Compensation Policy for Executive and Investment Management Positions

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CalPERS

Compensation Policy for Executive and Investment Management Positions

General Program Overview

Purpose

The compensation policy has been developed over years of public review, discussion and debate. It represents the strategic decision that pay must be high enough to encourage individuals to accept and remain in positions, but not so high as to attract candidates solely for the compensation. Moreover, compensation systems must be carefully structured to both recognize labor market forces, and reinforce maximum performance through placing a substantial portion of total annual compensation at risk. This pay-at-risk approach places a premium on achieving objectives that are directly connected to the CalPERS Board of Administration's strategic and business plans. As a result, the recruitment and retention of highly skilled executives and investment management professionals serve as the foundation for the organization's overall success.

Rationale

The rationale for establishing a compensation policy for executive and investment management positions covered by this policy is based on consideration of the labor market conditions affecting the recruitment and retention of professionals in the fields of institutional investing, actuarial valuation and pension administration, most of whom are recruited from the private sector. Especially in the case of investment management professionals, the civil service salary structure differs substantially from that of the for-profit sector, the primary recruitment source. Not only are these positions more highly compensated in the for-profit sector than traditional civil service pay scales can accommodate, but total cash compensation in the for-profit sector is tied to pay-for-performance and incentive bonuses in a manner that makes fixed civil service salary ranges and steps impractical for recruiting and compensating such professionals.

Authority

SB 269, enacted in 2003, amended Government Code Section 20098 to provide that the Board of Administration shall fix the compensation of the Chief Executive Officer, Chief Actuary, Chief Investment Officer and other investment officers and portfolio managers whose positions are designated managerial. The Government Code was further amended in 2007 and 2011 to include the General Counsel and Chief Financial Officer, respectively.

All covered positions, except the exempt Chief Executive Officer, shall be filled through general civil service appointments and are subject to most of the civil service provisions of existing law, including the tenure provisions governing managerial employees. The positions are not eligible to receive Merit Salary Adjustments (MSA) as provided in Government Code Section 19832. This policy describes the program components of base pay, performance (incentive) awards, and other special pay provisions comprising the compensation system for covered positions.

Compensation Administration and Management

The CalPERS Board of Administration (Board) reserves the right to rescind or modify this policy and the compensation schedules derived from them at any time.

Covered Positions

Executive Management Positions:

- Chief Executive Officer
- Chief Actuary
- Chief Financial Officer
- Chief Investment Officer[1]
- General Counsel

Investment Management Positions:

- Chief Operating Investment Officer
- Managing Investment Director
- Investment Director
- Investment Manager
- Associate Investment Manager

The covered positions listed above may change based on any future amendments to Government Code Section 20098.

[1] Considered an Investment Management Position for purposes of determining base pay ranges (see page 6).

Program Elements

There are three components to the CalPERS Executive Compensation Program:

- Base Pay / Salary
- Pay-for-Performance / Incentive Pay
- Special Pay

Base Pay Overview

- Each covered position classification has a discrete salary range (or base pay range)
- Base pay ranges are based on relevant public and private sector market data gathered every two years, or as the Board deems necessary
- Movement within defined base pay ranges is driven by the annual employee performance appraisal process or other compelling circumstances such as equity or retention

Annual Incentive Award Overview

- An incentive award is an annual, one-time contingent cash award reflecting an individual's achievement of measurable performance objectives or measures documented in an Annual Incentive Plan
- An incentive award is a form of pay-for-performance which is intended to ensure CalPERS is meeting critical organizational objectives
- Incentive award potential varies by position

Special Pay Overview

Special pay provisions are designed to address specific or extenuating circumstances:

- Special within-range salary movement may be granted to address retention, internal equity, or extraordinary performance, subject to appropriate approvals
- Additional compensation may be granted in conjunction with interim assignment of additional responsibilities until a position is filled
- A recruitment differential, or one-time payment upon appointment to a position, may be provided to eligible appointees based on an individual's specific circumstances

Base Pay

Base Pay Ranges

Base pay ranges, rather than single rates of pay, will be established for positions covered under Government Code Section 20098(a).

Determination of base pay 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, or as determined by the Performance, Compensation and Talent Management Committee (PCTMC)
- A review of relevant data when a position becomes vacant
- Consideration of industry standards and best practices relative to executive compensation

Determining Base Pay Ranges

At the discretion of the PCTMC, the target quartile for covered positions may be determined based on market salary data for the comparator groups below at the time each salary survey is conducted.

