DREXEL UNIVERSITY
Center for
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LEGISLATION TO ADDRESS EXTREME PAY DISPARITY

As CEO compensation packages continue to grow, especially in companies employing large numbers of low-wage workers, employee compensation has remained flat. As a result, large numbers of workers are forced to depend on public assistance due to low wages, creating major financial burden on state and federal governments. Such extreme inequality also creates poor health outcomes, causes social unrest, and reduces business productivity. Efforts must be made to prevent such harms and save public money from being plundered by corporations who push workers into financial insecurity where they must resort to utilizing public benefits to meet basic needs.

Background

The majority of America's lowest-paid workers (66 percent) are employed by large corporations with more than 100 employees, often in retail and food service sectors.

Of the top 50 employers of low-wage workers in 2012, the average executive received $9.4 million in compensation. The top 350 U.S. company CEO's were paid an average of $24.2 million in 2020, with benefits and stock options.[1] From 1978 to 2019, typical worker's compensation grew just 18 percent, while CEO compensation grew by 1,322 percent during the same period.[2] The average CEO-to-worker pay ratio for publicly traded companies in 2020 was 299-to-one.[3] At 58 companies, the CEO-worker pay gap was more than 1,000-to-one.[4] Despite increased productivity and profits, more than 6.3 million working adults and their families live in poverty (with millions more just barely above the poverty line) and are more likely to experience food insecurity, depression, and poor health outcomes.[5,6,7]

Over the past five years, lawmakers across the U.S. have begun to address these challenges and restore lost revenue through enacting fines and taxes on businesses with large disparities between highest and lowest paid employees.

Policy Recommendation

Tax code legislation should be implemented at the local, state, and/or federal level that fines companies for keeping worker wages low while continuing to increase top level employee compensation to extreme levels.

CEO Pay Ratio Tax: an excise tax on companies that pay CEOs or other employees significantly more than the average worker. Examples include the following:

Passed Legislation

- **Pay Ratio Surtax (ARB-LIC-5.02, 2017)** – Administrative rule adopted in Portland, Oregon, requires that publicly traded companies located in the city that are subject to the Business License Tax must pay a surtax if their CEO-to-median worker compensation ratio is equal to or above 100-to-one. If the ratio is equal to or above 100-to-one but less than 250-to-one, the surtax is ten percent. If the ratio is equal to or above 250-to-one the surtax is 25 percent. Portland collects $3.5 million each year from the tax, these funds are added to the city's general fund. No evidence has been presented that the tax drove any businesses out of the city.[8]

- **Disproportionate CEO Pay Tax (Proposition L, 2020)** – With 65 percent vote in favor, San Francisco voters approved a measure to impose a gross receipts tax or payroll tax on businesses with high pay disparity, depending on the type tax a business currently pays. Rates are graduated on ratios from 100-to-one (0.4 percent) to more than 600-to-one (2.4 percent). Unlike Portland, San Francisco will impose this tax on both public and privately held companies and collect pay data directly from them, not the federal government. The tax will take effect in 2022 is expected to bring in $60 to 140 million annually.

- **Payroll Expense Tax (CB.119810, 2020)** – While not specifically targeting payroll disparities, Seattle City Council passed an ordinance to address large companies doing business in the city with large payrolls (including CEO pay). It establishes a tiered system of taxation on companies with annual payroll expenses exceeding $7 million. Stock grants are included in the salary calculations, but stock options are not. The tax will initially fund coronavirus relief and eventually go toward affordable housing and homeless services.

Proposed State/Local Legislation

- **Pay Disparity Surcharge (SB.747, 2021)** – This 2021 bill proposes to impose a pay disparity general excise tax surcharge in the amount of 0.1 percent of the company's tax liability on any company conducting business in Hawaii whose top executive earns at least one hundred times more than the median income of company employees.

- **Act Establishing a Tax on Excessive Executive Compensation (HB.3083 / SB.1907, 2021)** – This 2021 proposal would require every corporation with a net income of $10,000,000 or more doing business in Massachusetts to be charged a tax in addition to their base corporate tax rate based on compensation ratio. Rates range from an additional zero percent for ratios below 50 to ten percent for those over 500.

- **Act Establishing a Pay Ratio on Corporation Income Tax on Publicly Traded Companies (HB.06373, 2017)** – This 2017 Connecticut bill proposed to replace the state corporate income tax on publicly traded corporations with a tax rate based on a pay ratio scale starting at five percent for a 25-to-one or less ratio up to 25 percent for pay ratio greater than 250-to-one.

- **Business Compensation Equity Fee Act (HB.3335, 2017)** – This act proposed an annual fee for each publicly traded company doing business in Illinois that reports a CEO-to-median employee pay ratio of at least 100-to-one, according to disclosures to the U.S. Securities and Exchange Commission. Fees were proposed at $1,500 for a pay ratio between 100-to-one and 250-to-one and $2,500 for greater than 250-to-one.

- Additional Proposals: California (SB.37, 2019), Minnesota (HF.65, 2017), New York (SB.1659, 2019), New York (A.07454, 2019), Rhode Island (HB.5141, 2017), Washington (HB.1681, 2019)

Proposed Federal Legislation

- **Tax Excessive CEO Pay Act (S.794 / HR.1979, 2021)** – This proposed amendment to federal IRS code would implement an excise tax on companies that pay CEOs 50 times more than median pay for workers by increasing taxes in amounts of 0.5 percent up to five percent for those making 500 times more than median workers. Privately held companies that make $100 million or more would also be included.

- **Equity in Compensation Act (S.2312, 2019)** – This proposal would apply surtaxes on corporate income tax liabilities, beginning with two percent on companies with pay ratios of 30-to-one and rising to ten percent on firms with ratios above 1,000-to-one.

Policy Considerations

The following should be considered in implementing new legislation to address disparities in worker compensation:

- Calculations should be based on lowest (not median/average) and highest paid worker data to truly address disparity
- Calculations of CEO compensation must include wages, benefits, and stock options
- Policies must apply to both public and private companies (including both non-profit and for-profit where pay inequity exists) in order to have a substantial impact
- Policies must use language that specify highest compensated managerial position to be used for calculations, as CEO or president may not be the highest paid in some organizations (for example, a college football head coach may be paid higher than the college president)
- Additional disincentives must be included for companies who reduce low-wage jobs without reduction in CEO and top-level compensation
- **Funds raised should be designated specifically for use in programs that address inequity by developing assets for low-wage workers** such as:
  - Direct cash assistance to low-wage workers ineligible for TANF or other benefits (those impacted by the "benefits cliff")
  - Increase in TANF cash allotment amounts
  - Low-income homebuyer programs
  - Matched savings accounts for low-income adults and children
  - Education grants for low-income adults and children
- **Without additional efforts to raise minimum wage and address issues of worker benefits and discrimination, tax disincentives alone will not be enough to address nationwide pay inequity**

Additional Resource

CEO-Worker Pay Resource Guide - https://inequality.org/action/corporate-pay-equity/

References

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