay> accessed 21 December 2023, 3-2.
[39] Fisch and Palia et al (n 34), 106.
[40] Mason (n 3), 309.
[41] Ibid.
[42] David I Walker, 'Who Bears the Cost of Excessive Executive Compensation (and Other Corporate Agency Costs)' [2012] 57(3) Villanova Law Review 653-674, 671.
[43] Armen A Alchian and Harold Demsetz, ' Production, Information Costs, and Economic Organization' [1972] 62(1) American Economic Review 777-795, 782–783.
[44] Faith Bugra Erdem, 'The Steps Taken by Say-on-Pay towards Shareholder Primacy: An Anglo-Saxon Perspective' [2022] 5(1) Strathclyde Law Review 133-140, 137.
[45] Ibid.

approach, that being say-on-pay, to curb very high executive pay, is that as the residual claimants, shareholders possess the incentive to effectively monitor the proportionality of the executives' pay with their performance.[46] This line of argument, however, is limited by the reality of shareholders being 'typically' unable to effectively conduct this monitoring function.[47] This is traceable to the collective action problem, as discussed by Berle and Means, both of whom contended that the diffusion of ownership amongst varying classes of shareholders reduces their incentive to participate in governance, based on the assumption that their vote would not influence the outcome.[48] Irrespective of that, say-on-pay is continuously rationalized with the agency-based theoretical model, built on the understanding that the separation between ownership and control manifests agency problems between the agent (directors) and the principal (shareholders). This rationale is reiterated by considering it against the lens of the 'managerial power perspective', which purports that weak governance structures enable the saturation of power with the CEO over the board and may enable them to act in their self-interest and control their own pay, thusly participating in rent extraction.[49] Nevertheless, the effective use of say-on-pay rests on the presumption that the board's decision will not be swayed by the costs and constraints of 'outrage' from relevant stakeholders.[50] In light of that, directors will be 'reluctant' in the first place to propose excessive compensation packages because of embarrassment or to avoid reputable harm, as evidenced in the past.[51] While this may lead to the inference that the board's reaction in fear of outrage could achieve the aims of say-on-pay by curbing the level of executive remuneration, the board could still resort to adopting 'camouflage' tactics to legitimize high executive pay.[52] In such cases, tighter transparency measures and enforcing a binding say-on-pay on the remuneration report may provide the oversight and control necessary. In that light, say-on-pay was still reasoned by some of the public to be 'a balanced, non-disruptive mechanism' for lessening agency costs, which are the 'most troubling and corrosive obstacles to the efficient operation of the market'.[53]

In justifying say-on-pay, it is important to examine the alternative view to the managerial power perspective, which views the agency problem from the lens of the 'optimal contracting' perspective.[54] This popular view asserts that executive pay arrangements are set by the board with the objective of minimizing agency costs by maximizing shareholder value and aligning shareholder interests with directors' interest,

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[46] Sung Eun(Summer) Kim, 'Dynamic Corporate Residual Claimants: A Multicriteria Assessment' [2021] 25(1) Chapman Law Review 67-96, 85; Alchian and Demsetz (n 43) 782–783.
[47] Ibid.
[48] Adolf A Berle and Gardiner C Means, *The Modern Corporation and Private Property* (2nd edn, Routledge Taylor and Francis Group 1991) 76-82; FrankH Easterbrook and Daniel R Fischel, 'Voting in Corporate Law' [1983] 26(1) Journal of Law and Economics 395-427, 407.
[49] Robert F Gox and Thomas Hemmer, 'On the relation between managerial power and CEO pay' [2020] 69(2-3) Journal of Accounting and Economics 1-22,1.
[50] Bebchuk and Fried (n 17), 75.
[51] Ibid; Kenneth J Martin and Randall S Thomas, 'The Effect of Shareholder Proposals on Executive Compensation' [1999] 67(4) University of Cincinnati Law Review 1021-1082, 1064.
[52] Bebchuk and Fried (n 17), 76.
[53] N Minnow, 'Should shareholders have a say on pay?– Yes' (*Investment News*, 21 May 2007) <https://www.investmentnews.com/industry-news/news/should-shareholders-have-a-say-on-pay-yes-9201> accessed 21 December 2023.
[54] Bebchuk and Fried (n 17), 71-76.