Base pay ranges are established by using a blend of private and public-sector data as follows:

Executive Management Positions:

- Leading US public funds, leading Canadian public funds, select California-based agencies (including large local agencies), banks and insurance companies.

Investment Management Positions:

- Large and complex institutional investors, including: US public funds, Canadian public funds and US corporate plan sponsors.
- Private sector asset management organizations of comparable size ($150B to $350B AUM) that are key competitors for CalPERS team members, including: investment management/advisory firms, insurance companies and banks.

Current Base Pay Ranges

Position	Pay Range	Maximum of Quartile Range			
		Q1	Q2	Q3	Q4
Chief Executive Officer	$224,000 - 352,800	$256,200	$288,400	$320,600	$352,800
Chief Actuary	$206,000 - 310,000	$232,000	$258,000	$284,000	$310,000
General Counsel	$214,000 - 351,624	$248,406	$282,812	$317,218	$351,624
Chief Financial Officer	$210,000 - 310,000	$235,000	$260,000	$285,000	$310,000
Chief Investment Officer	$408,000 - 612,000	$459,000	$510,000	$561,000	$612,000
Chief Operating Investment Officer	$240,000 - 393,120	$278,280	$316,560	$354,840	$393,120
Managing Investment Director	$262,000 – 428,064	$303,516	$345,032	$386,548	$428,064
Investment Director	$188,000 - 307,944	$217,986	$247,972	$277,958	$307,944
Investment Manager	$140,000 - 229,320	$162,330	$184,660	$206,990	$229,320
Associate Investment Manager	$108,000 - 162,000	$121,500	$135,000	$148,500	$162,000

Salary Surveys

To ensure base pay ranges are appropriate and relatively competitive with the defined market comparator group, a comprehensive salary survey of all comparable executive and investment management positions may be conducted every two years, or as the Board deems necessary. Special surveys may also be done to validate the existing range or establish a new recruiting range when a position becomes vacant or a new position is established. In the intervening years, base pay ranges may be adjusted by an amount reflective of general annual private sector salary movement as reported by a reputable source, such as the American Compensation Association. The implementation date of any revised or newly-established pay range will be determined by the Board at the time the range is approved.

Base Pay Upon Appointment

Individual base pay is determined at the time of hire by the hiring supervisor based on factors such as internal equity, value of skills and/or expertise, and other relevant factors.

For the Chief Executive Officer and Chief Investment Officer positions, base pay is determined by the Board, based on the recommendation of the PCTMC. An individual's base pay upon appointment may not exceed the maximum for the established pay range of the position.

Base Pay Increase

Individual base pay increases are considered annually in conjunction with the performance appraisal process. An individual may be granted an increase from 0-10% based on the following factors:

- Current quartile placement in the base pay range
- Overall Performance Rating on annual performance appraisal as defined in the merit matrix as follows:

Merit Matrix Based on a 4% General Market Increase in Executive Base Pay

	Position in Base Pay Range Before Increase			
Performance Rating	**First Quartile or Below**	**Second Quartile**	**Third Quartile**	**Fourth Quartile**
Outstanding	10%	8%	6%	4%
Consistently Exceeds Standards	8%	6%	4%	2%
Meets Standards	6%	4%	2%	0%
Does Not Fully Meet Standards	2%	0%	0%	0%

Annual base pay increases will be based upon the written performance appraisal, unless otherwise recommended by the PCTMC to address existing retention or pay equity considerations.

If the annual increase, as defined by the merit matrix, places the individual's base pay above the maximum for the base pay range, the individual will be placed at the maximum for the range. Under no circumstance can the base pay exceed the range maximum.

Annual Incentive Plan

Concept of Pay-for-Performance

This Annual Incentive Plan is intended to further the mission of CalPERS by providing "at-risk" pay for a portion of pay consistent with the CalPERS total compensation philosophy. The intent of this "at-risk" program is to promote an integrated focus on achievement or progress towards organization-wide, long-term strategies.

Elements of Annual Incentive Plan

The basis for payment of the incentive award is the Annual Incentive Plan, which will tie annual incentive awards to the following distinct segments of the plan:

- Organizational Performance Outcomes (e.g., Incentive Metrics)
- Individual Key Business Objectives (e.g. business goals, leadership)

All participants will have Organizational Performance Outcomes as part of their Annual Incentive Plan. Specific Organizational Performance Outcomes may vary from participant to participant. Participants may or may not have Individual Key Business Objectives.

