



Identifying a Compensation Comparator Group for Executive & Investment Management Staff

April 17, 2013

DISCUSSION DOCUMENT

Discussion Road Map: Where Are We Going?

- CalPERS wants to complete a market pay level analysis, an initiative that:
 - Is called for under CalPERS' written Compensation Policy and Procedures Manual.
 - Reflects good governance, business, HR, and risk management practices.
- To complete a pay level analysis, CalPERS' compensation comparator group needs to be identified.
- The Compensation Policy and Procedures Manual identifies a comparator group, *but*....
 1. The Policy's language is vague. More specificity is needed about the types of organizations to include (e.g., what types of "banks and insurance companies" and which countries for "non-US public funds").
 2. The Policy's peer group is likely outdated/ill-suited to CalPERS.
 3. The Policy is incomplete. It specifies a peer group for setting base salary. Nothing is stated about the standards for defining incentive or total pay levels.
- This report is intended to serve as a basis for discussion with the Performance, Compensation and Talent Management Committee. That is, this document:
 - Outlines several peer group alternatives for the Committee's evaluation/consideration.
 - Informs the Committee about the pros & cons of each peer group.
- Subsequent reports will cover:
 - CalPERS' relative pay competitiveness versus the various peer groups. These analyses will contain market data which will assist the Committee in achieving consensus regarding the optimal pay group and setting target pay within the selected peer group.
 - Implementation steps, as required.

Why Should CalPERS Complete a Market Pay Analysis?

- There are four key reasons for completing a competitive pay level analysis:
 1. To follow practices specified in CalPERS' Compensation Policy Manual:

Determination of base salary ranges will be based upon one or more of the following:

- Consideration of internal equity factors
- Relevant marketplace salary survey data gathered every two years
- A review of relevant data when a position becomes vacant
- Data gathered when the Performance, Compensation and Talent Management Committee (PCTMC) determines a special survey is necessary, or
- Consideration of industry standards and best practices relative to executive compensation

CalPERS has not completed a comprehensive salary survey since 2008.

2. To allow the Board to exercise sound pay governance practices.
 - To fulfill their oversight and fiduciary responsibilities, CalPERS' Board-members need to know "where the organization stands" relative to the competitive market.
3. To reaffirm CalPERS' human capital strategies in the context of potential changes in:
 - CalPERS' Board and/or individual Board-member's perspectives about pay.
 - CalPERS' investment and/or operating approaches.
 - The political and economic environment.

Why Should CalPERS Complete a Market Pay Analysis? . . .

4. To monitor and manage employee-related recruiting and/or retention risk.
 - The Board should actively monitor employee-related retention and recruiting risk in the same way that it monitors investment and other types of System-related risks.
 - While market pay levels have zigged and zagged with volatile markets, demand for top investment talent remains intense, particularly from private sector institutional managers who often view public funds as easy “picking grounds” for top talent.*

Public Fund CIOs Leaving for/Recruited By the Private Sector			
Year	Incumbent	From	To
2012	Stan Mavromates	Massachusetts PRIM	Mercer
2012	Ken Lambert	Nevada PERS	Peavine Capital
2012	Shawn Wischmeier	North Carolina Retirement Systems	Margaret A. Cargill Philanthropies
2012	Kenneth Goodreau	Rhode Island Retirement System	TIG Advisors
2011	M. Timothy Corbett	CT Retirement Plans and Trust Funds	Mass Mutual
2011	Raudline Etienne	NYS Common Retirement Fund	Albright Stonebridge Group
2011	Lisa Needle	San Diego County ER Association	Albourne America
2011	Robert Bordon	South Carolina Retirement System	FTA Partners
2011	Trent May	Wyoming Retirement System	Koch Industries/Koch Foundation
2010	Doug Wynkoop	Houston MERS	University of Florida Investment Corp.
2010	Adam Tosh	Kentucky Retirement Systems	Rogerscasey
2010	Mansco Perry	Maryland SRA	Macalester College
2010	Tim Barrett	San Bernardino County ER Association	Eastman Kodak
2009	Lee Partridge	San Diego County ER Association	Salient Partners, L.P.
2007	Peter Gilbert	Pennsylvania SERS	Lehigh University

* Appendix 4 shows P&I research about pay for CIOs in 50 non-profit organizations. Only two public fund CIOs ranked in this 50 highest-paid list. CalPERS’ CIO was paid less than all 50 of these CIOs.