by creating an ‘optimal principal-agent contract’.[55] The limitations of this perspective primarily begins with traditional consensus that the CEO ‘dominates’ the director appointment process, considering the rather infrequent use of independent nominating committees.[56] Additionally, market forces, such as the market for managerial labor or corporate control, cannot be depended on to align shareholders’ and directors’ interests. Bebchuk, Fried and Walker convey this by referring to the unlikely risk of executive dismissal on the basis of executive compensation levels, as such an occurrence would be strongly dependent on the company’s overall performance.[57] Further reiterating this is the argument that any added takeover risks are unlikely to deter executives from proposing the most generous pay possible for themselves.[58] Considering that, even though a rather dated study on Forbes 800 firms demonstrated that takeovers are more likely to take place in industries with overpaid CEOs, no difference was found between the remuneration levels of targeted and untargeted companies.[59] Current compensation practices mirror a blended mix of the optimal contracting and managerial power perspectives, therefore without any oversight from shareholders, it is plausible that managers will receive pay that is not so optimal, perhaps even not optimal for shareholders.[60] This demonstrates that the practice of say-on-pay is essential to reduce the level of executive compensation levels to some degree.

Say-on-pay on remuneration reports has the potential to transform the executive pay status quo for corporations with ‘unusually excessive’ remuneration arrangements, especially in poorly performing firms. While empirical data was yielded in support of that in both the UK and the US, where it was noted that boards have reacted to dissenting votes, it is important to note that this was only within the remit of firms with excessive CEO compensation as well as low financial performance.[61] Furthermore, the votes still had no significant general impact on the average level of CEO pay.[62] Even though the impact is reportedly limited to underperforming firms with overly excessive remuneration, it cannot be overlooked that say-on-pay has the prospective of putting a stop to ‘rewards for failure’ by enhancing the link between pay and performance.[63] However, the practice of this can demoralize not just executives but employees as well because the corporation’s performance is based on a ‘team’s effort’ in an environment generated by them as stakeholders.[64] It is important to consider that this could lead to a ‘luck-based’ pay practice where executives receive higher compensation if profits increase, even if this was manifested by external factors instead of their efforts.[65] Additionally, the rationale of

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[55] Lucian A Bebchuk, Jesse M Fried and David I Walker, ‘Executive Compensation in America: Optimal Contracting or Extraction of Rents?’ (2001) National Bureau of Economic Research Working Paper No. 8661, 1-2 <https://www.nber.org/papers/w8661accessed> 25 December 2023.
[56] Ibid, 14.
[57] Ibid, 24.
[58] Ibid, 26.
[59] Ibid.
[60] Ibid, 3.
[61] Fisch, Palia, et al. (n 32), 103 ; Petrin (n 9), 199.
[62] Ibid.
[63] Ferri and Maber (n 16), 558.
[64] Jeffrey N Gordon, '"Say on Pay": Cautionary Notes on the UK Experience and the Case for Shareholder Opt-In ' [2009] 46(1) Harvard Journal on Legislation 323-367, 328.
[65] Bebchuk and Fried (n 16), 77

‘pay for performance’ embraces excessive executive pay if it is proportionate to the financial performance, which negates the purpose of say-on-pay in both the UK and US and brings into question whether ‘pay for performance’ is the ultimate objective.[66] Having said that, even in light of the COVID-19 pandemic, the increase in investor scrutiny was still attributable to the strengthened spotlight on pay for performance, as the level of support received in the US for non-binding say-on-pay votes was less than 65% in 14 companies in the S&P 500 in 2021.[67] As Mason et al. contend, the say-on-pay movement was driven by the ‘public interest theory’ and was manifested to address market failures and develop public good.[68] The consideration of market forces as ‘not sufficiently strong and fine-tuned’ enough is a coherent argument when taking into account the limitations of the labor market for executives, the market for corporate control and capital.[69] This concern needs to be emphasized when attempting to achieve the desired outcomes of the ‘optimal contracting model’.