Organizational Performance Outcomes will be quantifiable metrics that reward for PCTMC pre-approved performance criteria in categories such as the following:

- Operational Effectiveness: Measures organizational efficiency
- Stakeholder Engagement: Measures member and/or employer perceptions
- Customer Satisfaction: Measures member and/or employer and/or employee perspectives on service received
- Investment Returns: Measures total fund and/or asset class and/or portfolio returns

The Chief Operating Investment Officer and other positions that have primary responsibility for risk management will not have Investment Returns as an Organizational Performance Outcome.

Individual Key Business Objectives can be either quantitative or qualitative performance measurements. If selected for a participant, the plan will be limited to one to three Key Business Objectives that represent specific focal points for the participant relative to the Organizational Performance Outcome categories discussed above.

Organizational Performance Outcomes and Individual Key Business Objectives will each be assigned a weight, with total weighting per incentive plan not to exceed 100%. Weights, like the applicability of each metric, may vary from participant to participant. Performance will be rated as follows:

Organizational Performance Outcomes	• Maximum (Far Exceeds High Expectations) • Between Target and Maximum • Target (Stretch High Expectations) • Between Threshold and Target • Threshold (Minimum incentive level) • Below Threshold (no award)
Individual Key Business Objectives	• Maximum (Far Exceeds High Expectations) • Target (Stretch High Expectations) • Threshold (Minimum incentive level) • Below Threshold (no award)

The Discretionary Modifier is an upward or downward adjustment that can be applied to all participants on an individual basis, as detailed in *Discretionary Performance Adjustments* (page 16).

Annual Incentive Plan Cycle

The Annual Incentive Plan cycle consists of the following activities:

- Annual Incentive Plan Development
- Semiannual Performance Reporting
- Performance Evaluation based upon achievement of Annual Incentive Plan measures

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Development of Annual Incentive Plan

Prior to the beginning of the fiscal year (or as soon as practical for new hires), each participant develops an Annual Incentive Plan comprised of quantitative and/or qualitative incentive plan measures for approval as follows:

Position	Approver(s)
Chief Executive Officer Chief Investment Officer	Board (upon recommendation of PCTMC)
Chief Actuary Chief Financial Officer General Counsel	Chief Executive Officer
Chief Operating Investment Officer Managing Investment Director Investment Director Investment Manager Associate Investment Manager	Chief Executive Officer Chief Investment Officer (by delegation from Chief Executive Officer)

Organizational Performance Outcomes and Key Business Objectives will be measured against approved performance criteria (e.g., benchmarks, enterprise performance targets). To ensure consistency with CalPERS long-term strategies, all measures require the review of appropriate supervisors and the Board's investment consultant as follows:

Position	Approvals					
	Supervisor	COIO	CIO	Investment Consultant	CEO	Board
Chief Executive Officer				✓[1]		✓
Chief Investment Officer				✓[1]	✓	✓
Chief Actuary					✓	
Chief Financial Officer					✓	
General Counsel					✓	
Chief Operating Investment Officer			✓		✓	
Managing Investment Director		✓	✓	✓[1]	✓	
Investment Director Investment Manager Associate Investment Manager	✓	✓	✓	✓[1]	✓	

[1] Investment Consultant review is required for all Investment Return performance outcomes.

Status Reports and Plan Changes

Each participant must prepare status reports on their Individual Key Business Objectives at mid-year (covering July 1 through December 31) and year-end (covering January 1 through June 30). Performance data on Organizational Performance Outcomes is reported at year-end.

Semiannual status reports require the following approvals:

Position	Approver(s)
Chief Executive Officer Chief Investment Officer	Board (upon recommendation of PCTMC)
General Counsel Chief Actuary Chief Financial Officer	Chief Executive Officer
Chief Operating Investment Officer Managing Investment Director Investment Director Investment Manager Associate Investment Manager	Chief Executive Officer Chief Investment Officer (by delegation from Chief Executive Officer)

Under extenuating circumstances, changes to incentive plan measures may be accepted and require the following approvals:

Position	Approver(s)
Chief Executive Officer Chief Investment Officer	Board (upon recommendation of PCTMC)
General Counsel Chief Actuary Chief Financial Officer	Chief Executive Officer
Chief Operating Investment Officer Managing Investment Director Investment Director Investment Manager Associate Investment Manager	Chief Executive Officer Chief Investment Officer (by delegation from Chief Executive Officer)

Investment Return performance measure changes also require review by the Board's investment consultant prior to approval and integration into the plan. The Chief Operating Investment Officer serves as the independent check in this process by overseeing the review of performance measures for consistency with established performance objectives, investment policies and compliance procedures.