CalPERS' Compensation Policy Manual Needs Clarification

- CalPERS' Compensation Policy Manual does not adequately specify the peers, process and methodology that should be used to set executive and investment professional pay.
 1. The peers are vaguely defined ...
 2. Many of the possible peers are not especially relevant for CalPERS.

<i>Determining Base Pay Ranges</i>	<p>Base salary ranges are established by using a blend of global private and public sector data as follows:</p> <ul style="list-style-type: none"> • Data is weighted 50% on the median of large financial services (banking and insurance) private sector, and 50% on the 75th percentile of large global (U.S. and non-U.S.) public sector (greater than \$75 billion in assets)
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Banks and Insurance Companies?

- Why? Do they have missions similar to CalPERS?
- For banks and insurance companies: what does "large" mean? \$1 billion? \$50 billion? \$200 billion? Further, retail-focused? Institutionally focused?
- Do banks and insurance companies manage money like CalPERS?
- Are banks or insurance companies considered leaders in asset/pension management?

\$75B+ AUM Public Sector Funds?

- U.S. Public Funds: All large funds? A select group of leading funds?
- Non-U.S. funds: Canada only? What about the Middle-East, Europe or Asia?
- Are public funds really competitors for talent and/or sources of talent for CalPERS?

CalPERS' Compensation Policy Manual Needs Clarification . . .

3. The Policy specifies the process, but not the underlying peer group that should be used to set incentive levels. What market standard(s) does the Board want to focus on?

*Performance
Award
Ranges*

The Board, upon recommendation of the Performance, Compensation and Talent Management Committee, sets the performance award ranges for all covered positions. The performance award range represents the percentage of base pay available to be earned based on the level of achievement (threshold, target, or maximum) on the performance plan objectives.

Performance award ranges will be periodically reviewed by Performance, Compensation and Talent Management Committee and may vary by position (see Appendix 1). Any change to an established performance award range must be approved by the Board of Administration.

For CalPERS, Identifying a Pay Comparator Group is Difficult

- No other organization is exactly like CalPERS relative to size and operating complexity:
 - \$250 billion AUM with \$160 billion managed internally.
 - Pension administration for ~1,400 employers.
 - Health purchasing for over one million members.
 - Customer service for ~1.6 million members.
- CalPERS has operating characteristics/requirements that are comparable to several types of potential comparators:
 - Asset liability management/funding requirements like an insurance company, bank, or corporate pension plan sponsor.
 - Asset management activities like an institutional investment manager or fund of fund manager.
 - Customer service/operations requirements comparable to public pension funds and retail-focused financial services firms, such as DC plan administrators, insurance companies, etc.
 - Missions aligned with public pension plans, endowments/foundations, and corporate plan sponsors.
- Pay levels and pay practices vary widely across the range of potential comparators:
 - Total compensation levels vary widely by type of firm and for different roles within individual firms.
 - The types of pay vehicles offered vary (e.g., some competitors offer defined benefit (DB) plans *and* long-term incentives (LTIs); others just DB plans, but not LTIs; others LTIs but not DB plans).
- Apart from pay, CalPERS offers specific benefits that selected competitors do not:
 - Civil service protection that provides staff with employment security.
 - A DB pension plan (which is not offered by many private sector firms).
 - The prestige, access and learning opportunities associated with working at CalPERS.

For CalPERS, Identifying a Pay Comparator Group is Difficult . . .

- As CalPERS weighs various comparator group alternatives, we suggest that the Committee focus on the following types of organizations:
 - Organizations that are comparable to CalPERS from the perspective of: (1) mission; (2) activities/functions performed; and (3) skills/capabilities required.
 - Organizations that CalPERS competes with for talent – meaning CalPERS either recruits from or loses people to such organizations.
 - Organizations or a group of organizations that have the breadth of activities that will allow CalPERS to obtain market pay levels for most of its positions.
- Regardless of which peer group the Committee selects, the peer group's pay is likely to be higher than CalPERS' current pay, especially for senior investment and portfolio management/trading roles.
- As a result, the Committee will need to choose both: (1) the peer group and (2) where to target CalPERS' salary and cash compensation levels relative to that group.
- The following pages outline three peer group alternatives for the Committee's review.
- We expect that next steps will include analyzing market compensation levels across several alternative peer groups to inform the Committee's decisions.