Meanwhile, some of the notable success of say-on-pay is evidenced by the increased likelihood of boards to adopt ‘reasonable’ pay policies.[70] For instance, Imperial Brands Group in the UK was influenced by its investors to rescind a large bonus increase to their CEO.[71] On the other hand, BP Plc proposed a pay policy to cut the CEO’s remuneration by 40%, which received considerable approval from their investors.[72] Regardless, these reactions to binding policy say-on-pay votes differs vastly to remuneration report non-binding votes. Exemplifying this is the binding 96% favoring vote to the company’s remuneration policy with a simultaneous 58% opposing majority of shareholders in Crest Nicholson to the remuneration implementation report, yet the remuneration proposal remained unchanged.[73] The enforceability of the vote for remuneration implementation reports is still an issue in the UK and the achievement of ‘public-good’ is somewhat within reach if the harmful impact of that issue is unaccounted.[74] In all cases, the concern stands in the US as the weight of the policy vote has remained advisory since its implementation and is not supplemented with a binding

[66] Gordon (n 64), 328.
[67] Ben Ashwell, 'Support for Say-on-Pay Votes Continues to Erode in US, Warn Compensation Advisers' (*Governance Intelligence*, 21 May 2021) <https://www.governance-intelligence.com/shareholders-actisism/support-say-pay-votes-continues-erode-us-warn-compensation-advisers> accessed 21 December 2023.
[68] Mason (n 3), 284.
[69] Bebchuck and Fried (n 16), 74.
[70] Katarzyna Chalaczkiewicz-ladna, 'Failed reform of say on pay in the UK? The future of shareholder engagement with executive pay' [2019] 40(2) Company Lawyer 47-53, 48.
[71] Kate Burgess, 'Debt misaligns Reckitt’s risk profile and shareholder returns' (*Financial Times*, 13 February 2017) <https://www.ft.com/content/61ba823e-f1d5-11e6-8758-6876151821a6> accessed 21 December 2023.
[72] Andrew Ward, 'Shareholders back BP move to cut chief’s pay' (*Financial Times*, 17 May 2017) <https://www.ft.com/content/c0924a70-3b0f-11e7-821a-6027b8a20f23> accessed 21 December 2023.
[73] Judith Evans and Kate Burgess, 'Housebuilder Crest Nicholson loses vote on pay' (*Financial Times*, 23 March 2017) <https://www.ft.com/content/5f8a7042-0fe3-11e7-b030-768954394623> accessed 21 December 2023.
[74] Mason et al (n 3), 284.

vote on remuneration policy.[75] Despite some of these retrospective successes, the degree of meaningfulness of the dual vote say-on-pay in the UK in reducing excessive remuneration and achieving a sense of public-good is debatable given that the average CEO pay is 118 times that of the average UK worker whilst the latter is 'grappling' amidst the cost-of-living crisis in spite the increase of wages of most workers.[76]

D. THE SHORTCOMINGS AND POTENTIAL IRRELEVANCE OF SAY-ON-PAY

Bainbridge unwaveringly contended that the framework of 'say-on-pay' continues to be equivalent to that of a 'toothless tiger'.[77] His argument is sustained by the observable pattern of shareholders 'rubber-stamping' CEO pay, which is conveyed in the Sembler Brossy report on say-on-pay votes in 2021 in Russell 3000 companies which indicated a rise in the rate of majority dissatisfied shareholders from 1.9% to 3.3%.[78] Even though shareholder votes on remuneration reports are found to be the most capable of attracting dissents than other resolutions, it remains unguaranteed that shareholders' voices will be taken into account and that the remuneration report will be improved as say-on-pay does not have 'real teeth'.[79]

In a much broader context, it is arguable that the say-on-pay frameworks in the US and the UK aim to solve a matter that cannot be considered as problematic.[80] The exponential growth of executive compensation is unquestionable; however, it has remained open to question time and time again whether this should be a cause for concern.[81] This is especially the case when considering that other occupations generate pay as generous as executives', if not more, such that being actors, footballers,

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[75] The Dodd-Frank Wall Street Reform and Environmental Protection Act 2010; The Securities Exchange Act 1934, s.14A.

