

Compensation Backgrounder Supplemental Overview: June 2023

Governance

Located in Fredericton, New Brunswick, Vestcor Inc. is an independent private not-for-profit private corporation that provides innovative, cost-effective global investment management and pension and benefit administration services solutions that are aligned with the best interests of a number of public sector entities. The cost savings that Vestcor provides significantly contribute to the long-term growth of our client's investments.

Vestcor is jointly owned by the New Brunswick Public Service Pension Plan and the New Brunswick Teachers' Pension Plan, and is governed by an independent expert Board of Directors who are legislated to manage the affairs of Vestcor on a commercial basis. All decisions and actions are based on sound business practices.

With respect to compensation matters, the Board of Directors is supported by its Human Resources and Compensation Committee (HRCC). The Board of Directors has established the HRCC to assist in fulfilling its obligations relating to the establishment of policies for compensation of employees, leadership succession planning, and setting of human resource policies and practices to attain Vestcor's strategic goals. The HRCC is comprised of Directors with experience in compensation-related issues. They are assisted from time to time by compensation consulting experts and through investment industry-based compensation surveys carried out by third parties.

The Board of Directors, with the assistance of the HRCC, developed a Compensation Philosophy and an Incentive Compensation Program, based on industry best practices, which support Vestcor's need to attract and retain experienced highly specialized professional talent required to successfully deliver on its corporate mandate and objectives. In addition, they support Vestcor's Strategic Plan, desired organizational culture, and positioning within the competitive marketplace.

Compensation Principles: The Incentive Compensation Plan

The Incentive Compensation Plan (ICP) is comprised of five areas, as follows:

- Corporate Scorecard
- Individual Performance
- Absolute Client Return
- Investment Total Fund Performance
- Investment Team Performance

The **Corporate Scorecard and Individual Performance** components are based on both overall and individual achievements toward the corporate business plan objectives, as pre-approved annually by the Board and aligned with Vestcor's strategic plan. The individual portion reflects each employee's quantitative and qualitative performance targets. For each eligible employee, the incentive is calculated as a percentage of salary, weighted to reflect their seniority, the specific role and impact that each has had on the annual business plan objectives.

The **Absolute Client Return** investment performance award is measured quantitatively over a longer term four-year cumulative basis, compared to client long-term total fund investment objectives. It applies only to the investment staff, the senior executive management team and select other positions.

The two final components **target top quartile** relative investment performance for the organization and focus on achieving sustained asset growth through continuous strengthening of team cooperation.

The **Investment Total Fund Performance** is measured quantitatively on a four-year cumulative basis, compared against the value-added target set by the Board. Net value-added investment returns represent the gross investment return in excess of the investment policy benchmark returns, after deducting all investment management costs.

The **Investment Team Performance is based on** specific asset class value added returns as compared to Board approved value added targets on actively managed portfolios to promote teamwork within these investment asset classes. Investment management employees are organized into one of four teams eligible for this ICP component: Fixed Income, Quantitative Investments, Equities, and Real Assets.

The ICP applies to employees who have been employed with Vestcor in a permanent role for a minimum of 6 months. To further align with our long-term performance, starting in 2021 a significant portion of the ICP award is deferred for payment in future years for certain positions, including all investment and risk management staff, CEO, CFO, CIO and CPBO.

The deferred ICP is paid out over four years, with 50% being paid in year one and the remaining 50% being paid out in equal installments over the subsequent three years. In an additional alignment to client investment performance, deferred amounts accrue a return equal to the total actual overall annual investment return achieved during the deferral period.

The amount of ICP awarded is included in the overall total corporate operating costs and outlined in detail in the Vestcor Inc. Annual Report.