Comparator Group Alternatives

#1: Retain & Clarify the Current Peer Group: 50% Public, 50% Private

Concept	<p>CalPERS' comparator group would be defined as:</p> <ul style="list-style-type: none"> ▪ A select group of leading U.S. and Canadian public funds (weighted 50%). ▪ A select group of large banks and insurance companies (weighted 50%). <p>Importantly, in contrast to the current approach:</p> <ol style="list-style-type: none"> 1. Public funds would be limited to the U.S. and Canada. A select group, rather than a pure \$75B AUM size-cut off, would be used. 2. A defined group of large banks and insurance companies would be used. The selection criteria for such firms (e.g., asset size, number of employees, complexity, investment operations) needs TBD. 3. These comparators would be used for salary <i>and</i> cash compensation benchmarking.
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Strengths	Weaknesses
<ul style="list-style-type: none"> ▪ CalPERS has been able to attract and retain staff with the current comparator group, but often faces limited candidate pools and long recruiting periods. ▪ CalPERS is a public fund and should benchmark its pay levels versus other public funds. The 50% weighting satisfies this objective. ▪ A 50% private sector weighting acknowledges that CalPERS competes with a broad range of firms for talent (not just public funds). ▪ This approach appears to conform with the current policy's possible intent, but includes critically needed clarifications. 	<ul style="list-style-type: none"> ▪ CalPERS is far larger and more complex than all other public funds. Are those funds relevant? ▪ CalPERS' top performers would not likely leave for another public fund. CalPERS mainly recruits from the private sector (not other public funds). ▪ Many banks and insurance companies do not have institutional money management organizations and, if they do, they are more narrowly focused than CalPERS (e.g., focused on fixed-income). ▪ It may be difficult/contentious to identify a bank and insurance company peer group.

#2: Continue 50% Public, 50% Private Blend BUT Modify the Private Sector Peers

Concept	<p>CalPERS' comparator group would be defined as:</p> <ul style="list-style-type: none"> ▪ A select group of leading U.S. and Canadian public funds (weighted 50%.) <i>This is identical to alternative #1.</i> ▪ A select group of large private sector organizations, including investment management firms, banks, and insurance companies (weighted 50%). <i>Compared with alternative #1, the private sector peer group is expanded to include investment management firms.</i> <p>These comparators would be used for salary <i>and</i> cash compensation benchmarking.</p>
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Strengths	Weaknesses
<ul style="list-style-type: none"> ▪ Continues the 50%; 50% approach, but with a more appropriate group of public funds and private sector firms. ▪ The private sector peer group would include investment management firms which: <ul style="list-style-type: none"> – Are the primary source and competitors for CalPERS' staff (see Appendix 3) – Manage a broader range of assets than banks and insurance companies (which often only focus on fixed income). – Have similar operations (e.g., compliance and support requirements of CalPERS). ▪ With a larger peer group, CalPERS could obtain survey data for more of its positions. 	<ul style="list-style-type: none"> ▪ CalPERS is far larger than “leading” public funds. ▪ CalPERS' top performers would not likely leave for another public fund. Why include public funds? ▪ Identifying a peer group of large private sector organizations could be difficult/contentious?

Comparator Group Alternatives

#3: Adopt a New Group Focused on Leading Institutional Investors

Concept	<ul style="list-style-type: none"> ▪ Adopt a new peer group that focuses on a cross-section of leading institutional investors, including top U.S. and Canadian public pension plans, endowments and foundations and corporate plan sponsors (see Appendix 1). ▪ Similar to options #1 and #2, this group contains both public and private sector firms. However, weightings are not assigned to the individual sectors. Rather, data for 22 firms would be compiled into one data set from which market data would be calculated.
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Strengths	Weaknesses
<ul style="list-style-type: none"> ▪ These comparators’ missions are similar to CalPERS’. ▪ These peers are leaders in pension/asset management. ▪ This peer group excludes banks and insurance companies whose executives often have different responsibilities and accountabilities. ▪ Compared with the current peer group, these firms are often more comparable to CalPERS. ▪ Given CalPERS’ size and scale, additional pay could be considered a “bargain” insurance policy to retain and attract top talent. For staff, pay would be taken “off the table.” 	<ul style="list-style-type: none"> ▪ Many of these peers (i.e., particularly the endowments and foundations): <ul style="list-style-type: none"> – Are much smaller than CalPERS. – Lack CalPERS’ operating complexity (e.g., \$250B AUM, of which \$160B (64%) is internally managed, <i>plus</i> pension and health plan administration for approximately 1.6 million members). – Do not manage money internally. ▪ CalPERS does not typically recruit from or lose people to endowments and foundations or corporate plan sponsors. ▪ Because many of the organizations are much smaller, CalPERS may not be able to obtain data for all of its positions. ▪ Selected weaknesses may be overcome with slight adjustments to this peer group (e.g., adding mid- sized money managers).