[76] Jamie Nimmo, 'Pay Gap Widens Between CEOs and Employees at Top UK Firms' (*BNN Bloomberg*, 18 December 2023) <https://www.bnnbloomberg.ca/pay-gap-widens-between-ceos-and-employees-at-top-uk-firms-1.2012987#:~:text=The%20CEOs%20of%20companies%20included,cost%2Dof%2Dliving%20crisis.> ac e sed 21 December 2023; ICAEW insights, 'Executive pay rises amid cost-of-living crisis' (Institute of Chartered Accountants in England and Wales ('ICAEW'), 31 August 2023) <https://www.icaew.com/insights/viewpoints-on-the-news/2023/aug-2023/executive-pay-rises-amid-costofliving-crisis> accessed 21 December 2023.

[77] Stephen Bainbridge, 'Say on Pay Remains a Toothless Tiger: So What's the Point?' (*ProfessorBainbridge.com*, 04 June 2021) <https://www.professorbainbridge.com/professorbainbridgecom/2021/06/say-on-pay-remains-a-toothless-tiger-so-whats-the-point.html> accessed 21 December 2023.

[78] Ibid; Semler Brossy, '2021 Say on Pay Reports 2021 Russell 3000 Average Vote Stays Consistent with Prior Years Despite an Uptick in Failures' (*Semler Brossy*, 27 January 2022) <https://semlerbrossy.com/insights/2021-say-on-pay-report/#:~:text=2021%20Say%20on%20Pay%20Reports%202021%20Russell%203000%20Average%20Vote,Despite%20an%20Uptick%20in%20Failures&text=Our%20year%2Dend%20report%20recaps,uptick%20in%20failures%20(63).> accessed 23 December 2023.

[79] Bainbridge (n 77); Chalaczkiewicz-ladna (n 70), 50; Gerner-Beuerle and Kirchmaier (n 28), 7.

[80] Bainbridge (n 8), 42.

[81] Ibid, 44

investment bankers to name a few. [82] This renders the framework as a ‘lukewarm’ attempt to ‘fix’ something that is not ‘broken’.[83] Then again, this would overlook the fact the executives have the freedom to set their own pay and do not bargain at arms-length in the manner that other employees do.[84] Alternatively, the degree of academic anticipation towards the failure of the say-on-pay framework in reducing excessive executive remuneration could perhaps convey that, despites its intended purpose to do so in design, it cannot resolve all issues within that context.[85] It is instead an ‘important step’ toward enhancing ‘boardroom practices’, which is one of the many external factors affecting executive pay.[86]

One of the many other rationales reiterating Bainbridge’s view is the low frequency of shareholder dissent to high executive compensation policies. The effective application of say-on-pay rests on the consensus that shareholders do not have their own ‘individual investment horizon’ or aggregately diversified portfolios to rely on.[87] This is clearly not the case as the size of each investor’s holdings vary.[88] While rational shareholders are expected to intervene by making a well-informed decision regarding executive remuneration if the benefits outweigh the costs, this remains as a rather rare occurrence because they hold diversified stocks and ultimately just care about the firm’s overall performance.[89] However, studies have found that institutional investors and mutual funds are more likely to vote against ‘abnormally’ high executive pay if they hold a lower fraction shares within their portfolios, meanwhile another study finds that short-term institutional investors are more likely to abstain as a way to avoid monitoring costs .[90] Regardless, it is important to note that investors’ behavior tends to ‘deviate from economic rationality’, whilst some retail investors might prefer to exercise rational apathy.[91] This inconclusiveness significantly impacts voting patterns,[92] which reduces say-on-pay’s ability to reduce overall excessive executive remuneration.

