



October 14, 2022

MEMORANDUM

TO: VRS Board of Trustees

FROM: Patricia S. Bishop
Director

RE: Agenda Materials for October 18th Board Meeting

We are looking forward to the October 18th Board meeting beginning at 1:00 p.m. in the VRS Boardroom located at 1111 East Main Street, Bank of America - Pavilion Building, 3rd floor. Enclosed are the agenda and meeting materials. Boxed lunches will be available beginning at noon.

In advance of the meeting, listed below are some important reminders:

- As part of a COVID-19 self-screening protocol, please ask yourself if you are experiencing any of the following:
 - A new fever (100.4°F or higher) or a sense of having a fever.
 - A new cough that cannot be attributed to another health condition.
 - New shortness of breath or difficulty breathing that cannot be attributed to another health condition.
 - New chills that cannot be attributed to another health condition.
 - A new sore throat that cannot be attributed to another health condition.
 - New muscle aches (myalgia) that cannot be attributed to another health condition, or that may have been caused by a specific activity (such as physical exercise).
 - A new loss of taste or smell.
 - Have you had a positive test for the virus that causes COVID-19 disease within the past 5 days?
 - In the past 5 days, have you had close contact (within about 6 feet for 15 minutes or more) with someone with suspected or confirmed COVID-19?

If you are experiencing any of the above symptoms, please do not attend the meeting in person.

Again, we look forward to seeing you at the Board of Trustees meeting on Tuesday. If you have any questions, please feel free to contact me.

Attachments

cc: The Honorable Stephen E. Cummings, Secretary of Finance
Craig Burns, Department of Taxation
Michael Jay, House Appropriations Committee
April Kees, Senate Finance Committee

Mike Tweedy, Senate Finance Committee
Zack Borgerding, Auditor of Public of Accounts
Jon Howe, Department of Planning and Budget
Dean Lynch, VA Association of Counties
Katie Boyle, VA Association of Counties
Bea Snidow, VA Education Association
Jamie Bitz, Joint Legislative Audit & Review Commission
Kimberly Sarte, Joint Legislative Audit & Review Commission
Hal Greer, Joint Legislative Audit & Review Commission
Elizabeth Bushnell Myers, Office of the Attorney General
Jessica Ackerman, VA Municipal League
Lawrence Kochard, VRS Investment Advisory Committee
Bonnie Atwood, VA Retired Teachers Association



Board of Trustees Meeting
VRS, 1111 E. Main St., 3rd Floor Board Room
Tuesday, 10/18/2022
1:00 - 3:30 PM ET

I. Approve Minutes

- **September 22, 2022**

- Board Minutes 9.22.22 - Page 5*

II. Report of the Chief Investment Officer

- Asset Allocation Report 8.31.22 - Page 18*

- Daily Asset Allocation Report 10.11.22 - Page 19*

- Performance Summary 8.31.22 - Page 20*

- Plan Tracking Error - Page 21*

- New Investments and Terminations - Page 22*

- DIME Quarterly Summary - QE 9.30.22 - Page 23*

- Manager Referral Quarterly Summary - QE 9.30.22 - Page 29*

- **RBA - Revisions to DB Plan Asset Allocation**

- RBA - Revisions to DB Plan Asset Allocation - Page 30*

III. Report of the Benefits and Actuarial Committee

- Report of the B&AC - Page 32*

- **RBA – Accept the Plan Actuary’s Valuations as of June 30, 2022, for the Five Statewide Retirement Plans, Group Life Insurance, Health Insurance Credit Plans for State and Teachers**

- RBA - Accept Plan Valuations - Page 35*

- Actuarial Valuation Results_Board - Page 36*

- **RBA – Amendments to the VRS Funding Policy Statement**

- RBA - Amendments to Funding Policy Statement - Page 70*

- VRS Funding Policy 2022 tracked changes - Page 72*

- VRS Funding Policy 2022 - Page 85*

IV. Report of the Administration and Personnel Committee

- Report of the A&PC - Page 98*

- **RBA – Revisions to the Investment Professionals’ Pay Plan**

- RBA - Amended Investment Pay Plan - Page 100*

- Investment Professionals Pay Plan_Clean - Page 101*

- Investment Professionals Pay Plan_Redline - Page 118*

- VRS Investment Pay Review_April 2022 - Page 136*

- **RBA – Appointment and Reappointment of Investment Advisory Committee Members**

- RBA - Reappoint - Appoint IAC Members - Page 154*

- Resume for Theodore Economou - Page 155*

- Bio for Thomas Gayner - Page 156*

- Bio for Larry Kochard - Page 157*

- Bio for Palmer Garson - Page 160*

- **RBA – Review Revised Governance Policy and Committee Charters (1st of 2 Reviews)**

- RBA - Amend Board Governance Documents (Rename A&P Committee) - Page 161*

- Edits to Board Governance Policy - Page 162*

Edits to AFT Committee Charter - Page 182

Edits to A&C Committee Charter - Page 186

Edits to Code of Ethics - Page 192

V. Proxy Voting Discussion (Corporate Governance Report)

Corporate Governance Report FY2022 - Page 202

Exhibit 1 - Proxy Voting and Securities Litigation Policy - September 2018 - Page 205

Exhibit 2 - 2022 US Proxy Voting Guidelines - Page 214

Exhibit 3_Managers Not Using ISS_FY2022 - Page 289

VI. Commending Resolution for Troilen G. Seward, Ed.S.

Resolution for Troilen G. Seward - Page 290

VII. Commending Resolution for Deborah Allen Hewitt, Ph.D.

Resolution for Deborah Allen Hewitt - Page 291

VIII. Report of the Director

FY 2023 Agency Roadmap Update - September - Page 292

Director's Report Slides - Page 294

Minutes

A regular meeting of the Virginia Retirement System Board of Trustees was held on September 22, 2022, in Richmond, Virginia with the following members participating:

Board members:

A. Scott Andrews, Chair
Joseph W. Montgomery, Vice Chair
Hon. J. Brandon Bell, II
John M. Bennett
Michael P. Disharoon
William A. Garrett
Dr. Susan T. Gooden, Ph.D.
W. Brett Hayes
Lindsey K. Pantele

Investment Advisory Committee:

Lawrence E. Kochard, Ph.D., Chair (*attended remotely*)

VRS Staff:

Patricia Bishop, Ron Schmitz, Jennifer Schreck, Andrew Junkin, Rory Badura, Daniel Ball, Parham Behrooz, Kevin Bliss, Deardrian Carver, Lakiesha Cheatham, Jeanne Chenault, Michael Cooper, David Cotter, Harriet Covey, Juanita Cribbs, Valerie Disanto, Pam Elam, Barry Faison, Jonathan Farmer, Laurie Fennell, Josh Fox, Jay Gentry, Brian Goodman, JT Grier, Krystal Groff, KC Howell, Robert Irving, Ross Kasarda, Kristina Koutrakos, Matt Lacy, Chung Ma, Curt Mattson, Walker Noland, Greg Oliff, Angela Payne, Steven Peterson, Laura Pugliese, Steven Ramirez, Paula Reid, Mark Rein, Dan Schlusser, Michael Scott, Virginia Sowers, Leslie Weldon, Dan Whitlock, Cindy Wilkinson, Steve Woodall and Nick Zizzo.

Guests:

Lauren Albanese, Financial Investment News; David Barry, Markets Group; Jeremy Bennett, Virginia Association of Counties; Jamie Bitz, Joint Legislative Audit and Review Commission; Joe Ebisa, With Intelligence; Emily Grimes, Department of Planning and Budget; Madeline Katz, Financial Times; Rob Kozlowski, Pensions & Investments; Elizabeth Myers, Office of the Attorney General; Erin Rodriguez, Auditor of Public Accounts; Adam Rosatelli, Senate Finance and Appropriations Committee; and Bea Snidow, Virginia Education Association.

The meeting convened at 1:00 p.m.

Opening Remarks

Mr. Andrews called the meeting to order and welcomed everyone to the September 22, 2022, meeting of the Virginia Retirement System Board of Trustees. Mr. Andrews introduced the newest Board member, Lindsey Pantele, who is replacing Troilen Seward as her term had expired. Ms. Pantele is a teacher with Henrico County Public Schools, where she was selected as the county's Teacher of the Year in May of 2020. Ms. Pantele earned her undergraduate degree in English and Language Arts, and a Master's in Teaching from Christopher Newport University.

Next, Mr. Andrews commended Ms. Seward for her 10 years of service to the VRS Board of Trustees and acknowledged her contributions to VRS and education throughout the Commonwealth. Mr. Andrews advised a formal recognition of Ms. Seward's service will take place during the October Board meeting.