Next Steps

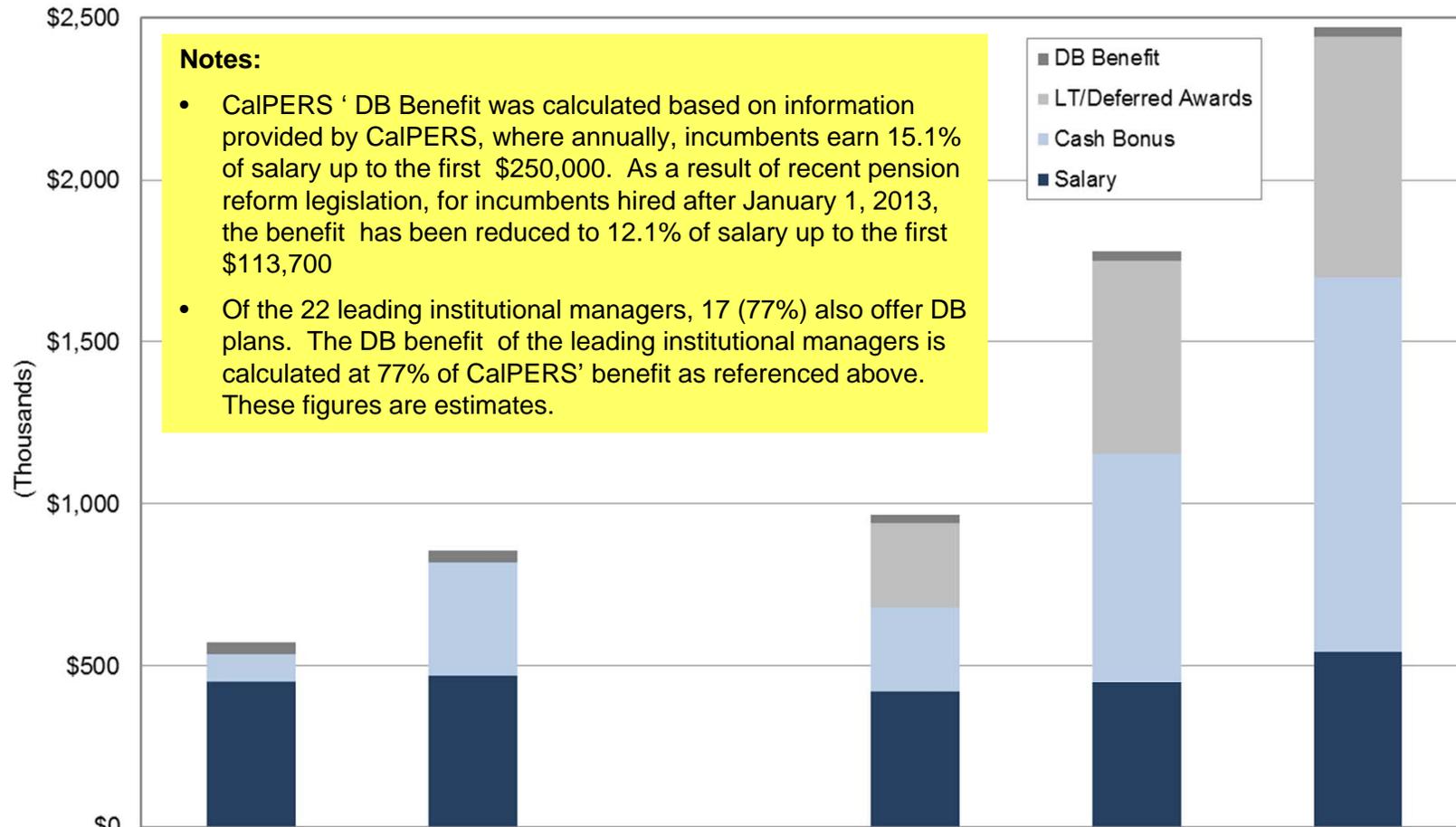
- McLagan will:
 - Complete a comprehensive, competitive pay level analysis, which will include market summary data for the three peer group alternatives. The analysis will detail how CalPERS' current salary and incentive structure compares to the alternative peer groups. McLagan will present this to the Committee in May, ultimately allowing the Committee to select a comparator group.
- Based on the peer group chosen by the Committee and using the results of an updated competitive pay level analysis, McLagan will, as required:
 - Develop recommendations related to updated salary ranges and incentive opportunities.
 - Develop a transition/implementation plan for the new pay structure.
 - Update the Compensation Policy Manual.