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[82] Ibid, 42
[83] Petrin (n 9), 204.
[84] Bainbridge (n 8), 42-43.
[85] David F. Larcker, Brian Tayan, et al, ‘Ten Myths of ‘Say on Pay’’ (2012) Stanford Closer Look Series: Topics, Issues and Controversies in Corporate Governance (No. CGRP-26), 2 <https://ssrn.com/abstract=2094704> accessed 23 December 2023.
[86] Keith L Johnson and Daniel Summerfield, ‘Shareholder Say on Pay – Ten Points of Confusion’ (2008) Harvard Law School Forum on Corporate Governance, 2 <https://corpgov.law.harvard.edu/wp-content/uploads/2008/11/say-on-pay-ten-points.pdf> accessed 23 December 2023.
[87] Mason et al (n 3), 310.
[88] Ibid.
[89] Ibid, 307-308.
[90] Ibid, 299; Miriam Schwartz-Ziv and Russ Wermers, ‘Do Institutional Investors Monitor their Large-Scale vs. Small-Scale Investments Differently? Evidence from the Say-On-Pay Vote’ (2022) European Corporate Governance Institute (ECGI) - Finance Working Paper No. 541/2017, 35 <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3096745> accessed 23 December 2023; Konstantinos Stathopoulos and Georgios Voulgaris, 'The Impact of Investor Horizon on Say-on-Pay Voting' [2016] 27(4) British Journal of Management 796-818, 798.
[91] Ibid, 308; David A Hoffman, 'The "Duty" to be a Rational Shareholder' [2006] 90(1) Minnesota Law Review 537-611, 543.
[92] Mason et al (n 3), 299.

On the other hand, based on the premise of director primacy, the matter of executive remuneration should not be subjected to much shareholder interference.[93] The exercise of effective board accountability by shareholders is hindered by information asymmetry and report complexity, which could lead to confusion about the criteria used in pay reports or possessing insufficient information of comparative groups' income from consultants.[94] Such asymmetry may take place when shareholders carry the onus of higher monitoring costs than of residual losses resulting from suboptimal monitoring.[95] Within the scope of that issue, it has been contended that the lack of accessible readability of remuneration reports in the UK are used as a ploy to 'bamboozle' shareholders into assenting for high pay based on the finding that '17 years of education - or a post graduate qualification' are essential to comprehensively decipher and vote on the report.[96] On the other hand, the use of 'plain English' rule may have significant impact on the length of the report, which also hinders its readability.[97] Furthermore, shareholders may base their decisions on their own short-term goals, which can be harmful to other stakeholders in the firm, or they may depend on proxy vote advisors.[98] The latter raises new issues of accountability related to conflicts of interests as such advisors tend to want to please directors.[99] Inevitably, shareholders will recognize the high cost of obtaining adequate information required to effectively interfere in corporate management and will therefore abstain from doing so.[100] It is clear that majority of shareholders prefer not to 'second-guess' the board, given that no 'shareholder revolt' has taken place.[101] The current utilization of say-on-pay, or lack thereof, reaffirms that an inherent sense director-primacy norm prevails to some degree, which hinders the meaningfulness of say-on-pay in reducing excessive executive remuneration.

The root of the concerns against say-on-pay is applicable to the UK and US as it lies with the 'inhibit[ion]' of the boards and executive management's ability to model the optimal remuneration package that maximizes the welfare of the contracting parties.[102] Exemplifying this are companies willing to offer high pay to 'attract, motivate and retain' their directors in response to the internationalization of the labor market.[103] Considering the 'deep' pool of talent that the US has, directors with US board past experience are on

