



GLOBAL
GOVERNANCE
ADVISORS

Opinion Letter

May 29, 2024

2024-25 Chief Executive Officer Annual Incentive Plan Performance Metrics Recommendations

Prepared for:

Performance, Compensation & Talent
Management Committee

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This memo is in response to your request for Global Governance Advisors (“GGA”), in its role as CalPERS’ Board compensation consultant, to review and propose the CEO annual incentive plan measures and weightings for the upcoming fiscal year 2024-2025.

Overall Framework

As presented at the April 15th PCTM Committee meeting, GGA continues to agree with the core performance areas and plan weightings since the establishment of these measures for fiscal year 2016-17. GGA also assessed the general competitive balance between Quantitative and Individual Key Business Objectives (previously referred to as Qualitative measures) for the CEO position and found that the current weightings are within GGA’s observed market norms.

As a result, GGA recommends that CalPERS continue to adhere to its historic performance measures and weightings for the upcoming 2024-2025 fiscal year, with consideration of adjusted performance expectations for certain performance metrics to continue to be challenging, yet fair in the expectations for the CEO while also ensuring value is provided to CalPERS members.

Proposed CEO Incentive Plan Measures and Weightings

NO CHANGE

GGA proposes that CalPERS adhere to the same Measures and Weightings used in Fiscal Year 2023-2024 while adjusting performance expectations for certain performance metrics.

| Plan Weight | Measure | Assessment Type |
|-------------|--------------------------------------|--------------------------------|
| 25% | Organizational Leadership Priorities | Quantitative Objectives |
| 15% | Total Fund Performance | |
| 20% | Enterprise Operational Effectiveness | |
| 10% | Investment Office CEM | |
| 15% | Customer Service | |
| 15% | Stakeholder Engagement | |
| | | |



Organizational Leadership Priorities (25% Weighting)

NO CHANGE

Established from Board expectations and insight, the CEO is to provide organizational leadership in support of the following priorities from July 1, 2024 to June 30, 2025:

- Board Support
- Open and Transparent Communication / Building Relationships
- Efficient and Effective Organization
- Supportive and Engaged Leadership
- Customer Satisfaction Driven Organization
- Team Member Engagement

Scoring Information: A single rating will be given for the above Organizational Leadership Priorities measure, based on the following table. Payout ratio for intermediate results will be determined by interpolation.

| Score | Payout Ratio |
|-----------------------------------|--------------|
| Exceptional | 1.50 (150%) |
| Consistently Exceeds Expectations | 1.25 (125%) |
| Fully Meets Expectations | 1.0 (100%) |
| Inconsistently Meets Expectations | 0.5 (50%) |
| Does Not Meet Expectations | 0 (0%) |

Please Note: The rating levels outlined above align with last year’s levels.

Total Fund Performance (15% Weighting)

NO CHANGE

This metric is based on fund performance against the policy benchmark for the five-year period of July 1, 2020, through June 30, 2025. Payout ratio for intermediate results will be determined by interpolation.

| Variance from Benchmark (bps) | Payout Ratio |
|-------------------------------|--------------|
| +10 | 1.50 (150%) |
| +5 | 1.00 (100%) |
| 0 | 0.00 (0%) |

Please Note: The rationale and historical analysis that led to the performance expectations outlined above were discussed in detail in advance of Fiscal Year 2022-2023 based on GGA's assessment of the historical performance of CalPERS' Total Fund and typical minimum performance levels expected by pension fund stakeholders. It is recommended that GGA work with CalPERS' investment consultant (Wilshire) and the incoming CEO during Fiscal Year 2024-2025 to validate the continued reasonableness of the current performance hurdles given it will have been 3 years since the last detailed analysis was conducted. It will also allow for alignment with the new CIO's vision moving forward.

Enterprise Operational Effectiveness (20% Weighting)

CHANGE PROPOSED

This metric for 2024-25 is defined as Overhead Operating Costs as a percentage of Total Operating Costs (“OOC”) and is measured based on year-over-year improvement.

- Total Overhead Operating Costs ("OOC") identify all administrative costs not mapped directly to Product and Service Delivery Operating Costs ("PSDOC"); and excludes Board and Third-Party Administrator Costs
 - $OOC = OOC / (OOC + PSDOC)$

Past 2023-2024 Metrics

| Score | Payout Ratio |
|------------------|--------------|
| < -1.1% | 1.50 (150%) |
| -1.1% to < -0.6% | 1.25 (125%) |
| -0.6% to 0.0% | 1.00 (100%) |
| > 0.0% to 1.0% | 0.75 (75%) |
| > 1.0% to 1.5% | 0.50 (50%) |
| > 1.5% | 0.00 (0%) |



Proposed 2024-2025 Metrics

| Score | Payout Ratio |
|--------------------|--------------|
| < -1.05% | 1.50 (150%) |
| -1.05% to < -0.55% | 1.25 (125%) |
| -0.55% to 0.0% | 1.00 (100%) |
| > 0.0% to 0.55% | 0.75 (75%) |
| > 0.55% to 1.05% | 0.50 (50%) |
| > 1.05% | 0.00 (0%) |

Additional details on how GGA arrived at the proposed 2024-2025 performance expectations for Enterprise Operational Effectiveness is provided in a separate memo titled, *Annual Incentive Plan Metrics and Additional Considerations* and also dated May 29, 2024.

Ultimately, the recommended adjustments are intended to align CalPERS closer with recognized probability levels in recent years and make the performance expectations challenging, yet fair for eligible CalPERS team members while ensuring value is provided to CalPERS members.

Investment Office CEM (10% Weighting)

CHANGE PROPOSED

This metric for Fiscal Year 2024-2025 is determined by CalPERS annual participation in the CEM benchmarking survey and shows how CalPERS’ investment costs and return performance compares to a customized peer group over a five-year period.