Mr. Andrews also introduced Andrew Junkin, who will succeed Ron Schmitz as the new Chief Investment Officer upon Mr. Schmitz's retirement in January 2023. Mr. Junkin joins VRS after serving as CIO for the state of Rhode Island and a fifteen-year tenure with Wilshire, the last five of which he served as president. Mr. Junkin will be working closely with Mr. Schmitz over the following months to provide continuity and facilitate an effective transition. Mr. Andrews thanked Mr. Schmitz for his leadership and assistance during the transition period.

Approval of Minutes

Following a motion by Mr. Montgomery, and a second by Mr. Bennett, the VRS Board of Trustees unanimously approved the minutes from its June 23, 2022, meeting.

Committee Assignments

Next, Mr. Andrews advised that with the appointment of a new Board member, updates to the committee assignments are required, in accordance with the Governance Policy. Upon a motion by Mr. Andrews, with a second by Mr. Montgomery, the Board unanimously approved the following changes to the committee assignments:

- Mr. Disharoon will fill the vacant seat on the Administration and Personnel Committee.
- Ms. Pantele will take Mr. Disharoon's seat on the Benefits and Actuarial Committee.

Report of the Investment Advisory Committee

Lawrence Kochard, Chair of the Investment Advisory Committee, began his report by noting the IAC met on August 18, 2022, and approved the minutes from its April 13, 2022, meeting. The Committee received the Chief Investment Officer's (CIO) report that included an overview of market conditions, asset allocation, tracking error and total fund performance as of June 30, 2022. The Committee was informed by the CIO that Public Equity was below its lower policy limit due to market action as of June 30, 2022. The Board previously approved new policy weights for the new fiscal year, and, as of July 1, 2022, the portfolio was within its allowable range. The Committee noted that returns, short- and long-term, have been favorable and all asset classes generally remain above their respective benchmarks.

The Committee also received the Portfolio Solutions Group program review. The Committee then participated in the forward returns and stress test scenarios discussion which included four prospective recovery scenario simulations and their potential implications for the long-term assumed rate of return, funded status, contribution rates and liquidity.

Mr. Andrews thanked Mr. Kochard for his report.

Report of the Chief Investment Officer

Ron Schmitz, CIO, began his report with a market overview and discussed asset allocation, total fund portfolio and tracking error, concluding that risk measures are within Board-approved levels.

Mr. Schmitz discussed in more detail the asset allocation positioning as of June 30, 2022, and more recently, as of September 12, 2022. Mr. Schmitz informed the Board, that as expected and previously disclosed, due to market action and not staff action, Public Equity had indeed fallen below its lower policy limit as of June 30, 2022. He told the Board their approval of the new policy weights at their last meeting had, as intended, moved Public Equity back within the allowable range. Mr. Schmitz then shared with the Board that continued market action was affecting the weightings of equity related exposures and the potential for another market-driven breach of policy was expected. He reviewed his previous and current view of looking at equity (public and private) exposure and positioning within the applicable allowable ranges on a combined basis for the total fund. As a result, Mr. Schmitz was not recommending any corrective action at this time. The Board agreed with Mr. Schmitz's evaluation of the situation and his recommendation.

Next, Mr. Schmitz discussed the New Investment and Terminations report, the Diverse Investment Manager Engagement (DIME) report, and the External Investment Manager Referral report.

Mr. Andrews thanked Mr. Schmitz for his report.

Annual CEM Benchmarking Report on Administration

Mike Heale of CEM Benchmarking, Inc., provided the annual Pension Administration Benchmarking Report for FY 2021 to the Board. CEM measures cost and service levels and provides an analysis of performance relative to peer agencies, as well as comparative data and insights from a broader group of CEM-participating plans. The presentation focused on VRS compared to a peer group of other U.S.-based retirement systems with similar membership size. Areas of service reviewed and measured included the call center, VRS website (including myVRS), one-on-one membership counseling and presentations, pension inceptions and member statements.

With a cost of \$81 per active member and annuitant, VRS' total pension administration cost per active member and annuitant is \$26 below the peer group average of \$107. Mr. Heale provided a summary of the trend in total pension administration costs from 2014 to 2021. He noted that VRS' total pension administration cost per active member and annuitant increased on average by 3.9% per annum, compared to a peer average of 1.9% per annum. This increase is mainly due to IT upgrade projects, like myVRS, and the introduction of new programs such as the Hybrid Retirement Plan, the Virginia Local Disability Program and communication initiatives for the Line of Duty Act.

Mr. Heale advised that VRS achieved a total service score of 81, which is above the peer group median of 79. VRS' service score has steadily increased since 2014, however, the COVID-19 pandemic impacted some areas of key service measures included in the service score. Areas specifically impacted were the call center and attendance of one-on-one member counseling and presentations. Despite these challenges, improvements to the agency's website by adding additional online tools, such as online retirement applications and refund requests, had a positive impact on the total service score.

Mr. Heale concluded by reiterating that VRS provides a relatively high level of service at a cost comparatively lower than its peers.

Mr. Andrews thanked Mr. Heale for his presentation and commended the VRS staff for achieving these exceptional results. In addition to having placed in the desirable quadrant for over a decade, Mr.

Andrews noted that providing a high level of service at a lower cost when compared to U.S. peers is a testament to staff's commitment to exceptional service and continuous improvement.

Report of the Defined Contribution Plans Advisory Committee

The VRS Board of Trustees received the report of the Defined Contribution Plans Advisory Committee following its meeting on September 8, 2022 and placed it on file.

GOVERNING DOCUMENTS UPDATE

Defined Contribution Incentive Plan (DCIP) Plan Document Amendments and Amended DCIP Master Trust

Staff presented a Request for Board Action regarding amendments to the Defined Contribution Incentive Plan for VRS Personnel. On January 1, 2021, most Defined Contribution (DC) Plans were amended and restated to bring them up to date, but this plan was not updated. VRS worked with outside benefits counsel to amend and restate this plan to have language consistent among all plans. This plan has undergone several name changes since its inception 20 years ago. The last amendment and restatement occurred in May 2013; first amendment in November 2014, second amendment February 2017, and in September 2020 the plan name was changed to its current name. This document has been amended to include provisions of recent federal legislation and the format is now consistent with the other plan documents. This amendment removes restrictions and allows participants, at least age 55, to transfer assets from the plan into their cash match plan. It also includes the first amendment to the Master Trust, which changes the reference to the correct plan name and adds provisions to cover the return of mistaken contributions and strengthens compliance language for separate accounting.

Upon a motion by Senator Bell, with a second by Mr. Montgomery, the VRS Board of Trustees approved the following action:

RBA: Approve Amended and Restated Defined Contribution Incentive Plan for VRS Personnel (DCIP) and First Amendment to the DCIP Master Trust.

Request for Board Action 2022-09-13: The VRS Board of Trustees approves the Amended and Restated Defined Contribution Incentive Plan for VRS Personnel (DCIP) (effective as of January 1, 2023) and the First Amendment to the DCIP Master Trust (effective September 22, 2022).

ADMINISTRATION

Administrative Reports & Communications

Staff provided an overview of the DC plans, as well as an update on administrative reports for the second quarter of 2022. An overview of assets and accounts across the various defined contribution plans, as well as account trends, was also provided. VRS won National Association of Government Defined Contribution Administrators (NAGDCA) Leadership Awards in two categories – COVID-19 response and for participant communication and engagement. VRS is also a finalist for the NAGDCA Art Caple award, which will be announced later in September. Staff shared that assets have decreased since last quarter in the COV457/Cash Match Plan. Hybrid plan assets have also decreased; however, this plan continues to be consistent in account balance growth and voluntary contributions, with 47% maximizing at 4% and 47% contributing 1% or less. Highlights from Hybrid Automatic Escalation were shared, which

included interactive webpages for members and employers, an Employer Guide and a member poster in preparation for 2023. Staff also shared an overview of ORPHE assets, including participant counts and balances with DCP (MissionSquare) and TIAA. Further, staff provided updates from the Annual Review with MissionSquare, which addressed topics such as participant engagement, key accomplishments and future initiatives. In addition, staff offered an update regarding the Service Review with TIAA where total payouts, assets and engagement activity were presented.

DC Plans Record Keeper Update

Staff provided an update on the DC Plans Consultant RFP. The RFP is in its final review prior to posting and will be issued this month. The RFP will be out for eight weeks after which the review process will start.