Annual Incentive Award

Incentive Award

An incentive award is part of an individual's total compensation: a one-time payment based on achieving specific objectives or measures as defined in an Annual Incentive Plan.

Incentive Award Ranges

The Board, upon recommendation of the PCTMC, sets the incentive award ranges for all covered positions. The incentive award range represents the percentage of base pay available to be earned based on the level of achievement (threshold, target, or maximum) on the Annual Incentive Plan measures.

Current incentive award ranges and requirements for classifications with alternate range options are displayed in the table below. Incentive award ranges will be periodically reviewed by the PCTMC, and any change to established incentive award ranges must be approved by the Board.

Classification	Incentive Award Range	Target Award	Alternate Incentive Award Range Requirements
Chief Executive Officer	0 - 40%	27%	
Chief Actuary	0 - 40%	27%	
Chief Financial Officer	0 - 40%	27%	
General Counsel	0 - 40%	27%	
Chief Investment Officer	0 - 75%	50%	
Chief Operating Investment Officer	0 - 60%	40%	
Managing Investment Director	0 - 75%	50%	
Investment Director	0 - 60%	40%	
	0 - 75%[1,2]	50%	Newly appointed Investment Directors must complete one annual performance review cycle before being considered for this award schedule. See *Movement Between Incentive Award Ranges*, page 14.
Investment Manager	0 - 45%	30%	Range assigned upon appointment will be based on factors such as equity with peers and experience.
	or		
	0 - 60%	40%	
	0 - 75%[1,2]	50%	Newly appointed Investment Managers must complete one annual performance review cycle before being considered for this award schedule. See *Movement Between Incentive Award Ranges*, page 14.
Associate Investment Manager	0 - 40%	27%	

[1] The Chief Investment Officer, upon final approval of the Chief Executive Officer, will have discretion to increase the award schedule up to 0 - 75% based on consideration of criteria listed in *Movement Between Incentive Award Ranges* (page 14).

[2] Newly appointed Investment Directors who held the 0 - 75% range as Investment Managers may retain the range upon promotion, with Chief Investment Officer and Chief Executive Officer approval.

Movement Between Incentive Award Ranges (Investment Directors and Investment Managers Only)

For Investment Directors and Investment Managers, any movement from one established incentive award range to another must be fully documented in a request from the appropriate supervisor for review by the Chief Operating Investment Officer and approval by the Chief Investment Officer. Final approval of all schedule changes resides with the Chief Executive Officer.

Incentive award range changes are considered annually as part of the year-end process and become effective in the subsequent fiscal year. Criteria considered in support of a change to an individual's Incentive Award Range include the following:

- **Performance:** Individual performance that significantly and consistently exceeds expectations
- **Equity:** Demonstrated value of incumbent and/or inequity with relevant peers
- **Retention:** To retain competent investment professionals at risk of leaving to accept offers from other money managers or employers

Incentive Award Computation

Incentive awards are computed using the following formula:

Performance Measure Weight	**X**	**Level of Achievement (Multiplier)**	**X**	**Target Award**	**=**	**Incentive Award**

Performance Periods

Quantitative performance measures tied to investment returns will generally be based on five-year, multi-year performance against relevant benchmarks, utilizing an award schedule approved by the Board. The purpose of the schedule is to align the investment award schedules for individuals with the long-term investment objectives of the organization.

Quantitative performance measures other than total fund or specified asset class performance will generally be based on annual performance, whether internal performance improvement objectives or relevant benchmarks.

Individual Key Business Objectives (qualitative performance measures) will generally be based on annual performance.

The performance measurement periods and the provisions of the instructions for calculation are effective July 1, 2016, and will remain in effect until the issuance of a replacement schedule by the Board.

