OBJECTIVE CRITERIA COMMITTEE MINUTES
BOARD OF TRUSTEES
MARYLAND STATE RETIREMENT AND PENSION SYSTEM

December 17, 2018

The Objective Criteria Committee convened at the SunTrust Building, 120 East Baltimore Street, 16th Floor, Board Room, Baltimore, Maryland, beginning at 1:03 p.m.

The Committee Members present included:

Eric Brotman, Chairman, Presiding	Theresa Lochte
Susanne Brogan (Designee)	Mary Miller
Nancy K. Kopp	Marc Nicole (Designee – via phone)
Brooke Lierman	Andrew Serafini

Other Trustees present included: Richard Norman (via phone)

Agency Staff members attending included: R. Dean Kenderdine, Executive Director/Board Secretary Anne Gawthrop, Angie Jenkins, and Andrew Palmer

Assistant Attorneys General present included: Rachel Cohen

Other attendees included: Joe Rice and Hal Wallach of CBIZ Compensation Consulting and Phillip Anthony

Minutes

On a motion made by Treasurer Kopp and seconded by Ms. Lochte, the Committee approved the November 29, 2018 open session meeting minutes.

Draft Objective Criteria Committee Governance Charter

Mr. Kenderdine reported that subsequent to the OCC meeting, additional edits were made to the draft Objective Criteria Committee Governance Charter that had been approved by the Committee at its last meeting. These additional edits add language that makes the charter fully reflective of the legislation granting the Board salary setting authority. The Committee was provided with a copy of the edits which were reflected by strike-outs or capitalized language. The Committee accepted the charter revisions.

Compensation Philosophy Statement for the System's Investment Division

Hal Wallach and Joe Rice from CBIZ Compensation Consulting presented the Committee with a red-lined version of the Compensation Philosophy for the System's Investment staff, which reflected the changes requested by the Committee at its November 29, 2018.

Objective Criteria for Establishing New Positions and their Qualifications within the Investment Division

CBIZ provided the Committee with recommended criteria for staffing levels for comment and suggestion for improvement before CBIZ presents them to the Board. The report provided the following recommendations for objective criteria:

- Documented business case, referencing objective measures, such as:
  - Reduction in fees from third-party services
  - Changes in number of investment strategies
  - Changes in the number of managed investment accounts
  - Overtime hours.
- Backup/Redundancy
  - Ensure that there is sufficient backup and knowledge within each asset class or investment strategy for continuity in the event of employee exit.
- Succession Planning
  - Identify risk associated with key positions due to the potential for exit from the organization (retirement or flight risk)

- Peer Benchmarking
  - Report current staffing levels compared to the market benchmark ranges (*i.e.*, 25th to 75th) as reported by periodic benchmarking from CEM Benchmarking.

Trustee Lochte asked how often periodic benchmarking would be conducted.

Mr. Rice responding that it should be done every three to five years.

Prospective Salary Ranges and Proposed Criteria for Base Salary and Adjustments

Messrs. Rice and Wallach next addressed the matter of objective criteria for setting base salaries and adjustments for qualified investment staff. The consultants presented data based on practices offered within the competitive market, considering the System's industry, size, as well as the duties and responsibilities of each relevant investment staff position.

The consultants provided a table to the Committee with proposed salary ranges for each qualified position, as follows:

Proposed Salary Ranges				
	Structure Range			
Title	Minimum	Midpoint	Maximum	Range Spread
Executive Assistant	41,358	54,541	65,827	59%
Accounting Lead Specialized	46,857	61,983	75,012	60%
Assistant Director – Investment Administration	46,857	61,983	75,012	60%
Sr. Compliance Analyst	60,543	80,463	97,203	61%
Director – Investment Administration	60,543	80,463	97,203	61%
Managing Director – Investment Admin & Acct.	92,333	107,785	123,236	33%
Director – Accounting	60,543	80,463	97,203	61%
Investment Associate	65,435	76,886	88,337	35%
Sr. Investment Analyst I	71,978	84,575	97,171	35%
Sr. Investment Analyst II	81,051	97,261	113,471	40%
Sr. Investment Analyst III	101,313	121,576	141,839	40%
Sr. Compliance Manager	108,873	127,926	146,979	35%
Sr. Portfolio Manager I / Sr. Risk Manager I	116,713	145,891	175,069	50%
Sr. Portfolio Manager II / Sr. Risk Manager II	128,384	160,480	192,576	50%
Sr. Portfolio Manager III / Sr. Risk Manager III	147,642	184,552	221,463	50%
Sr. Portfolio Manager IV	155,024	193,780	232,536	50%
Sr. Portfolio Manager V	170,526	213,158	255,790	50%
Managing Director	188,563	245,132	301,700	60%
Deputy Chief Investment Officer	207,419	269,645	331,871	60%
Chief Investment Officer	269,645	350,538	431,432	60%

Messrs. Rice and Wallach provided the Committee with a comparative salary analysis that indicated that of the 17 current investment discretion position, the average overall base salary compa-ratio (employee's salary divided by the market 50th percentile) is 74.4%. A compa-ratio of 74.4% means that, on average, division salaries were 25.6% below the midpoint of the market for similar positions.