INVESTMENTS

Annual Investment Review

Staff announced the VRS Board of Trustees appointed Andrew Junkin to the Chief Investment Officer position. Staff reviewed investment duties and responsibilities of DCPAC. Staff provided the Committee with an overview of annual investments as of June 30, 2022, including the unbundled DC plans and investment options and the bundled TIAA ORPHE Retirement Choice (RC) investment menu options. Staff also informed the Committee of ongoing monitoring of DC investment trends and developments such as default investment options, investment menu structure, behavioral finance, investment advice and retirement income.

OTHER BUSINESS

Discussion of New Ideas

No new ideas were brought before the Committee.

2022 MEETINGS

Senator Bell confirmed the following DCPAC meeting date for 2022:

- December 1, 2022, at 1:00 p.m.

The ORPHE Annual Employer Update is scheduled for September 29, 2022. This is not a DCPAC Committee meeting; however, members may attend if interested.

Mr. Andrews thanked Senator Bell for his report.

Report of the Audit and Compliance Committee

The VRS Board of Trustees received the report of the Audit and Compliance Committee and placed it on file.

APPROVAL OF MINUTES

Mr. Montgomery began his report by noting the Committee approved the minutes of its June 16, 2022, meeting.

AUDIT REPORTS

The Committee received two audit reports.

- The review of *Disability Retirements* concluded disability retirement processes are operating as expected and disability payments are valid, accurate and complete. There were no formal recommendations as a result of this review.
- The review of *Fixed Income and Securities Lending Programs* determined that VRS provides appropriate oversight and monitoring of the programs. There were no formal recommendations as a result of this review.

INTERNAL AUDIT DEPARTMENT'S ANNUAL PROGRESS REPORTS FOR FISCAL YEAR 2022

The Committee received the following updates:

Internal Audit Director's Annual Report

The Audit Director provided the Committee with a summary of the Internal Audit Department's accomplishments over the past year as well as an overview of the department's initiatives and challenges for the coming fiscal year and the remainder of the long-range plan. She recognized the contributions of the Internal Audit team during the year.

The Audit Director explicitly confirmed the department and its staff are organizationally independent of the activities they examine. The Audit Director also discussed plans to augment the department's information technology audit resources to ensure the function will possess the appropriate qualifications to meet the needs of the proposed audit plan. The Audit Director also discussed the department's conformance with the Institute of Internal Auditors' *Standards* including review of the relevant charters and expected updates to *The Standards* effective 2024.

Annual Report on the Audit Recommendation Follow-Up System (ARFUS)

The annual ARFUS Report as of June 30, 2022 was presented. The Audit Director noted ARFUS contained ten internal recommendations, one represented as implemented. Internal Audit reviewed and released one recommendation, leaving nine outstanding as of June 30, 2022.

Annual Plan and Long-Range Plan Progress

The Audit Director discussed the annual plan results for the fiscal year ended June 30, 2022, along with the status of the long-range plan for the four years ending June 30, 2024. The Audit Director noted as of the conclusion of the second fiscal year of the long-range plan, modifications have been made to the remaining plan to accommodate the changing risk environment.

Proposed FY 2023 Annual Audit Plan

The Audit Director discussed the proposed annual audit plan for fiscal year 2023, which is derived from the approved long-range audit plan. The Committee reviewed the plan and voted to recommend approval of the request for board action to the full Board of Trustees.

Upon a motion by Mr. Montgomery, with a second by Mr. Bennett, the VRS Board of Trustees approved the following action:

RBA: Approve FY 2023 Audit Plan

Request for Board Action 2022-09-14: *The VRS Board of Trustees approves the proposed FY 2023 Annual Audit Plan.*

Quarterly Report on Fraud, Waste and Abuse Hotline Cases

It was noted there was one Fraud, Waste and Abuse Hotline complaint reported to Internal Audit via the Office of the State Inspector General during the period of May 1, 2022 through July 31, 2022. The case was unsubstantiated and closed.

Miscellaneous Updates

The Committee received the following miscellaneous updates:

Results of Agency Performance Outcomes and Agency Operational Measures

The Audit Director discussed the Internal Audit Department's review of management's representations regarding the Agency Performance Outcomes and Operational Measures for the fiscal year ended June 30, 2022, noting nothing came to its attention that indicated the outcomes and measures were not appropriately represented for the fiscal year.

Internal Audit's Review of Investment Variable Performance Program

The Audit Director noted the Internal Audit Department completed its review of the Investment Department Variable Performance Program's proposed compensation amounts and determined they were accurately computed in accordance with the authorized pay plan.

Management's Quarterly Travel Expense and Per Diem Report

The Committee received Management's Quarterly Travel Expense and Per Diem report.

Next Committee Meeting Date

The Committee's next meeting is scheduled for Thursday, December 8, 2022, at 10:00 a.m.

AUDIT DIRECTOR'S PERFORMANCE EVALUATION

The Committee went into closed session to review the Audit Director's performance for the fiscal year ended June 30, 2022.

Upon return to open meeting, the Committee voted to recommend approval of the action to the full Board.

Upon a motion by Mr. Montgomery, with a second by Chief Garrett, the VRS Board of Trustees approved the following action:

RBA: Internal Audit Director's Performance Review

Request for Board Action 2022-09-15: *The VRS Board of Trustees approves a 7% performance bonus for the Audit Director.*

Mr. Andrews thanked Mr. Montgomery for his report.

Report of the Administration and Personnel Committee

The VRS Board of Trustees received the report of the Administration and Personnel Committee and placed it on file.

APPROVAL OF MINUTES

Mr. Andrews began his report by noting the Committee approved the minutes of its June 14, 2022, meeting.

REVIEW ATTAINMENT OF FY 2022 AGENCY PERFORMANCE OUTCOMES (APOs) AND OPERATIONAL MEASURES

Michael Cooper, Chief Operating Officer, reviewed the results of the FY 2022 agency performance outcomes (APOs) and operational measures. Mr. Cooper noted that the agency had four APOs for the fiscal year, with a target of completing at least three. Staff met this goal by successfully completing all four APOs. In addition, there were sixteen operational measures for the year, of which thirteen had to be met to meet the target for the year. Staff successfully met its target for fifteen of the sixteen operational measures. The only measure not met for the year was the call abandonment rate.

The Committee recommended approval of the request for board action to the full Board of Trustees.

Upon a motion by Mr. Andrews, with a second by Mr. Montgomery, the VRS Board of Trustees approved the following action:

RBA: Attainment of FY 2022 APOs and Operational Measures (and corresponding lump-sum bonus)

Request for Board Action 2022-09-16: The VRS Board of Trustees approves the attainment of FY 2022 APOs and Operational Measures and a lump-sum bonus equal to 2.5% of salary for eligible administrative employees and eligible Investment Department operations and administration employees.

REVIEW PERFORMANCE BONUSES FOR ELIGIBLE ADMINISTRATIVE AND INVESTMENT OPERATIONS AND ADMINISTRATION EMPLOYEES

Paula Reid, Human Resources Director, presented a request for board action to approve the performance bonuses for eligible administrative and investment operations and administration employees. Eligible employees who earn an “exceptional” rating on their performance evaluation qualify for a 4% bonus. Employees who earn an “exceeds” rating on their performance evaluation are eligible for a 2% bonus. The bonus amount is based on their salary as of June 30, 2022.

The Committee recommended approval of the request for board action to the full Board of Trustees.

Upon a motion by Mr. Andrews, with a second by Dr. Gooden, the VRS Board of Trustees approved the following action:

RBA: Performance Bonuses for Eligible Administrative and Investment Operations and Administration Employees

Request for Board Action 2022-09-17: *The VRS Board of Trustees approves performance lump-sum bonuses for eligible administrative employees and eligible Investment Department operations and administration employees.*

BUDGET UPDATE

Jonathan Farmer, Budget and Performance Reporting Manager, presented the FY 2022 year-end budget results, explaining that VRS finished with an unexpended appropriation of approximately \$9.08 million, which will be returned to the Fund. Mr. Farmer next provided an update on the agency's FY 2023 budget, noting that expenses to date are in line with budgeted amounts.

INFORMATIONAL ITEM (INTERNAL AUDIT DIRECTOR'S PERFORMANCE REVIEW)

Mr. Andrews informed the Committee that the Audit and Compliance (A&C) Committee reviewed the Internal Audit Director's performance at its September 13, 2022 meeting. Each year, the A&C Committee reviews the Internal Audit Director's performance and makes a recommendation for a performance bonus to the Board of Trustees. A copy of the request for board action to provide a performance bonus in the amount of 7% was shared with the Committee for informational purposes.