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[93] Jingchen Zhao and Zhihui Li, 'The Regulatory Framework of Executive Remuneration: Contributions from Shareholder Activism and Board Accountability' [2019] 15(2) Hastings Business Law Journal 203-252, 224.
[94] Charlotte Villiers, 'Executive Pay: Beyond Control' [1995] 15(2) Legal Studies 260-282, 264.
[95] Walker (n 42), 671.
[96] Tamara Heath, 'Companies bamboozling shareholders into voting for big pay rises for executives' (*The University of Melbourne - Newsroom*, 4 May 2023) <https://fbe.unimelb.edu.au/newsroom/companies-bamboozling-shareholders-into-voting-for-big-pay-rises-for-executives> accessed 1 January 2024.
[97] Reggy Hooghiemstra, Yu Flora Kuang and Bo Qin, 'Does obfuscating excessive CEO pay work? The influence of remuneration report readability on say-on-pay votes' [2017] 47(6) Accounting and Business Research 695–729, 696.
[98] Petrin (n 9), 197.
[99] Ibid, 203.
[100] Bainbridge (n 8), 47.
[101] Mason et al (n 3), 310.
[102] Hemphill and Lillevik (n 1); Claudine Mangen and MIchel Mangan, '"Say on Pay": A Wolf in Sheep's Clothing?' [2012] 26(2) Academy of Management Perspectives 86-104, 87.
[103] Ernestine Ndzi, 'UK Shareholder Voting on Directors' Remuneration: Has Binding Vote Made Any Difference?' [2017] 38(5) Company Lawyer 139-149, 148.

somewhat of a pedestal, as they tend to receive higher compensation than those that do not globally.[104] Even though high pay was perceived as 'demoralizing' by some, a recent study finds that there is a 'general employee insensitivity' towards CEO pay and that negative effects are conditional upon high media coverage of the remuneration and over-compensation specifically in the financial sector.[105] The case for reducing executive remuneration by the implementation of report remuneration say-on-pay is rather weak when a UK-based company wants to either compete with US-based companies or even attract a director with US-board experience.[106]

Beyond that, the concern of the federal legislation of say-on-pay in the US is that it reinforces the federalization of corporate law, which has an adversarial impact on the operation of the capital market in the US.[107] This simplistic 'one-size-fits all' model of governance constrains states from utilizing the 'valuable opportunity' of trying 'novel social and economic experiments' without risking other states, which could potentially produce an efficient corporate law rule addressing the issue of excessive executive remuneration.[108] Though, relying on individual states to provide this efficient corporate law rule is highly optimistic, and runs on the risk that a state might abstain from providing any kind of oversight, because directors are viewed as 'platonic guardians' of a corporation.[109] Alternatively, there is no guarantee that this hypothetical rule will have any meaningful impact on reducing excessive executive remuneration.

E. ARE THE CURRENT SAY-ON-PAY FRAMEWORKS THE END ALL BE ALL SOLUTION FOR EXCESSIVE REMUNERATION?

In spite of the many shortcomings of the dual vote say-on-pay that were addressed, claiming that its potential is 'superfluous' would be very misguiding.[110] Rather, its current application is unsatisfactory and the meaningfulness of say-on-pay as a legal tool to reduce excessive remuneration can be enhanced by strengthening it. In conjunction with the vote, it is highly recommended to enforce employee engagement in pay-related decisions through employee representatives, as an extension of Regulation 13 of the Companies (Miscellaneous Reporting) Regulations 2018 with a clearer scope. This is

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[104] Randall Thomas and Brian R Cheffins, 'The Globalization (Americanization?) of Executive Pay ' [2004] 1(2) Berkley Business Law Journal 233-290, 256.
[105] Jospeh J Gerakos, Joseph D Piotroski and Suraj Srinivasan, 'Do US Market Interactions Affect CEO Pay?: Evidence from UK Companies' (2011) Harvard Business School Working Paper 11-075, 11 <https://www.hbs.edu/ris/Publication%20Files/11-075_0646e2d8-cbc6-49af-a694-0149594ce1e1.pdf> accessed 25 December 2023.
[106] Ibid, 31.
[107] Stathopolous and Voulgaris (n 6), 363, Bainbridge (n 8), 45.
[108] H Kent Baker and Rob Weigand, 'Corporate Dividend Policy Revisited ' [2015] 41(2) Managerial Finance 126-144, 139; Bainbridge (n 8), 46; *New State Ice Co. v. Liebmann*, 285 U.S. 262 (1932), 285.
[109] Stephen Bainbridge, 'Director Primacy in Corporate Takeovers: Preliminary Reflections' [2002] 55(1) Stanford Law Review 791-818, 791.
[110] Christoph Van der elst, 'A Plea for a Better Response to a Failed Say on Pay Vote' (*The CLS Sky Blue Blog*, 26 August 2016) <https://clsbluesky.law.columbia.edu/2016/08/26/a-plea-for-a-better-response-to-a-failed-say-on-pay-vote/> accessed 25 December 2023.