Results for the Year Ended December 31, 2022

For the year ended December 31, 2022, and after consideration of Vestcor's strong long-term investment performance, Annual Business Plan achievements, and the continuing competitive talent retention environment, the Board approved:

- A modest cost of living salary increase;
- A merit pool based on the business plan achievement (Corporate Scorecard) factor of 1.34 versus a maximum factor of 2, compared to a factor of 1.28 for the year ended December 31, 2021. Individual components were based on each employees' contribution to the business plan accomplishments; and
- Investment management related incentive payments based on record high long-term net of expense four-year Total Funds outperformance over client policy benchmarks of 1.31% per year and the strong long-term performance of three out of four investment teams.

The total fund active nominal return for investment mandates where Vestcor investment teams have full management discretion for the year ended December 31, 2022 was -3.46%, however the more relevant longer-term annualized active nominal return for the past four years ending December 31, 2022 was 5.97%, which represents approximately \$4.6 billion of cumulative gross investment earnings. Most importantly, this equated to a 6.92% gross per annum return since Vestcor's inception in 1996.

The performance-based incentive component of total compensation expense was \$9.027 million for the year ended December 31, 2022, compared to \$8.570 million in 2021. \$2.905 million was related to the deferred portion of the ICP, which will be paid out over three years, and \$2.657 million was from the LTIP which is being phased out through 2023. As noted above, this performance-based incentive component is largely based upon the outperformance of the longer-term four-year investment performance versus client benchmarks of 1.31% per year, which represents approximately \$1.018 billion of net investment value added return, and the Corporate Scorecard factor of 1.34.

Further details on the ICP and amounts awarded in 2022 are detailed in the 2022 Annual Report. Visit vestcor.org/annualreports to access a copy.

External Compensation Reviews 2020-2021

In 2020, the HRCC, as part of its periodic review cycle, retained an independent expert compensation advisor (Willis Towers Watson) to provide external third-party advice with respect to an extensive Total Compensation Review for all Vestcor employee positions. Previous reviews had been completed in 2017 for administration and corporate services positions, and in 2015 for investment positions.

In conducting the review, investment and pension administration positions were compared to other internally managed pension funds of similar asset size and investment strategy complexity. Corporate services positions were compared to similar general industry positions adjusted for regional differences, and to other Atlantic Canada organizations of similar size.

The results led to modifications to our incentive plan, in line with the evolution of industry best practices. While continuing to be performance based the new plan is clearer, simpler, and provides further alignment with the goals and objectives of our clients, while providing the necessary means to better serve Vestcor’s challenging talent attraction and retention objectives.

The new Incentive Compensation Plan (ICP) took effect on January 1, 2021, replacing the former program which was made up of the Annual Incentive Plan (AIP) and Long-Term Incentive Plan (LTIP). The AIP was retired as of 2021, while the LTIP which was based on longer-term previously accumulated four-year results will be phased out through 2023. Once fully transitioned, the change in design to the ICP is not intended to significantly affect the overall total incentive award opportunity.

In 2021, Willis Towers Watson was also retained to review and provide advice with respect to the investment benchmarks and value-added targets referenced by Vestcor in our incentive plan. Overall, they were very comfortable with the current performance benchmarks and targets used by Vestcor for the individual asset classes and total fund.

Further detail on the ICP and the phasing out of the previous AIP and LTIP are in the 2020 and 2021 Annual Reports, available at vestcor.org/annualreports.

Message from Board Chairperson David Losier

Chair of the Board of Directors of Vestcor Inc., Mr. Losier is also a Member of the Audit, Human Resources & Compensation, and Governance Committees.

“Although 2022 was a very challenging year for investment managers, Vestcor's clients could once again count on the exceptionally talented team we have assembled right here in New Brunswick to significantly outperform their investment benchmarks, deliver tremendous value and customer service. The Vestcor board of directors will continue to follow industry best practices in our human resource programs to the benefit of all our stakeholders.”

REFERENCES

- Vestcor Compensation Philosophy Overview - vestcor.org/governance, under “Board Committees”, “The Human Resources & Compensation Committee”
- Human Resources and Compensation Committee Terms of Reference - vestcor.org/governance, under “Board Committees”, “The Human Resources & Compensation Committee”
- Vestcor Inc. 2022 Annual Report - vestcor.org/annualreports