OTHER BUSINESS (PROPOSED COMMITTEE NAME CHANGE)

Trish Bishop, VRS Director, presented information in support of a name change for the Administration and Personnel Committee. Ms. Bishop noted that after discussion with staff, research of other organizations and recognition of a desire to use more current language, staff recommends the Committee name be changed to Administration, Finance and Talent Management (AFT) Committee. The Committee agreed with the recommendation and directed staff to prepare necessary updates to the governance documents. Ms. Bishop noted that the changes will be presented to the A&P Committee at its next meeting, followed by two reviews by the Board as required by the Board Governance Policy.

COMPENSATION AND BENEFITS (CLOSED SESSION)

The Committee went into closed session to discuss benefits and compensation related to specific individuals.

Upon return to open meeting, the Committee recommended approval of two requests for board action to the full Board of Trustees.

Following a motion by Mr. Montgomery, with a second by Chief Garrett, the VRS Board of Trustees approved the following action:

RBA: FY 2022 Incentive Pay for Investment Professionals

Request for Board Action 2022-09-18: *The VRS Board of Trustees approves payment of an incentive amount of approximately \$7,343,564.18 for FY 2022 to VRS investment professionals as authorized by the Investment Professionals' Pay Plan.*

Internal Audit reviewed the proposed investment incentive compensation for the fiscal year that ended June 30, 2022 and found that the aggregate amount was accurately computed in accordance with the Investment Professionals' Pay Plan.

Mr. Andrews advised the Board has established this pay plan in order to attract, retain and provide incentive for investment professionals. VRS' total fund outperformed a traditional 60/40 passively managed stock/bond index by over 10% and exceeded the assumed rate of return for the three-, five- and 10-year periods. The investment team also achieved 600 basis points of added value above the benchmark and, in light of market conditions for most of 2022, including inflation, war and supply chain disruptions, the team's performance has been outstanding. As reported by CEM, VRS' skilled negotiation of external investment management costs and effective cost management results in approximately \$61 million in savings per year, in addition to saving roughly \$40.9 million in external investment management fees as approximately one-third of plan assets are managed in-house. Mr. Andrews advised the VRS trust fund amount is its largest to date and the pay plan is essential in providing incentives to retain the expertise to manage a fund of this size.

Upon a motion by Mr. Montgomery, with a second by Chief Garrett, the VRS Board of Trustees approved the following action:

RBA: VRS Director's Performance Review

Request for Board Action 2022-09-19: The VRS Board of Trustees approves a 5% performance bonus for the VRS Director payable on October 14, 2022 and a supplemental payment of \$85,000 made on December 1, 2022 as authorized in the 2022 Appropriation Act.

Mr. Andrews advised VRS continues to advance in providing members and retirees convenient and effective ways to plan for their future and manage benefits. Mr. Andrews also commended staff for successfully navigating to a hybrid work environment after two years of remote work and accomplishing all four APOs and 15 of the 16 operational measures for the year. In addition, VRS earned several national and local awards that reflect the tremendous work and dedication of VRS staff on a day-to-day basis.

Operational Update Series: Enterprise Risk Management

Next, as part of the ongoing Operational Update Series, Ms. Bishop introduced Michael Cooper, Chief Operating Officer, who presented an update on VRS' Enterprise Risk Management (ERM) program. Mr. Cooper reviewed the key principles and benefits of ERM that involve looking at risk beyond the traditional sense, including looking at risk from a positive perspective, in order to leverage risk and identify opportunities and gain efficiencies.

Following its establishment, the ERM staff committee developed a risk portfolio and assessment implementation strategy centered around risk identification, assessment, response, monitoring and management. Mr. Cooper advised staff developed and executed a risk response plan based on the results of the assessment, as well as strategies for monitoring and reporting risk. The program also incorporates two-way communication and feedback between the Board and committees and the various roles within the agency.

Lastly, Mr. Cooper provided an overview of the program's next steps, which include increasing the understanding of ERM across the agency by providing education and training for VRS staff.

Mr. Andrews thanked Mr. Cooper for his presentation.

Signature and Custodial Authorization Resolutions

Ms. Bishop presented the Resolution for Master Custodial Services and the Resolution for Payment of Retirement System Funds in the State Treasury and Signing Official Documents. The documents set out the Board's intentions regarding authority to sign documents.

Ms. Bishop noted the changes to the documents reflect new roles and new team members. Leslie Weldon will be added as the new Chief Financial Officer following Mr. Faison's signature authority expiration and retirement on December 31, 2022. Andrew Junkin will be added as the new Chief Investment Officer upon Mr. Schmitz's signature authority expiration and retirement on January 1, 2023. In addition, Robert Robinson, Procurement Manager, and Richard Budaji, General Services Administrator, are added in keeping with their duties for executing purchase orders.

Policy Update

Cindy Wilkinson, Director of Policy, Planning and Compliance, presented updates to the Freedom of Information Act (FOIA) Electronic Meeting Policy. Ms. Wilkinson advised that the General Assembly adopted amendments to FOIA, effective September 1, 2022, that change the methods by which public bodies can meet remotely or, in a new option, meet virtually when no members are physically present. Ms. Wilkinson reviewed the changes and updates to the policy and discussed the circumstances under which members of public bodies may participate remotely.

Upon a motion by Mr. Montgomery, with a second by Mr. Disharoon, the VRS Board of Trustees approved the following action:

RBA: Adopt a revised "FOIA Electronic Meeting Attendance Policy."

Request for Board Action 2022-09-20: The Board adopts a revised "FOIA Electronic Meeting Attendance Policy."

Mr. Andrews thanked Ms. Wilkinson for her presentation.

Report of the Director

Ms. Bishop, Director, began her report with an update on the agency road map for FY 2023, noting all projects are progressing as planned, as well as a review of New Coverage Elections.

Ms. Bishop announced that NAGDCA presented VRS with two Leadership Recognition Awards for the SmartStep Auto-Increase Awareness Campaign in the categories of COVID-19 Response and Participant Education and Communication. In addition, the campaign received the 2022 NAGDCA Art Caple President's Award, which recognizes a public sector retirement plan that has championed a participant-first mentality.

The VRS Member Guide received a Capital Award in the 2022 Virginia Public Relations competition from the Richmond Chapter of the Public Relations Society of America (PRSA). This award recognizes outstanding public relations tactics.

Lastly, Ms. Bishop advised staff will be polling Board members in the coming weeks for the 2023 meeting schedule.

Mr. Andrews thanked Ms. Bishop for her report.

Information Technology and Litigation (Closed Session)

Upon a motion by Mr. Montgomery, with a second by Mr. Hayes, the Virginia Retirement System Board of Trustees convened a closed meeting under the Virginia Freedom of Information Act for the purpose of (a) consultation with legal counsel about actual or probable litigation pursuant to the exemption contained in Virginia Code § 2.2-3711(A)(7), and (b) discussion of an information technology system or software program where discussion in an open meeting would jeopardize the security of such information technology system or software program, pursuant to the exemption contained in Virginia Code § 2.2-3711(A)(19).

Upon return to open meeting, Mr. Montgomery moved, with a second by Dr. Gooden, the following resolution:

WHEREAS, the Virginia Retirement System Board of Trustees convened a closed meeting on this date pursuant to an affirmative recorded vote and in accordance with the provisions of the Virginia Freedom of Information Act; and

WHEREAS, § 2.2-3712 of the *Code of Virginia* requires a certification by the Board that such closed meeting was conducted in conformity with Virginia law;

NOW, THEREFORE, BE IT RESOLVED, the Board certifies that, to the best of each member's knowledge, (i) only public business matters lawfully exempted from open meeting requirements under this chapter were discussed in the closed meeting to which this certification resolution applies, and (ii) only such public business matters as were identified in the motion by which the closed meeting was convened were heard, discussed or considered by the Board.