advantageous because employee representatives are strongly argued to have incentives to prevent expropriations and manipulations in earnings, hold very firm-specific knowledge and have a long-term interest in the company, as opposed to retail and short-term institutional investors.[111] Based on the rational choice theory, the behavior of other employees in the company is 'completely determined' by incentives, including an overall sense of fairness and risk aversion, which can be manifested with the implementation of this suggestion.[112] However, based on behavioral economics, people tend to make decisions in methods that 'systematically departs' from what has been predicted by the rational choice theory.[113] In that light, the enactment of a compulsory requirement of that nature is easier said than done, as it was previously considered by the Government in the UK and was dismissed from the 2016 published reports.[114] Because the business community strongly rejected this proposal and the distortion it may cause to the unitary-board system, a non-compulsory form of employee board representatives was introduced in 2018.[115] While the enforcement of employee involvement in the executive pay-setting process could be transformative in employee-management engagement and reducing excessive executive remuneration as the empirical evidence from the German jurisdiction demonstrates,[116] it can be predicted that it will not be well-received by the business communities in the UK and the US. This prediction is based on the past reception in the UK and the complexities associated with the call for federal legislation for employee-board representatives in the US which would entangle corporate state law with federal labor law.[117]

Encouraging the increase of the percentage value of the long-term incentive plans ('LTIPs') from the overall compensation package, by setting a specific cap on the number of shares that can be issued under LTIPs, could enhance the impact or say-on-pay. While LTIPs have been rising in popularity amongst companies, as most are using three to four different schemes to renumerate their top executives,[118] the enforcement of such a specific percentage value and cap on shares would prompt performance-based payments on a wider scale. Moreover, this restriction on LTIPs can limit the nullification of the shares through unloading and hedging transactions in order to reduce risk-bearing costs,

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[111] Conny Overland and Niuosha Samani, 'The Sheep Watching the Shepherd: Employee Representation on the Board and Earnings Quality' [2021] 31(5) European Accounting Review 1299-1336, 1299.
[112] Stephen M Bainbridge, 'Law and Economics' in Stephen M Bainbridge (ed*), Corporation Law and Economics* (New York Foundation Press 2002) 18-38, 23.
[113] Ibid, 25.
[114] Tobore O Okah-Avae, 'Recent Developments in Executive Pay Legislation: How Effective Have These Been in Making Executive Pay Fairer? ' [2019] 30(6) International Company and Commercial Law Review 327-339, 334.
[115]Financial Reporting Council (FRC), UK Corporate Governance Code 2018 (FRC, July 2018), 5 <https://www.frc.org.uk/library/standards-codes-policy/corporate-governance/uk-corporate-governance-code/#:~:text=UK%20Corporate%20Governance%20Code%202018%20(Current%20edition),-Current%20edition&text=The%20Code%20is%20separated%20into,'comply%20or%20explain'%20basis > accessed 25 December 2023.
[116] Felix Hörisch, 'The Macro-Economic Effect of Co-determination on Income Equality' (2012) Working Paper 147/2012 <https://www.mzes.uni-mannheim.de/publications/wp/wp-147.pdf> accessed 25 December 2023.
[117] Lenore Palladino, 'Economic Democracy at Work: Why (and How) Workers Should be Represented on US Corporate Boards' [2021] 1(3) Journal of Law and Political Economy 373-396, 375.
[118] Martin and Thomas (n 49), 1030.