The Committee was provided with the following proposed criteria for an employee to be eligible for an increase in compensation:

- Salary ranges are established with range midpoints that approximate the median of the market
- When an employee's salary is at or above the salary range midpoint, an increase should only be considered in years when the fund meets or exceeds policy benchmarks.
  - If an employee's salary is below the salary range midpoint, an increase should be considered regardless of fund performance
- Additional factors such as the degree of fund success and an individual's asset class performance may be utilized for setting pay
- Compensation adjustments may be made for additional education and certifications
  - This will encourage investment staff to participate in advanced training and education.
  - Additional training offers an overall benefit to the operation of the Agency and System.
- In order to receive compensation, the certification or degree must be deemed beneficial to the Agency as part of the employee's work responsibilities and must exceed the minimum requirements for the employee's position.

Mr. Brotman requested that language be added to include that if an employee's asset class meets/does not meet benchmark, then the employee will/will not get an increase. Mr. Brotman does not want anyone to be excluded from an increase by language that says increases would only be considered in years when the fund meets or exceeds policy benchmark.

Ms. Brogan asked who has the authority for determining who among the staff gets salary increases.

Ms. Cohen responded that the Statute requires the Board, not the CIO, to determine compensation for Investment Division staff and approve any salary increases.

Ms. Brogan asked if the Agency pays for education.

Mr. Kenderdine responded that the Agency does pay for education, after the course or program is successfully completed.

Proposed Incentive Compensation Objective Criteria and Prospective Plan Design Parameters

Messrs. Rice and Wallach next addressed the matter of objective criteria for incentive compensation for qualified investment staff. The consultants documented incentive plan practices offered within the competitive market, considering the System's industry, size, as well as the duties and responsibilities of each relevant investment staff position. They reported that approximately one-half of larger public pension plans (those with more than $10B in assets) provide incentive compensation.

The consultants' analysis also found that performance metrics typically include a combination of (1) comparison to a "Total Policy" index, as well as (2) "absolute" performance, with common performance periods including one, and three-year horizons.

A table was presented showing “market average target incentive percentages, as a percent of base salary, for each of the qualified positions, with maximum award opportunities generally around 150% of the target percentages.

Market Average Annual Incentive (Percent of Base Salary)		
Position	Target (all peers)	Target (bonus-paying)
Chief Investment Officer	20.0%	30%
Deputy Chief Investment Officer	25.0%	35%
Managing Director	25.0%	35%
Sr. Portfolio Manager V	40.0%	50%-60%
Sr. Portfolio Manager IV	40.0%	50%-60%
Sr. Portfolio Manager III / Sr. Risk Manager III	25.0%	35%
Sr. Portfolio Manager II / Sr. Risk Manager II	20.0%	30%
Sr. Portfolio Manager I / Sr. Risk Manager I	20.0%	30%
Sr. Compliance Manager	0.0%	5%-10%
Sr. Investment Analyst III	10.0%	10%-15%
Sr. Investment Analyst II	10.0%	10%-15%
Sr. Investment Analyst I	5.0%	5%
Investment Associate	0.0%	5%

The consultant’s then offered proposed incentive plan design parameters to the Committee which included:

- ➢ Utilizing the following performance metrics for determining incentive awards (performance measured/compared over a three-year period for each):
  - Actual System performance vs. Policy Benchmark
  - Actual System performance vs. Actuarial Assumed Rate of Return
  - Actual System performance vs. Asset Class
- ➢ That the plan have a single hurdle that must be met for any incentives to be awarded – the fund must have a positive return relative to the Policy Benchmark over a three-year period.
- ➢ For new hires and job changes, the performance period will be measured based on time in the job (in full year increments), until they reach three years of service.
- ➢ Any earned amounts will be paid over a two-year period in equal installments (50% of earned amount per year).

Mr. Brotman recommended including a requirement that each staff member’s assigned asset class have a positive return over a three-year period in relation to the asset class benchmark. It should apply to the incentive compensation as it did in the base salary. The incentive eligibility requirements should not preclude anyone who is performing well.

Mr. Wallach responded that they would revise the language so that the requirement for the plan to outperform its benchmark will affect the incentive based on the plan exceeding the actuarial rate but not limit incentives for individual asset class performance.

Ms. Miller questioned the inclusion of the Sr. Compliance Manager position as the November meeting minutes did not distinguish salary and incentive pay for that position. Ms. Miller asked that the current minutes reflect that this position is not eligible for incentive awards.

Ms. Lochte asked the consultant to add a Scenario #3 where the benchmark is 0 and the assumed rate of return is 0, but with a positive asset class incentive.

Ms. Miller asked that the historical performance slide be done in the reverse order and show statistics from 2010 to 2018, not 2018 to 2010, as presented.

Final Discussion

Mr. Brotman summarized the meeting and requested that Messrs. Rice and Wallach, prepare only recommendation slides for presentation to the Board of Trustees on January 15, 2018.

Mr. Palmer commented that the Board should receive the Objective Criteria recommendations and the process for implementation, including positions, salary ranges and incentive plan.

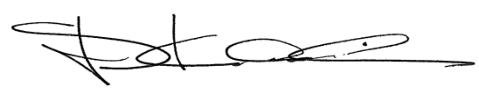
Mr. Brotman confirmed that the Committee will be recommending to the Board, for its approval, the Compensation Philosophy Statement, Objective Criteria for Base Salary and Adjustments and Objective Criteria for Incentive Compensation.

Mr. Kenderdine reported that the consultant would prepare the recommendations as requested by the Committee and the presentation would be sent to the Committee for a final review and an electronic vote on January 7 or January 8.

Adjournment

There being no further business before the Committee, on a motion made by Ms. Lochte and duly seconded, the meeting adjourned at 3:30 p.m.

Respectfully submitted,



R. Dean Kenderdine
Secretary to the Board