Incentive Award Calculation (Investment Returns & Metrics)

The incentive award for any Investment Return Metric will be calculated based on five-year performance, relative to benchmark, regardless of when a participant began employment in a covered position. The incentive award for all other Organizational Performance Outcomes will be calculated based on annual performance. Below are sample award calculations for Organizational Performance Outcomes.

Sample 5-Year Investment Return Payout Table:

Variance (bps) from Benchmark	Payout Ratio (Multiplier)
+35	1.50
+30	1.41
+20	1.25
+5	1.00
0	0.76
-15	0.05
< -15	0.00
Payout ratio for intermediate results will be determined by interpolation.	

Sample Incentive Metric Payout Table:

Sample Scores	Performance Level	Payout Ratio (Multiplier)
> 70%	Maximum	1.50
> 65% to 70%	One Up from Goal	1.25
> 60% to 65%	Goal	1.00
> 55% to 60%	One down from Goal	0.75
> 50% to 55%	Threshold	0.50
≤ 50%	Below Threshold	0.00

Rating Scale for Qualitative Measures

The following scale describes an individual's level of achievement on Individual Key Business Objectives (qualitative performance measures) and the corresponding multiplier used when computing the incentive award:

Performance Rating Scale for Qualitative Measures	
Rating	**Rating (Multiplier)**
Far Exceeds High Expectations	1.5
Meets High Expectations	1.0
Does Not Meet High Expectations	0
Intermediate points are interpolated	

Definitions for the Performance Ratings above are as follows:

Performance Rating Definitions
Far Exceeds High Expectations Continuously delivered results that significantly exceeded expectations. Successfully met challenges which were at times beyond the employee's control and required sustained extraordinary effort. The quality of program management, work products, and leadership is superior.
Meets High Expectations The quality of employee performance is consistent with expectations. The quality and timeliness of work products achieved desired results. Responsiveness to priorities and overall leadership has been completely demonstrated and work produced is satisfactory.
Does Not Meet High Expectations Results were not achieved or were achieved at significantly lower than expected levels. Responsiveness to changes in priorities has been slow, work products are incomplete, and/or the quality of leadership is below expectations.

Discretionary Performance Adjustments

Discretion can be exercised in the following situations:

- An award can be adjusted upward by any percentage based on qualitative individual contributions. Discretionary adjustments may not exceed the maximum incentive opportunity; in the event an adjustment exceeds the maximum incentive opportunity, the incentive award will be limited to the maximum incentive opportunity.
- An award can be adjusted downward by any percentage, or eliminated altogether based on unsatisfactory individual performance.
- For situations of non-adherence to CalPERS' risk management principles, policies, processes, or procedures, an award can be reduced by either 50% or eliminated entirely, based on the severity of non-adherence.

These adjustments will be made based on the overall performance evaluation process, and will take into account qualitative factors such as performance relative to CalPERS' culture and values; leadership; extraordinary contributions, efforts, or results; development and successful implementation of business or stakeholder imperatives; or strategic workforce activities involving succession planning, retention and flight risk, or talent supply or development.

Discretionary Modifier adjustments will be administered as follows:

Position	Approval Authority
Chief Executive Officer	Board (by recommendation of the PCTMC)
Chief Investment Officer	Board (by recommendation of the Chief Executive Officer and PCTMC)
Chief Actuary Chief Financial Officer General Counsel	Chief Executive Officer (Board retains veto authority)
Chief Operating Investment Officer Managing Investment Director Investment Director Investment Manager Associate Investment Manager	Chief Executive Officer (based upon recommendation of the Chief Investment Officer)

Discretion exercised by the Chief Executive Officer must be disclosed to the PCTMC as part of the annual incentive award determination process.

Pro-Rata Awards

Incentive awards may be prorated based on months of service for participants who are appointed during the fiscal year. The recommendation for a pro-rata incentive award will be based on the nature of the performance measures, the level of progress in their achievement, as well as overall performance.

An individual appointed during the second half of a fiscal year will normally not receive an incentive award until after completion of the following full fiscal year, at which time the award will be pro-rated to reflect the entire period of performance in the covered position.

At the discretion of, and upon the recommendation of the Chief Executive Officer and the PCTMC, the Board may grant a partial year pro-rata award to an individual who has served fewer than six months in a covered position, if the award is based entirely on performance measures designed to cover the period of time between the appointment and the end of the fiscal year. An individual who vacates a covered position within six months of appointment shall not receive an award.