Past 2023-2024 Metrics

| Score | Payout Ratio |
|---|--------------|
| Outperforms US Benchmark on Net Value Added (Returns) and Cost by 0.2% and 5 bps, respectively | 1.50 (150%) |
| Outperforms US Benchmark on Returns and Cost by .001% and 1 bps, respectively | 1.00 (100%) |
| Outperforms US Benchmark on Cost or Outperforms US Benchmark on Returns | 0.50 (50%) |
| Underperforms US Benchmark on Returns and Cost | 0.00 (0%) |



Proposed 2024-2025 Metrics

| Score | Payout Ratio |
|---|--------------|
| Outperforms US Benchmark on Net Value Added (Returns) and Cost by 0.1% and 8 bps, respectively | 1.50 (150%) |
| Outperforms US Benchmark on Returns and Cost by .05% and 4 bps, respectively | 1.00 (100%) |
| Outperforms US Benchmark on Cost or Outperforms US Benchmark on Returns | 0.50 (50%) |
| Underperforms US Benchmark on Returns and Cost | 0.00 (0%) |

Additional details on how GGA arrived at the proposed 2024-2025 performance expectations for Investment Office CEM performance is provided in a separate memo titled, *Annual Incentive Plan Metrics and Additional Considerations* and also dated May 29, 2024.

Ultimately, the recommended adjustments are intended to align CalPERS closer with recognized probability levels in recent years and make the performance expectations challenging, yet fair for eligible CalPERS team members while ensuring value is provided to CalPERS members.

Customer Service (15% Weighting)

CHANGE PROPOSED

This metric for Fiscal Year 2024-2025 is based on two Service Dimensions:

- Benefit Payment Timeliness: Percentage of benefit payments issued to our customers within established service levels
- Customer Satisfaction: Customer service with CalPERS services as measured by surveys and other methods

Past 2023-2024 Metrics

| Score | Payout Ratio |
|--------------|--------------|
| ≥ 96% | 1.50 (150%) |
| 95% to < 96% | 1.25 (125%) |
| 94% to < 95% | 1.00 (100%) |
| 93% to < 94% | 0.75 (75%) |
| 92% to < 93% | 0.50 (50%) |
| < 92% | 0.0 (0%) |



Proposed 2024-2025 Metrics

| Score | Payout Ratio |
|----------------|--------------|
| ≥ 97% | 1.50 (150%) |
| 96% to < 97% | 1.25 (125%) |
| 95.5% to < 96% | 1.00 (100%) |
| 95% to < 95.5% | 0.75 (75%) |
| 94% to < 95% | 0.50 (50%) |
| < 94% | 0.00 (0%) |



Additional details on how GGA arrived at the proposed 2024-2025 performance expectations for Customer Service is provided in a separate memo titled, *Annual Incentive Plan Metrics and Additional Considerations* and also dated May 29, 2024.

Ultimately, the recommended adjustments are intended to align CalPERS closer with recognized probability levels in recent years and make the performance expectations challenging, yet fair for eligible CalPERS team members while ensuring value is provided to CalPERS members.

Stakeholder Engagement (15% Weighting)

CHANGE PROPOSED

This metric for Fiscal Year 2024-2025 is based on results of the following three Stakeholder Engagement Survey questions:

- Is CalPERS sensitive to the needs of Stakeholders?
- Does CalPERS do a good job of keeping its stakeholders informed?
- On a scale of one to ten, how would you rate CalPERS being effective in engaging and communicating with stakeholders?

• Past 2023-2024 Metrics

| Score | Payout Ratio |
|--------------|--------------|
| ≥ 83% | 1.50 (150%) |
| 81% to < 83% | 1.25 (125%) |
| 80% to < 81% | 1.00 (100%) |
| 79% to < 80% | 0.75 (75%) |
| 78% to < 79% | 0.50 (50%) |
| < 78% | 0.00 (0%) |

Proposed 2024-2025 Metrics

| Score | Payout Ratio |
|-------------------|--------------|
| ≥ 80.5% | 1.50 (150%) |
| 80% to < 80.5% | 1.25 (125%) |
| 79.75% to < 80% | 1.00 (100%) |
| 79.5% to < 79.75% | 0.75 (75%) |
| 79% to < 79.5% | 0.50 (50%) |
| < 79% | 0.00 (0%) |



Additional details on how GGA arrived at the proposed 2024-2025 performance expectations for Customer Service is provided in a separate memo titled, *Annual Incentive Plan Metrics and Additional Considerations* and also dated May 29, 2024.

GGA notes that changes made to the stakeholder perception survey methodology which apply an equal weighting in the survey results between the two Member groups and two Employer groups have been done to ensure the results of any one group do not skew the overall results one way or the other. Using historical data provided by CalPERS' Policy Research and Data Analytics (PRDA) Division, we back tested survey results under the new survey weighting methodology and found that the same stakeholder perceptions scores from the four groups would result in slightly different scores under the new methodology when compared to the current methodology. In GGA's view, this means that adjustments are required to the performance expectations to ensure that similar performance under the current methodology results in a similar payout outcome under the annual incentive plan as the new methodology. The recommendations are also intended to align CalPERS closer to the recognized probability levels in recent years, continue to make the performance expectations challenging yet fair for eligible CalPERS team members, all while ensuring that CalPERS continues to provide value to its members.

We trust that this letter addresses your concerns on this matter and look forward to discussing it in more detail at the June PCTM meeting. If you have any questions on the contents of this letter, please let us know.

Sincerely,

Global Governance Advisors



Peter Landers
Senior Partner



Brad Kelly
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cc: Brittany Emmons, CalPERS