Leading Institutional Investors – A Possible Alternative Peer Group

Leading Institutional Managers (22)				
		12/31/11 AUM *	% Internally Managed	# of Inv Staff
Canadian Pension Plan Investment Board	Canadian Pension Fund	\$160.3		
Caisse de depot et Placement de Quebec	Canadian Pension Fund	157.3		
California State Teachers' Retirement System	US Public Fund	144.8		
General Motors Asset Management	US Corp. Plan Sponsor	127.0		
GE Asset Management	US Corp. Plan Sponsor	121.0		
Ontario Teachers Pension Plan Board	Canadian Pension Fund	115.9		
Teacher Retirement System of Texas	US Public Fund	101.6		
State of Wisconsin Investment Board	US Public Fund	77.2		
University of California Retirement System	Endowment & Foundation	68.7		
Division of Investment Services, State of Georgia	US Public Fund	64.6		
State Teachers Retirement System of Ohio	US Public Fund	61.7		
Ontario Municipal Employees Retirement System	Canadian Pension Fund	54.4		
Virginia Retirement System	US Public Fund	51.0		
Healthcare of Ontario Pension Plan	Canadian Pension Fund	39.9		
Harvard Management Company, Inc.	Endowment & Foundation	32.0		
Lockheed Martin Investment Management Company	US Corp. Plan Sponsor	28.0		
University of Texas Investment Management Company	Endowment & Foundation	25.7		
DuPont Capital Management	US Corp. Plan Sponsor	25.6		
Yale University Investments	Endowment & Foundation	20.0		
Stanford University	Endowment & Foundation	19.5		
Princeton University	Endowment & Foundation	15.8		
Columbia University	Endowment & Foundation	7.8		
	US Public Fund	6	27%	
	Canadian Pension Fund	5	23%	
	US Corp. Plan Sponsor	4	18%	
	Endowment & Foundation	7	32%	
		22	100%	
	High Quartile	\$112.3	55%	100
	Median	58.0	32%	68
	Low Quartile	26.3	13%	27
California Public Employees' Retirement System		\$225.0	64%	194
<i>CalPERS' Rank</i>		<i>1 of 23</i>	<i>5 of 19</i>	<i>5 of 23</i>