An individual who is promoted from the Investment Officer III, CalPERS (IO III) classification to a covered position during the fiscal year would be eligible to receive an incentive award based on the incentive plans and annual base salaries of both positions (as pro-rated to reflect the mid-year appointment), subject to the applicable policy provisions and calculation processes outlined in the respective IO III and Executive and Investment Management Positions policies. A partial year award shall not be granted to an individual who has served fewer than a combined six months in both positions during the fiscal year.

Authority to Defer, Reduce or Eliminate Incentive Awards [1]

Payment of incentive awards shall be subject to and conditioned upon all of the following:

In the event that Total Fund for a performance period is negative, and such negative return exceeds the benchmark for the period, then the Board will have the discretion to reduce, defer or eliminate all or a portion of an employee's incentive award. In the event that the Board elects to defer payment of an award to a subsequent fiscal year, payment of the award may be deferred up to 115 days beyond the end of the first subsequent fiscal year in which the one-year absolute return on the Total Fund exceeds zero percent (0%), or, as to an individual who has been involuntarily terminated without cause by the State of California (as determined by the Board in its sole discretion) ("Terminated Without Cause"), died, becomes "disabled," or "retires," up to 115 days after the end of the fiscal year in which the individual was Terminated Without Cause, died, became "disabled" or "retired." To the extent payment is deferred for more than 120 days after the end of the fiscal year for which the incentive award is payable, the incentive award shall be credited with earnings that approximate the absolute return of the Total Fund for the deferral period as determined by the Board, but not in excess of 15% annually. The Board shall not be obligated to treat all employees eligible to an incentive award alike in determining whether to defer, reduce or eliminate an incentive award, how large a portion to defer or reduce, and when to pay the deferred or reduced incentive award.

a) An employee will be entitled to an incentive award for any period only if the employee has complied with the CalPERS Investment Policy and CalPERS ethics-related policies, such as, but not limited to, CalPERS Fraud, Criminal Acts, and Internal Investigations Policy, CalPERS Statement of Incompatible Activities, CalPERS Conflict of Interest Code, and regulatory requirements (collectively, Incentive Award Policies) throughout the period, as determined by the Board in good faith. An Incentive Award Policies violation in a prior period shall be treated as a continuing violation in each subsequent period through the date as of which the Board determines that the violation was adequately remedied. All references to the Board in this subsection and the following subsections also refer to the Board's delegate or CalPERS staffing on behalf of the Board, and all references to "employees" in these subsections refer both to current employees and former employees.

[1] The terms "disabled," "disability," "retired," "retires" and "retirement" throughout the policy are used as defined in California Public Employees' Retirement Law sections 20026, 20027 and 20060.

b) If the Board believes an employee is not entitled to an incentive award due to an Incentive Award Policies violation, it will notify the employee in writing by certified mail or personal service on the employee. If the employee disputes that finding, the employee must so notify the Board in writing within 15 days of receiving the Board's notice. If the employee does not timely notify the Board, the employee will be deemed to have admitted the violation. If the employee admits or is deemed to have admitted the violation, the employee will not receive the incentive award in question. If the employee timely denies the violation, the Board will conduct such further investigations as it deems appropriate ("Investigation"). The Investigation must be completed within 90 days of the date the incentive award would have been paid but for the violation. Within 60 days after the Investigation has been completed, the Board shall determine whether the violation occurred. Its good faith determination shall be final and binding. The Board shall delay payment of the incentive award pending that determination. If the Board determines that there was no violation, the employee will receive the incentive award plus interest at the annual rate of 6% interest for the period of late payment in excess of 60 days. This payment will be made by the earlier of (1) 30 days after the Board's determination following the Investigation, or (2) December 31 following the Board's determination.'

c) If an incentive award is paid to an employee but, within three years after the payment, the Board determines that the employee was not entitled to the payment because of an Incentive Award Policies violation, it will notify the employee in writing by certified mail or personal service on the employee. If the employee disputes that finding, the employee must so notify the Board in writing within 15 days of receiving the Board's notice. If the employee does not timely notify the Board, the employee will be deemed to have admitted the violation. If the employee timely denies the violation, the Board will conduct an Investigation. When the Investigation has been completed, the Board shall determine whether the violation occurred. Its good faith determination shall be final and binding. If the Board determines that there was a violation, or if the employee admits the violation or is deemed to have admitted it, the employee must repay the incentive award, plus interest at the annual rate of 6% interest for the period from payment to repayment, within 365 days after the Board's determination following the Investigation.

d) If at any time the Board determines the criteria used to determine an employee's incentive award were, with hindsight, improperly designed or otherwise mistaken, the Board may correct those criteria in any way, even if correction reduces or eliminates the incentive award the employee would otherwise receive.

e) Notwithstanding anything else, an employee shall not be entitled to an incentive award to the extent the Board determines that payment of the incentive award would violate applicable law.