The Board approved the resolution upon the following roll call vote:

Mr. Bell: Aye
Mr. Bennett: Aye
Mr. Disharoon: Aye
Chief Garrett: Aye
Dr. Gooden: Aye
Mr. Hayes: Aye
Mr. Montgomery: Aye
Ms. Pantele: Aye
Mr. Andrews: Aye

Other Business

Lastly, Mr. Andrews reviewed the following meeting schedule:

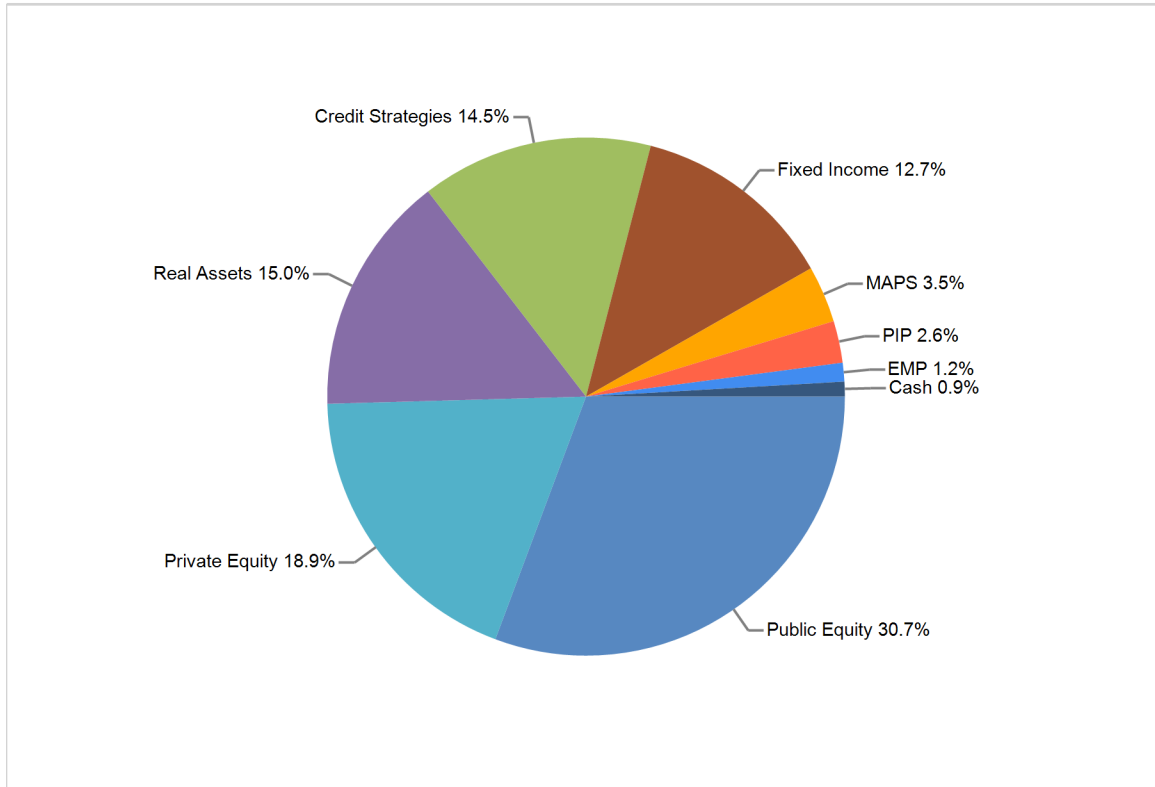
- Benefits and Actuarial Committee – October 17 at 1:00 p.m.
- Administration and Personnel Committee – October 18 at 11:00 a.m.
- Board of Trustees – October 18 at 1:00 p.m.

Adjournment

There being no further business and following a motion by Mr. Montgomery, with a second by Mr. Disharoon, the VRS Board of Trustees agreed to adjourn the meeting at 3:37 p.m.

Chair

Secretary



	<u>Current \$Bil</u>	<u>Current Weight</u>	<u>Policy Weight</u>	<u>Variance</u>	<u>Allowable Range</u>		<u>Internal %</u>
Total Fund	101.6						27.0%
Public Equity	31.2	30.7%	34.0%	-3.3%	-5%	+5%	43.4%
Fixed Income	12.9	12.7%	15.0%	-2.3%	-3%	+5%	96.3%
Credit Strategies	14.7	14.5%	14.0%	0.5%	-5%	+5%	
RS Credit	4.4	4.3%	5.6%	-1.3%			
NRS Credit	10.3	10.2%	8.4%	1.8%			
Real Assets	15.2	15.0%	14.0%	1.0%	-5%	+5%	9.5%
Public RE	1.4	1.4%					99.9%
Private RE	9.2	9.1%					
Other RA	4.6	4.5%					
Private Equity	19.2	18.9%	16.0%	2.9%	-5%	+5%	
MAPS	3.6	3.5%	4.0%	-0.5%	-2%	+2%	
DSTRAT	1.8	1.8%					
RBI	1.8	1.8%					0.6%
PIP	2.7	2.6%	2.0%	0.6%	-2%	+2%	
EMP	1.2	1.2%	0.0%	1.2%		+3%	
Cash	0.9	0.9%	1.0%	-0.1%	-1%	+4%	

	<u>Current \$Bil</u>	<u>Current Weight</u>	<u>Policy Limit</u>
Hedge Funds	9.9	9.7%	15.0%

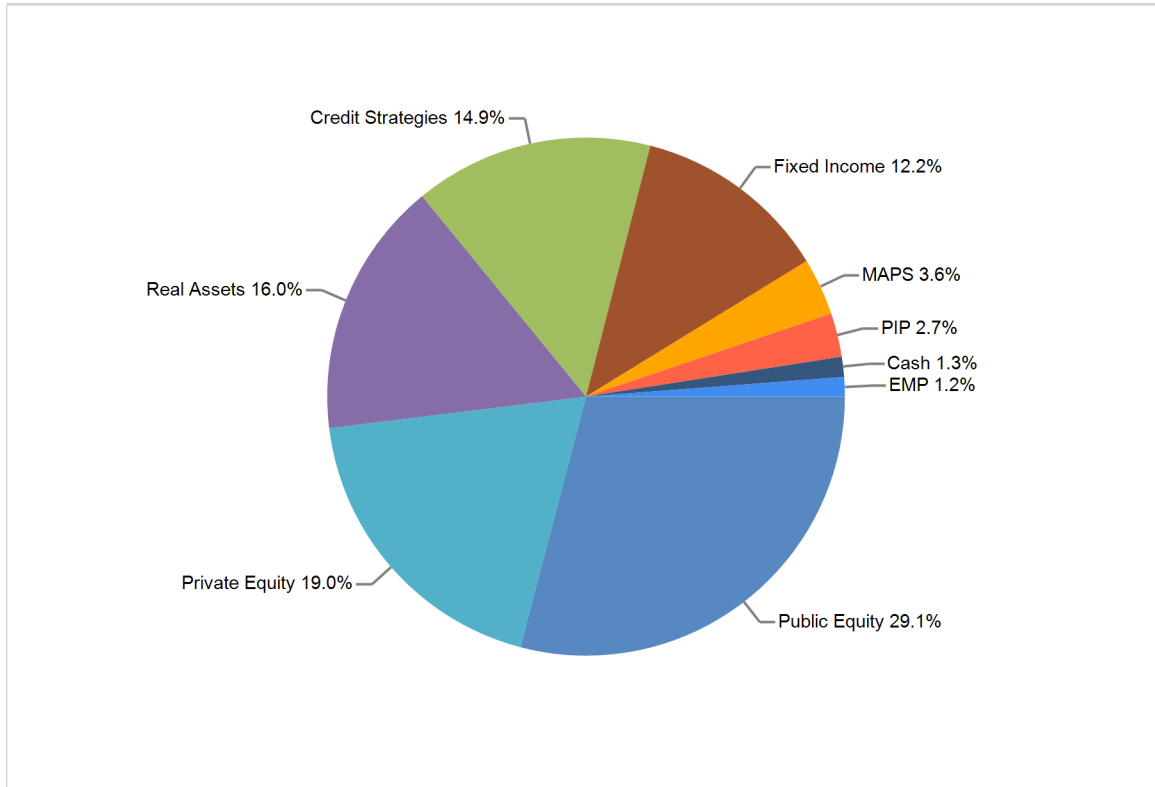
<u>Tracking Error</u>	
3Yr-Total Fund:	1.98%
3Yr-Total Public:	1.73%
5Yr-Total Fund:	1.80%
5Yr-Total Public:	1.42%

*Total Fund includes the following amt held by the Treasurer of VA: \$ 298 million

• The values shown for each asset class on this report may differ from the VRS Monthly Performance Report due to adjustments related to derivative positions in the Rebalance Account, pending transactions, and certain accruals. The values on this report are a more descriptive representation of the Virginia Retirement System's true economic exposure to each asset class.(5 adjustments applied)

*Total Fund and Total Public annualized tracking error is calculated using compounded quarterly returns as of 6/30/2022

* Differences in totals are due to rounding.