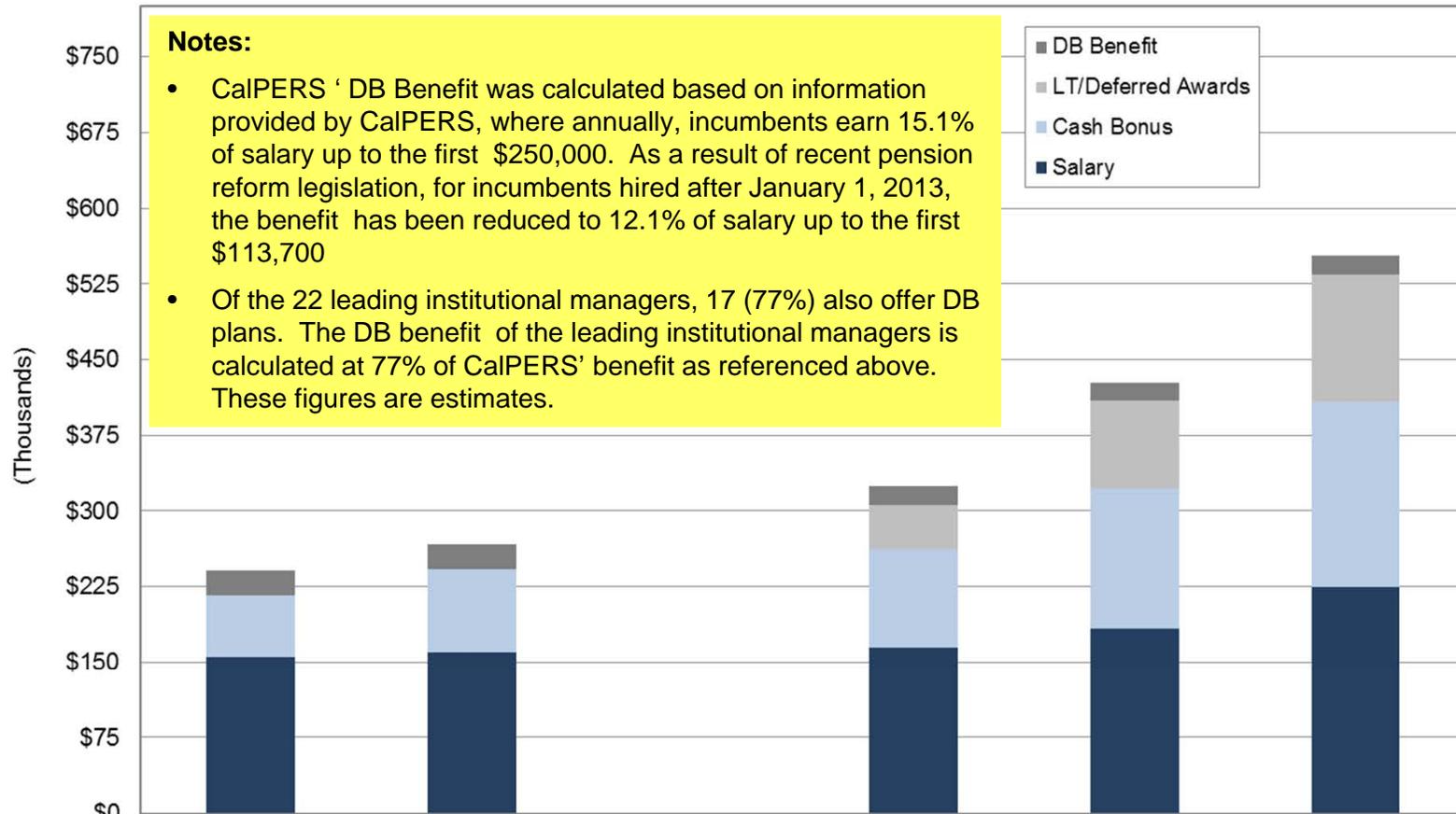
* Endowment & Foundation AUMs are as of 6/30/11

Competitive Pay Levels: Chief Investment Officer



	CalPERS		Leading Institutional Managers		
	2012 Actual	2013 Policy	LowQ	Median	HighQ
Salary	\$450	\$468	\$419	\$448	\$544
Total Cash	534	819	681	1,153	1,699
Total Comp	534	819	939	1,749	2,441
Total Comp + DB Benefit	572	857	968	1,778	2,470

Competitive Pay Levels: Portfolio Manager



	CalPERS*		Leading Institutional Managers		
	2012	2013			
	Actual	Policy	LowQ	Median	HighQ
Salary	\$156	\$159	\$164	\$183	\$225
Total Cash	217	242	262	322	408
Total Comp	217	242	306	409	534
Total Comp + DB Benefit	241	266	324	427	552

* Based on an average of 61 CalPERS' Portfolio Managers for which full compensation and market data is available.

CalPERS' Investment Office Talent

- INVO's largest source of staff is the asset management industry:
 - Of 65 investment staff hired in the last 3 years, 57% came from asset management or asset management related-financial firms.
 - 31% of new staff previously worked at asset managers. 26% of new staff came from other financial services firms, primarily investment banking, proprietary trading, research and asset servicing.
 - INVO also hired a number of staff (14%) from consulting and professional service firms.
 - Only 2 people joined CalPERS from other public pension funds, both of them from CalSTRS.