Action upon Unsatisfactory Performance

Individuals who receive an Overall Performance Rating of 'Does Not Fully Meet Standards' in their annual performance appraisal will be ineligible to receive any portion of the incentive award at any time for the year in which the unacceptable rating was received.

Action upon Separation

Employee must be employed by CalPERS on the date the award is approved by the Board to receive an award, except in the case of death, "disability," or "retirement" or "Termination Without Cause."

Special Pay

Special Within-Range Base Pay Adjustment – Investment Management Positions

The Chief Investment Officer may, at any time during the year, recommend granting a special within-range base pay adjustment of up to 15% of annual base pay to an investment management team member covered by this policy, to address retention or internal equity issues. In extenuating circumstances, the within-range adjustment may exceed 15% of annual base pay. All adjustments (up to and exceeding 15%) must be approved by the Chief Executive Officer by delegation from the Board, and will be reported to the PCTMC.

Criteria considered in support of a Special Within-Range Base Pay Adjustment include the following:

- **Performance:** Individual performance that significantly and consistently exceeds expectations
- **Equity:** Demonstrated value of incumbent and/or inequity with relevant peers
- **Retention:** To retain competent investment professionals at risk of leaving to accept offers from other money managers or employers

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Special Within-Range Base Pay Adjustment – Executive Positions

There may be extraordinary circumstances that warrant a covered executive's base pay rate be increased, in conjunction with or outside of the annual performance appraisal process, to address unique retention or pay equity considerations. When a Special Within-Range Base Pay Adjustment is deemed necessary for an executive, the following approvals are required:

Position	Approver(s)
Chief Executive Officer Chief Investment Officer	Board (upon recommendation of PCTMC)
General Counsel Chief Actuary Chief Financial Officer	Chief Executive Officer (by delegation from the Board)

Interim Appointments

Interim appointments to covered positions may be made in instances where it is necessary to temporarily assign a team member the full range of responsibilities in a position until a new permanent appointment is completed. Such assignments shall typically be at least 60 days in duration. Interim incumbents may be eligible for additional pay while performing the interim higher-level duties. Additional pay may be based on factors such as level of duties and the base pay range of the vacant position.

Interim appointments and temporary additional compensation require the following approvals:

Position	Approver(s)
Chief Executive Officer Chief Investment Officer	Board (upon recommendation of PCTMC)
General Counsel Chief Actuary Chief Financial Officer	Chief Executive Officer (by delegation from the Board)
Chief Operating Investment Officer Managing Investment Director Investment Director Investment Manager Associate Investment Manager	Chief Executive Officer (upon recommendation of Chief Investment Officer)

The Chief Executive Officer will report interim appointments and additional temporary compensation to the PCTMC and the Board.

Recruitment Differential

In order to attract and retain highly skilled executives and investment management professionals, a recruitment differential may be provided when hiring individuals from outside State service. It is a one-time, front-end payment upon appointment and is designated as an incentive to accept a position. The amount of the differential is specific to each eligible individual's personal circumstances. In no case shall a recruitment differential exceed 60% of a new hire's annual base pay. The following approvals are required:

Position	Approver
Chief Executive Officer Chief Investment Officer	Board (upon recommendation of PCTMC)
General Counsel Chief Actuary Chief Financial Officer	Chief Executive Officer
Chief Operating Investment Officer Managing Investment Director Investment Director Investment Manager Associate Investment Manager	Chief Executive Officer (upon recommendation of the Chief Investment Officer)

The following payback provisions apply to all employees awarded a recruitment differential:

- 100% payback is required if employee resigns less than 12 full months from appointment date
- 50% payback is required if employee resigns between 12 to 24 months from appointment date

Any exception to the repayment schedule requires approval of the Chief Executive Officer and/or other approving authority as listed above.