	<u>Current \$Bil</u>	<u>Current Weight</u>	<u>Policy Weight</u>	<u>Variance</u>	<u>Allowable Range</u>		<u>Internal %</u>
Total Fund	97.1						26.4%
Public Equity	28.2	29.1%	34.0%	-4.9%	-5%	+5%	45.5%
Fixed Income	11.9	12.2%	15.0%	-2.8%	-3%	+5%	96.3%
Credit Strategies	14.5	14.9%	14.0%	0.9%	-5%	+5%	
RS Credit	3.9	4.0%	5.6%	-1.6%			
NRS Credit	10.6	10.9%	8.4%	2.5%			
Real Assets	15.6	16.0%	14.0%	2.0%	-5%	+5%	7.9%
Public RE	1.2	1.3%					99.9%
Private RE	9.6	9.9%					
Other RA	4.7	4.9%					
Private Equity	18.4	19.0%	16.0%	3.0%	-5%	+5%	
MAPS	3.5	3.6%	4.0%	-0.4%	-2%	+2%	
DSTRAT	1.7	1.7%					5.3%
RBI	1.8	1.9%					0.4%
PIP	2.7	2.7%	2.0%	0.7%	-2%	+2%	
EMP	1.2	1.2%	0.0%	1.2%		+3%	
Cash	1.2	1.3%	1.0%	0.3%	-1%	+4%	

	<u>Current \$Bil</u>	<u>Current Weight</u>	<u>Policy Limit</u>
Hedge Funds	9.4	9.7%	15.0%

<u>Tracking Error</u>	
3Yr-Total Fund:	2.16%
3Yr-Total Public:	1.71%
5Yr-Total Fund:	2.02%
5Yr-Total Public:	1.42%

*Total Fund includes the following amt held by the Treasurer of VA: \$ 284 million

• The values shown for each asset class on this report may reflect adjustments related to derivative positions in the Rebalance Account, pending transactions and certain accruals, in order to provide a more descriptive representation of the true economic exposure to each asset class (6 adjustments applied)

*Total Fund and Total Public annualized tracking error is calculated using compounded quarterly returns as of 9/30/2022

* Differences in totals are due to rounding.

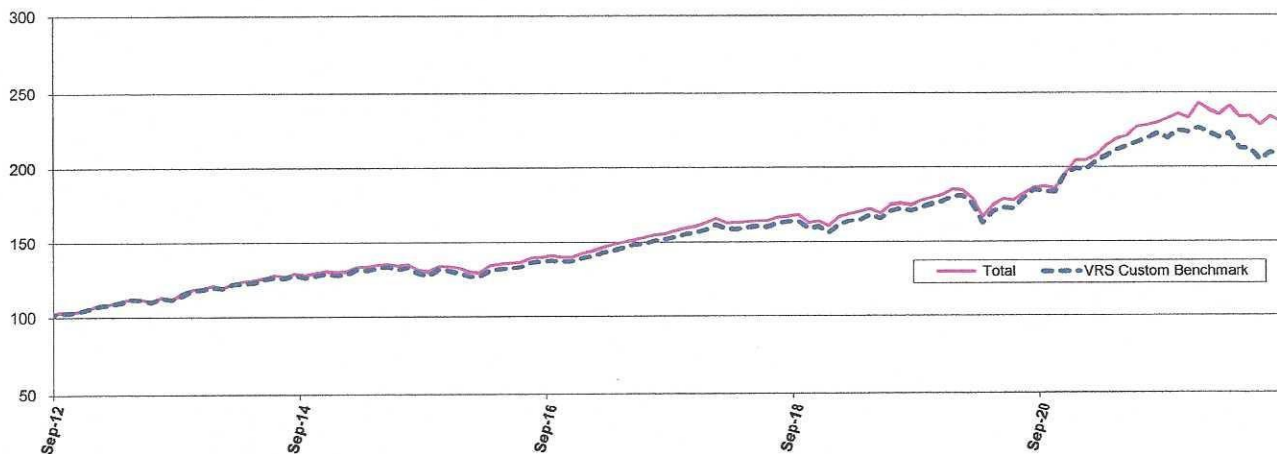
PERFORMANCE SUMMARY
Rolling Periods Ending
August 31, 2022



TOTAL FUND PERFORMANCE

	10 Yr	5 Yr	3 Yr	1 Yr	Qtr	Month	Fiscal YTD	Cal YTD	Market Value (\$MM)
Total Public Equity Strategies	8.9	6.4	7.7	-15.0	-5.5	-3.2	2.7	-16.2	30,283
<i>Benchmark</i>	8.9	7.0	8.0	-15.9	-5.5	-3.5	3.4	-17.5	
Total Fixed Income	2.1	1.5	-0.7	-11.6	-2.2	-2.5	-0.1	-10.9	12,622
<i>Benchmark</i>	1.3	0.5	-2.1	-12.0	-2.2	-2.7	-0.1	-11.2	
Total Credit Strategies	6.5	6.2	6.8	2.0	-0.3	-0.3	1.3	-1.4	14,718
<i>Benchmark</i>	4.7	3.6	2.5	-4.1	-0.4	-0.1	3.2	-5.1	
Total Real Assets	10.9	10.0	11.0	21.3	4.7	-0.7	0.2	10.8	15,235
<i>Benchmark</i>	9.2	8.4	9.3	18.0	3.6	0.6	2.6	11.4	
Total Private Equity	17.4	21.0	25.4	27.1	0.3	-0.1	-0.3	4.9	19,174
<i>Benchmark</i>	13.5	11.9	13.4	-7.2	-5.9	0.1	-7.8	-7.4	
Total Private Investment Partnerships	n/a	11.1	12.7	17.0	1.6	0.0	0.0	4.8	2,655
<i>Benchmark</i>	n/a	9.1	9.5	3.3	-0.5	0.3	-0.4	0.7	
Total Multi-Asset Public Strategies	n/a	n/a	4.3	-3.9	-2.8	-0.9	1.8	-5.6	3,601
<i>Benchmark</i>	n/a	n/a	3.7	-8.3	-2.7	-2.2	1.6	-9.3	
Total Fund	8.6	8.2	9.6	0.2	-1.7	-1.6	0.9	-5.1	101,648
<i>VRS Custom Benchmark</i>	7.4	6.3	6.4	-7.2	-2.8	-1.6	0.8	-8.8	

10-Year Performance
Indexed to 100



Effective July 2013, the VRS Custom Benchmark is a blend of the Asset Class Benchmarks at policy weights.

The VRS Cash Account, the Treasurer Short-Term Investment Account, the VRS Rebalancing Account, transition activity and accounts with market values of less than \$1 million are included in the Total Fund's market value. Differences in market value totals are due to rounding.

Total Fund Tracking Error

Figure 1: Policy Tracking Error Rolling Three Year - Plan (as of 6/30/2022)