P&I's Top Paid Tax Exempt CIOs

<i>Pensions & Investments Top Paid Tax-Exempt CIOs</i>				
Rank	CIO	Organization	AUM (billions)	Total Compensation
1	Jane Mendillo	Harvard University (HMC)	\$27.60	\$4,754,379
2	David F. Swensen	Yale University	16.70	3,795,540
3	Nirmal Narvekar	Columbia University (CIMC)	6.50	3,447,953
4	Scott C. Malpass	University of Notre Dame	5.20	2,057,827
5	Laurance Hoagland	Hewlett Foundation	7.40	2,015,635
6	Mark Schmid	University of Chicago	5.60	1,790,730
7	Chris J. Brightman	University of Virginia (UVIMCO)	3.90	1,708,610
8	Denise Strack	Moore Foundation	5.20	1,671,347
9	William H. McLean	Northwestern University	5.90	1,594,019
10	Andrew Golden	Princeton University (PRINCO)	14.40	1,458,504
11	John Powers	Stanford University (SMC)	13.90	1,395,189
12	Susan E. Manske	MacArthur Foundation	6.00	1,353,124
13	Neal F. Triplett	Duke University (DUMAC)	5.70	1,253,819
14	John H. Moehling	Packard Foundation	6.40	1,196,037
15	D. Ellen Shuman	Carnegie Foundation	2.50	1,152,874
16	Bruce Zimmerman	University of Texas (UTIMCO)	14.10	1,127,186
17	Suzanne Brenner	Metropolitan Museum	3.00	1,120,956
18	Landis Zimmerman	Hughes Medical Institute	16.80	1,058,357
19	Joseph Boateng	Casey Family Programs	1.90	1,038,916
20	Scott Wise	Rice University (RMC)	3.80	1,038,536
21	James Williams	Getty Foundation	3.50	1,019,191
22	Cynthia E. Frost	Brown University	2.20	1,011,351
23	Thomas "Britt" Harris	Texas TRF [Pension]	100.70	1,001,512
24	Jonathan King	University of North Carolina (UNCMCo)	2.00	983,764
25	Kristin Gilbertson	University of Pennsylvania	5.70	961,059

P&I's Top Paid Tax Exempt CIOs...

<i>Pensions & Investments Top Paid Tax-Exempt CIOs</i>				
Rank	CIO	Organization	AUM (billions)	Total Compensation
26	Paul Lawler	Kellogg Foundation	\$6.70	\$925,565
27	Seth Alexander	MIT	9.90	888,495
28	Scott Pittman	Mt. Sinai Medical Center	1.10	873,511
29	Randy Kim	Hilton Foundation	1.90	852,881
30	Michael J. Smith	Mott Foundation	2.10	852,153
31	Mary Cahill	Emory University	4.70	851,982
32	Srinivas Pulavarti	University of Richmond	1.60	826,768
33	Kathryn J. Crecelius	Johns Hopkins University	2.20	825,947
34	Brian S. O'Neil	Johnson Foundation	10.10	808,800
35	Matthew Wright	Vanderbilt University	3.00	779,405
36	Robert J. Manilla	Kresge Foundation	3.10	774,816
37	Eric Doppstadt	Ford Foundation	10.70	768,126
38	Jeffrey Heil	Doris Duke Charitable Foundation	1.60	750,000
39	Kimberly G. Walker	Washington University (St. Louis)	4.50	710,836
40	Gloria D. Reeg	N.Y. Presbyterian Hospital	1.60	683,968
41	Bruce W. Madding	Henry J. Kaiser Foundation	0.60	651,815
42	Marie N. Berggren	University of California	5.40	637,823
43	David Clay	Grinnell College	1.30	628,243
44	Colette D. Chilton	Williams College	1.50	628,120
45	Jonathan Hook	Ohio State University (OSUniversity Foundation)	1.90	627,300
46	John E. Hull	Mellon Foundation	5.10	620,616
47	Deborah Kuenstner	Wellesley College	1.30	620,116
48	Charles W. Cary, Jr.	Georgia TRS [Pension]	45.90	609,440
49	Lisa Danzig	Rockefeller University	1.60	608,209
50	Donna J. Dean	Rockefeller Foundation	3.80	589,577
		High Quartile	\$6.65	\$1,239,374
		Median	4.60	943,312
		Low Quartile	2.03	754,532