essentially offsetting any possible gains or losses.[119] Specifically with the introduction of environmental, social and governmental ('ESG') metrics, management will be highly incentivized to 'deliver change' given the tensions between maximizing profits and the changes required to mitigate ESG matters.[120] Furthermore, environmental and sustainable metrics are pragmatically long-term in nature and will encourage long-term strategic focus.[121] Even though LTIPs, used in conjunction with say-on-pay, has the potential to decrease the excessive levels of executives' remuneration, the concerns discussed in section III regarding pay-for-performance still stand. Perhaps, the most effective way to enhance the ability of say-on-pay to reduce excessive executive remuneration is to set pay caps.[122] Because of its restrictive nature and conflict with the foundation of the free market that the UK and the US operate in,[123] it is unsurprising to predict that this suggestion will not be very welcomed nor enforced in the foreseeable future.

Given that the policy vote is non-binding in the US, some American scholars agree that a possible way for shareholders of US-based companies to demonstrate their dissatisfaction would be to 'vote with their feet' through selling all or part of their shares.[124] This is more of a quick-fix band-aid solution for shareholders themselves due to the lack of teeth in their votes, resultantly this will not prompt a reduction of executive pay or any meaningful impact on distributive justice as they can be easily replaced by other investors. Meanwhile, strengthening shareholder education on the impact of their utilization of the advisory say-on-pay on the way that they hold their board accountable, as well as the company's performance, has some degree of potential to create a governance-related changes to the current pay practices. The success of this and its ability to create value would largely depend on the board responsiveness – which cannot be guaranteed – and whether the vote has a binding impact.[125]

F. CONCLUSION

The dilemma posed by the current pay practices reflects the broader issues reflecting the toxicity in the free-market capitalist system.[126] Theoretically, a say-on-remuneration report has the potential to play some part, however miniscule, in reducing exorbitantly

[119] Nitzan Shelon, 'Replacing Executive Equity Compensation: The Case for Cash for Long-Term Performance' [2018] Delaware Journal for Corporate Law (Forthcoming) 1-40, 8
[120] PwC, 'Brining ESG into Executive Pay' (*PwC*, 2020), 2 <https://www.pwc.co.uk/human-resource-services/pdf/bringing-esg-into-executive-pay-v3.pdf> accessed 28 December 2023
[121] Ibid, 4.
[122] Okah-Avae (n 114), 336.
[123] Ibid.
[124] Stathopoulos and Voulgaris (n 6), 360.
[125] Jie Cai and RalphA Walking, 'Shareholders' Say on Pay: Does It Create Value?' [2011] 46(2) The Journal of Financial and Quantitative Analysis 299-339, 325.
[126] Villiers (n 26), 153; High Pay Commission, Cheques With Balances: why tackling high pay is in the national interest (High Pay Center, 2021), 68 < https://highpaycentre.org/wp-content/uploads/2020/10/Cheques_with_Balanceswhy_tackling_high_pay_is_in_the_national_interest.pdf > accessed 25 December 2023.

high executive pay. However, the success of that would be not only be contingent upon the overly optimistic creation of a holistic change in shareholder behavior and attitude, but also in changing its nature to binding. The grant of advisory power by the US framework is more limited, given that both policy and remuneration report votes are advisory, and is arguably implemented as a political response to 'popular outrage'.[127] While several suggestions were made to enhance the say-on-pay framework, the preservation of the existing model in the UK and US, as Villiers reiterates bearing in mind the current business climate, is likely to cause disappointment.[128] Having examined the extent to which say-on-pay on remuneration reports is meaningful in reducing excessive executive pay, it is evident that the attitude and degree of rationality of shareholders towards using their own voice have both played a significant role in the ineffective use of the vote. Needless to say, the issues surrounding say-on-pay are so much more deep-seated, to the point where the interests of managers and shareholders and more often than not, unaligned. It remains of the utmost significance that the appropriate steps are undertaken to eliminate the weaknesses of the current say-on-pay model in order to reduce high executive payments and to foster a sense of distributive justice.

[127] Hemphill and Lillevik (n 1), 114.
[128] Villiers (n 26), 154.