Year-End Performance Appraisal Process (Incentive Award and Base Pay Increase)

Performance Appraisal Process Overview

The year-end performance appraisal process is the basis of the payment of the annual incentive award and the individual base pay increase. The performance appraisal document is completed at the end of the plan/fiscal year and covers both individual achievement on the Annual Incentive Plan and general managerial performance as described below.

The Chief Executive Officer, with partial re-delegation to the Chief Investment Officer for the investment management positions, will approve performance appraisal outcomes and base pay increases within the established ranges for covered positions. The PCTMC completes the performance appraisal for the Chief Executive Officer and Chief Investment Officer.

Annual Incentive Award Determination Process

As part of the performance appraisal process, each participant must submit a year-end (2nd semiannual) status report to his/her immediate supervisor reflecting the final status of all incentive plan measures. This comprehensive report is the basis for the annual incentive award.

For purposes of determining the award amount, the following occurs:

- The primary evaluator assigns performance ratings (for qualitative measures) and comments, soliciting additional input if appropriate.
- Performance ratings on quantitative investment measures are determined by calculations performed by the Board’s Investment Consultant, based upon investment performance data provided by State Street and other sources.
- Using calculations received from the Board’s Investment Consultant, Human Resources aggregates the quantitative factor multipliers (ratings), adds in the impact of qualitative factors ratings, and calculates the dollar value of the incentive award.
- CalPERS’ external auditor or other select independent advisor will review and assess the accuracy of data and processes used to calculate the results of all Organizational Performance Outcome performance achievement prior to any award being paid.

Final approval of incentive awards is defined as shown in the *Performance Appraisal Approval Process* section of the policy on page 25.

Base Pay Increase

The general assessment of managerial performance and the Overall Performance Rating is the basis of a participant's base pay increase. Base Pay Increases are administered separately and apart from the Annual Incentive Plan. At the end of the plan/fiscal year (June 30), all participants prepare a year-end Summary of Accomplishments highlighting their most noteworthy achievements not covered in the incentive plan. The primary evaluator completes the assessment of the individual's general managerial performance and assigns an Overall Performance Rating.

The Overall Performance Rating, as indicated below, is the basis for recommending a base pay increase as defined in the Merit Matrix on page 8.

Overall Performance Rating Scale

Overall Performance Rating Scale
Outstanding: Continuously delivered results that significantly exceeded expectations. Successfully met challenges which were at times beyond the executive's control and required sustained extraordinary effort. The quality of program management, work products, and leadership is superior.
Consistently Exceeds Standards: Overall performance exceeded expectations and was characterized by applying a high degree of initiative and resourcefulness in addressing several key issues during the year. The quality of work products and responsiveness to priorities is exceptional.
Meets Standards: The quality of executive performance is consistent with expectations. The quality and timeliness of work products meets expectations. Responsiveness to priorities and overall leadership has been completely demonstrated and work produced is satisfactory.
Does Not Fully Meet Standards: There is a pattern of less than anticipated quality in program performance. Responsiveness to changes in priorities has been slow, work products are incomplete, and/or the quality of leadership is below expectations.

Performance Appraisal Approval Process

The following depicts the primary evaluator and final approver for all performance appraisal outcomes:

Position	Primary Evaluator	Provides Input	Approver(s)
Chief Executive Officer	PCTMC	Board members not on PCTMC	Board
Chief Investment Officer	PCTMC	Chief Executive Officer, Board members not on PCTMC	Board
General Counsel Chief Actuary Chief Financial Officer	Chief Executive Officer	PCTMC and other Board members (optional)	Chief Executive Officer (Board retains veto authority)
Chief Operating Investment Officer Managing Investment Director	Chief Investment Officer	Chief Executive Officer	Chief Executive Officer (by delegation from the Board; based on recommendation of Chief Investment Officer)
Investment Director	Managing Investment Director	Chief Investment Officer Chief Operating Investment Officer	Chief Executive Officer (by delegation from the Board; based on recommendation of Chief Investment Officer)
Investment Manager	Investment Director	Managing Investment Director Chief Operating Investment Officer	Chief Executive Officer (by delegation from the Board; based on recommendation of Chief Investment Officer)
Associate Investment Manager	Investment Manager	Managing Investment Director Chief Operating Investment Officer	Chief Executive Officer (by delegation from the Board; based on recommendation of Chief Investment Officer)