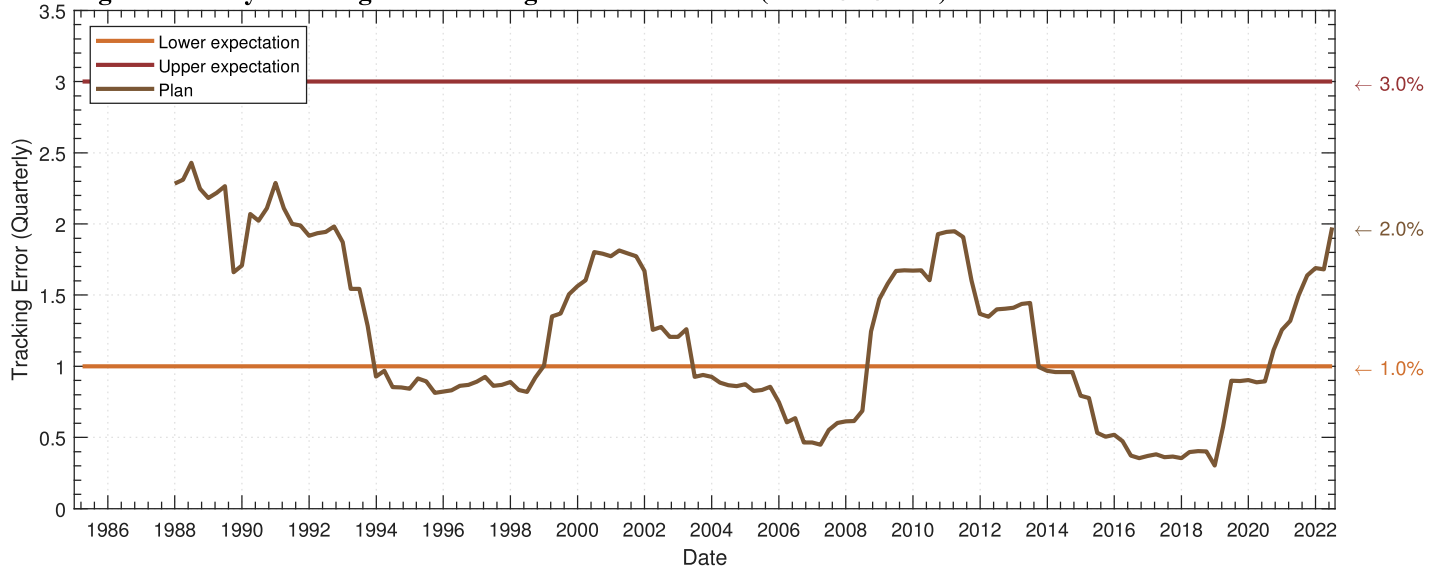
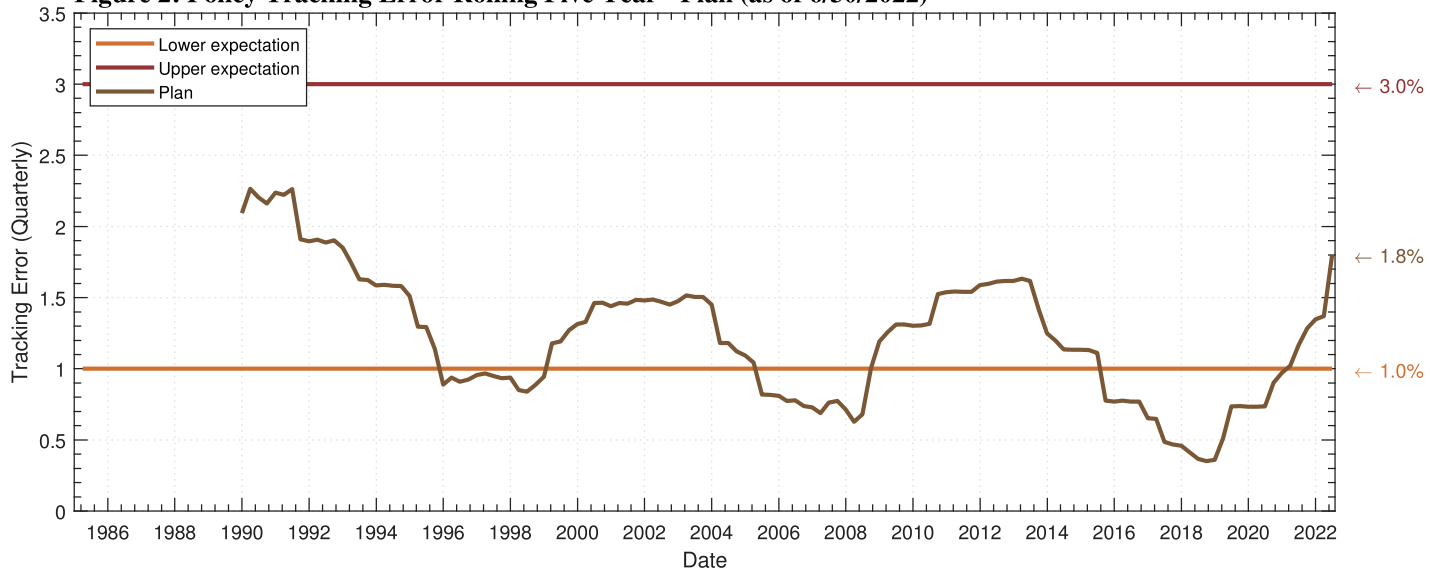


Figure 2: Policy Tracking Error Rolling Five Year - Plan (as of 6/30/2022)



The VRS Defined Benefit Plan Investment Policy Statement established the total fund tracking error range as the allowable observed tracking error calculated quarterly using 5 years of history.

Program	Action	Effective Date	Commitment/ Current Value	Funding/ Defunding Period	Description
Credit Strategies	Terminated	09/30/2022	\$510 Million	Immediate	PIMCO HY – A separate account invested in high yield bonds.
Credit Strategies	Hired	10/04/2022	\$250 Million	3 Years	Apollo EPF IV – A special situations strategy targeting asset-backed investment opportunities in the European market.
Real Assets	Hired	09/30/2022	€100 Million	5 Years	Antin Infrastructure Partners V – A closed-end fund investing in diversified infrastructure deals in Europe as well as the United States.

VRS Investment Department
DIME Quarterly Report
Activity for Quarter Ending September 30, 2022

Investment Program	Activity	Manager Name	Description	VRS Action
Public Equity	Virtual Manager Meeting	Alpine Peaks Capital (women-owned firm) ¹	Manager runs long/short strategy that focuses on small and mid-cap companies.	Staff had an update meeting with this manager to discuss the firm and their strategies.
Public Equity	Manager Meeting	Axiom Investors (women-owned firm) ²	Manager focused on dynamic growth equity investing.	Staff had an update meeting with this manager to discuss the firm and their strategy.
Public Equity	Manager Meeting	Doma Perpetual (minority-owned firm) ¹	Manager focused on a long-only global strategy.	Staff had an update meeting with this manager to discuss the firm and their strategy.
Public Equity	Virtual Manager Meeting	Fithian Investment Advisors (women-owned firm) ¹	Manager focused on a long-only global strategy.	Staff had a meeting with the manager to discuss their firm and strategy.
Public Equity	Virtual Manager Meeting	Sit Investment Associates, Inc. (minority-owned firm) ¹	Manager focused on domestic and international growth equities.	Staff had an update meeting with this manager to discuss the firm and their strategy.
Public Equity	Manager Meeting	Yulan Capital Management (women-owned firm) ¹	Manager focused on China driven Asia long-short equity investing.	Staff had a meeting with the manager to discuss their firm and strategy.
Public Equity	On-Going Monitoring of Current VRS Manager	Ariel Global (minority and women-owned firm) ¹	Current VRS global equity manager.	Staff performed on-going due diligence and monitoring of this current VRS minority and women-owned manager during the quarter.
Public Equity	On-Going Monitoring of Current VRS Manager	Advent Capital Management (minority-owned firm) ¹	Current VRS convertible bond manager.	Staff performed on-going due diligence and monitoring of this current VRS minority manager during the quarter.

VRS Investment Department
DIME Quarterly Report
Activity for Quarter Ending September 30, 2022

Investment Program	Activity	Manager Name	Description	VRS Action
Public Equity and Credit Strategies	Periodic Update Communication with Consultant	N/A	Aon Hewitt Investment Consulting is the consultant used by these two investment programs.	Periodic communication to review the DIME monitoring activity done on behalf of VRS as well as industry trends.
Credit Strategies	Materials Review	Brinley Partners (women-owned firm) ¹	Manager invests in secured credit, unsecured credit and preferred equity across various industries.	Staff reviewed materials.
Credit Strategies	Virtual Manager Meeting	Vista Equity Partners (minority and women-owned firm) ¹	Manager focused on customized debt and structured equity financing to enterprise software, data and technology-enabled businesses.	Staff reviewed materials and had a meeting with the manager to discuss their firm and strategy.
Credit Strategies and Risk-Based Investments	Periodic Communication with Fund-of-Fund Manager	N/A	Aksia is the consultant used by these two investment programs.	Periodic communication to review DIME and other emerging managers along with other opportunities more broadly.
Risk-Based Investments	Telephone Call with Manager	Gladius Capital Management (minority-owned firm) ¹	A provider of derivative based solutions to manage risks.	Staff had a call with this manager to discuss their firm and strategies.
Risk-Based Investments	Telephone Call with Manager	Systematica Investments (women-owned firm) ¹	A multi-asset class manager.	Staff had a call with this manager to discuss their firm and strategies.
Dynamic Strategies	Virtual Manager Meeting	Nipun Capital (minority and women-owned firm) ¹	Manager focused on emerging markets strategy.	Staff had a meeting with the manager to discuss their firm and strategy.
Real Assets	Virtual Manager Meeting	Aiga Capital Partners (minority-owned firm) ²	Manager focused on making structured equity and debt investments in climate focused development companies/deals.	Staff held an introductory meeting with this manager to discuss their background, company, current fundraise initiative and market update.

