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Memorandum

To: Michael Bilbrey, Board of Administration and Chair of the Performance, Compensation and Talent Management Committee ("PCTMC") of CalPERS

Date: June y, 2017

From: Eric Gonzaga / Grant Thornton LLP

Re: Proposed Salary Range Maximum Increases

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Dear Mr. Bilbrey,

Background

The Performance, Compensation and Talent Management Committee ("PCTMC") engaged Grant Thornton ("us", we", or "Firm") to assess proposed modifications to the existing salary ranges for Management covered under Government Code Section 20098.

Historically, the PCTMC requests a periodic total compensation survey, inclusive of a review of salary ranges. The last comprehensive review and update of the salary ranges occurred in 2015, completed by McLagan. In 2016, the PCTMC worked with Grant Thornton to update its total compensation philosophy, and implement a new annual incentive plan. The PCTMC also received recommendations on design of a long-term incentive plan, as well as an updated salary structure that reallocates the mix of pay amongst salary, annual incentives, and long-term incentives. The latter recommendations were not implemented, and will be discussed at a later time. At this point, the existing salary ranges are the same as revised in 2015.

At the request of the PCTMC, management recently conducted a review of existing salary ranges, utilizing the 2015 McLagan survey, a published pension fund survey, and 27 public sector agencies in California. As a result of this analysis, it is proposed that the PCTMC consider increasing salary range maximums by 4% to 5%, depending on the number of incumbents at the top of the range, or in the upper quartile of the range.

Analysis and Conclusions

Grant Thornton has reviewed the proposed changes and the supporting detail, and believes that these proposed modifications are reasonable and conservative. Our conclusions are based on the following:

- Existing salary ranges for CalPERS are currently at the 25th percentile of the previously reviewed salary data from the 2015 McLagan study, which include both industry and government agencies.
- In 2016 and 2017, we estimate that salaries have increased, on average, by 6% to 6.3% over 2015 salary levels. Our database indicates that these trends are similar nationally in financial services and in public agencies. Additionally, we note that these trends are comparable for the State of California, regardless of industry. We cite the World at Work 2016/2017 Salary Budget Survey in support of these trends, which collected salary increase trends from 5,077 organizations.

- Given the salary increase trends, the proposed salary range increases of 4% or 5% are still modestly below market movement of 6% to 6.3% that is typical nationally and for all organizations in California.
- Assuming the salary increases are implemented, total compensation will still lag industry peers significantly, particularly due to common long-term incentive plan practices and increases in variable compensation payouts over the last two years.

We believe that the proposed adjustments are well within market practice, and will allow for appropriate modest adjustments, while CalPERS contemplates implementation of a long-term incentive plan (strongly recommended by us), in addition to possible reallocation of pay between salary and variable compensation, per our 2016 study.

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We hope this information is helpful to you, and please feel free to reach out to us with any questions.

CAVEATS

This memorandum address certain U.S. Federal income tax issues only and does not address state, local or other foreign tax issues. Our discussion is based on the Internal Revenue Code of 1986, as amended, the Treasury Regulations promulgated thereunder, and other relevant authorities. These authorities are all subject to change, and such change could have retroactive effect. Any such changes could thus have effect on the validity of our conclusions. Unless specifically requested, we will not update this Memorandum for subsequent changes or modifications to these authorities. Further, this memorandum is based on interpretation of these authorities; another knowledgeable party (such as the IRS or court hearing the same facts) might reach different conclusions.

The advice expressed in the Memorandum is not an opinion as to the tax consequences of the transaction. We would need to perform a more thorough review and analysis before we could render an opinion. Our conclusions are limited to the issues addressed in this Memorandum, and are based on facts, assumptions, documents and representations we have received from you, and on any assumptions stated herein. We have neither independently investigated nor verified these facts, representations or assumptions, although we have considered their reasonableness. If any of the facts, representations or assumptions reflected in the Memorandum are not accurate, our conclusions are not applicable.

DISCLOSURE PURSUANT TO IRS CIRCULAR 230

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