VRS Investment Department
DIME Quarterly Report
Activity for Quarter Ending September 30, 2022

Investment Program	Activity	Manager Name	Description	VRS Action
Real Assets	Virtual Manager Meeting	Ember Infrastructure (women-owned firm) ¹	Manager focused on middle market infrastructure in the energy transition space.	Staff held an introductory meeting with this manager to discuss their background, company, current fundraise initiative and market update.
Real Assets	Telephone Call with Manager	Envra (women-owned firm) ¹	Manager focused on infrastructure and infrastructure related technology investments in small and mid-sized markets.	Staff held an introductory call with this manager to discuss their background, company, current fundraise initiative and market update.
Real Assets	Telephone Call with Manager	Homestead Capital (minority-owned firm) ²	Manager focused on value-add farmland investing, both row crops and permanent plantings.	Staff held an update call with this manager to discuss their existing portfolio and performance, fundraise progress, and current pipeline.
Real Assets	Telephone Call with Manager	Urban Energy (women-owned firm) ¹	Manager invests in upstream energy throughout specific U.S. basins.	Staff held an introductory call with this manager to discuss their background, company, current fundraise initiative and market update.
Real Assets	On-Going Monitoring of Current VRS Manager	Artemis Real Estate Partners (women-owned firm) ¹	Current VRS real estate manager.	Staff performed on-going due diligence and monitoring of this current VRS women-owned manager during the quarter.
Real Assets	On-Going Monitoring of Current VRS Manager	Capri EGM (minority-owned firm) ¹	Current VRS real estate manager.	Staff performed on-going due diligence and monitoring of this current VRS minority-owned manager during the quarter.
Real Assets	On-Going Monitoring of Current VRS Manager	Grain Management (minority-owned firm) ¹	Current VRS infrastructure manager.	Staff performed on-going due diligence and monitoring of this current VRS minority-owned manager during the quarter.
Real Assets	On-Going Monitoring of Current VRS Manager	Pantheon Ventures	Current VRS infrastructure and natural resource fund-of-funds manager.	Staff had periodic communication with this manager to discuss potential DIME firms in their market.

VRS Investment Department
DIME Quarterly Report
Activity for Quarter Ending September 30, 2022

Investment Program	Activity	Manager Name	Description	VRS Action
Real Assets	On-Going Monitoring of Current VRS Manager	Pritzker Realty Group (women-owned firm) ¹	Current VRS real estate manager.	Staff performed on-going due diligence and monitoring of this current VRS women-owned manager during the quarter.
Real Assets	On-Going Monitoring of Current VRS Manager	Tristan Capital Partners (minority-owned firm) ¹	Current VRS real estate manager.	Staff performed on-going due diligence and monitoring of this current VRS minority-owned manager during the quarter.
Real Assets	Periodic Update Communication with Consultant	N/A	The Townsend Group is the consultant used by Real Assets.	Periodic communication to review the DIME monitoring activity done on behalf of VRS as well as real estate and infrastructure industry trends.
Private Equity	Virtual Manager Meeting	1315 Capital (women-owned firm) ¹	An expansion and growth middle market manager focusing on commercial-stage healthcare services, medical technology, and therapeutics / pharmaceutical services.	Staff had a meeting with this manager during the quarter.
Private Equity	Virtual Manager Meeting	Eden Capital (women-owned firm) ¹	A middle market buyout manager targeting technology, business services, and education companies.	Staff had a meeting with this manager during the quarter.
Private Equity	Virtual Manager Meeting	iAngels (women-owned firm) ¹	An Israeli-based venture manager targeting tech startup and scaleup investments originated in Israel.	Staff had a meeting with this manager during the quarter.
Private Equity	Virtual Manager Meeting	Relevance Ventures (minority-owned firm) ¹	An early-stage venture manager focusing on comprehensive social, environmental, and individual wellness investments.	Staff had a meeting with this manager during the quarter.
Private Equity	Virtual Manager Meeting	Trident Management LLC (minority-owned firm) ¹	A control-oriented buyout firm investing with independent sponsors as operating partners to acquire US based companies.	Staff had a meeting with this manager during the quarter.

VRS Investment Department
DIME Quarterly Report
Activity for Quarter Ending September 30, 2022

Investment Program	Activity	Manager Name	Description	VRS Action
Private Equity	Virtual Manager Meeting	Vistria Group (minority-owned firm) ¹	A middle market buyout manager targeting education, healthcare, and financial services companies.	Staff had a meeting with this manager during the quarter.
Private Equity	On-Going Monitoring of Current VRS Manager	Asia Alternatives (minority and women-owned firm) ¹	A fund-of-funds manager focusing on alternative investments in Asia.	Staff had a meeting with this manager during the quarter.
Private Equity	On-Going Monitoring of Current VRS Manager	Clearlake Capital Group (minority-owned firm) ¹	A private equity fund investing in special situations and distressed opportunities in small and medium-sized companies.	Staff had a meeting with this manager during the quarter.
Private Equity	On-Going Monitoring of Current VRS Manager	SIRIS Capital (minority-owned firm) ¹	A middle market buyout firm making control investments in data/telecommunications, technology and technology-enabled business service companies in North America.	Staff had a meeting with this manager during the quarter.
Private Equity	On-Going Monitoring of Current VRS Manager	Sycamore Partners (minority-owned firm) ¹	Middle market buyout fund targeting consumer and retail companies.	Staff had a meeting with this manager during the quarter.
Private Equity	On-Going Monitoring of Current VRS Manager	TSG Consumer Partners (women-owned firm) ²	Growth fund investing exclusively in middle market consumer-branded companies.	Staff had a meeting with this manager during the quarter.
Private Equity	On-Going Monitoring of Current VRS Manager	Veritas Capital (minority-owned firm) ²	Middle market buyout fund targeting primarily technology or technology-enabled solutions to government.	Staff had a meeting with this manager during the quarter.

VRS Investment Department
DIME Quarterly Report
Activity for Quarter Ending September 30, 2022

Investment Program	Activity	Manager Name	Description	VRS Action
Private Equity	On-Going Monitoring of Current VRS Manager	Vista Equity Partners (minority and women-owned firm) ¹	A large market buyout fund targeting enterprise software companies.	Staff had a meeting with this manager during the quarter.
Private Equity	Communication with Trade Association	N/A	The National Association of Investment Companies (NAIC) is the trade association representing private equity firms whose investment strategies focus on emerging domestic and global mid-market opportunities.	Staff attended a reception with this trade association during the quarter.
Private Equity	Periodic Update Communication with Consultant	N/A	Grosvenor Capital Management Customized Fund Investment Group is the consultant used by Private Equity.	Periodic communication to review the DIME monitoring activity done on behalf of VRS as well as industry trends.
Fixed Income	On-Going Monitoring of Current VRS Manager	Payden & Rygel (women-owned firm) ¹	Current VRS emerging market debt manager.	Staff had various interactions with this current VRS women-owned manager during the quarter.

Index:

- 1 – The manager is considered Diverse Investment Management Engagement (DIME) under the Commonwealth of Virginia definition, which defines ownership threshold of 51% or more.
- 2 – The manager is considered DIME under the definition that considers industry best practices, and defines an ownership threshold of greater than or equal to 33% and less than 51% of firm ownership or carry.

VRS Investment Department
Quarterly External Investment Manager Referral Report
Activity for Quarter Ending September 30, 2022

Investment Program	Type of Contact	Investment Manager Name	Official Making Referral	VRS Action
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No activity to report this quarter.

Approve additional changes to Defined Benefit Plan Strategic Asset Allocation and Allowable Ranges.

Requested Action

The VRS Board of Trustees approves additional changes to update the Defined Benefit Plan Strategic Asset Allocation and Allowable Ranges to also reflect two high-level rebalancing ranges, one for equity exposures (public and private equity) and one for fixed income exposures (fixed income and cash), in addition to the previously approved Board target asset mix and hedge funds policy limit.

Description/Background

Board Strategic Asset Allocation and Allowable Ranges. At the June 23, 2022 Board meeting, the Board approved the FY 2023 individual asset class target exposures and allowable ranges. In addition, at the June 19, 2015 Board meeting, the Board approved an overall hedge funds policy limit of 15%. The CIO is not recommending any changes to these two items.

The CIO is recommending the addition of two high-level rebalancing ranges, one for equity exposures (public and private equity) and one for fixed income exposures (fixed income and cash).

The high-level rebalancing ranges will provide the CIO flexibility to exceed the individual equity and fixed income related allowable ranges if a deviation is caused by market actions or Fund liquidity needs, if the CIO believes bringing an asset class back within the allowable range would not be economically prudent, and, if staff has not taken tactical action to intentionally cause the applicable asset class to be out of compliance.

Asset Class	FY 2023 Target	Allowable Ranges	
		Min	Max
Public Equity	34%	-5%	+5%
Fixed Income	15%	-3%	+5%
Credit Strategies	14%	-5%	+5%
Real Assets	14%	-5%	+5%
Private Equity	16%	-5%	+5%
PIP	2%	-2%	+2%
MAPS	4%	-2%	+2%
Exposure Management	0%	-	+3%
Cash	1%	-1%	+4%
Total Fund	100%		

	Policy Limit
Hedge Funds	15.0%

High-Level Exposure	FY 2023 High-Level Target	High-Level Allowable Ranges	
		Min	Max
Total Equity (Public and Private Equity)	50%	-10%	+10%
Fixed Income and Cash	16%	-4%	+9%

Staff will not, by its tactical actions, underweight or overweight any individual asset class beyond the minimum and maximum allowable ranges. However, market action or Fund liquidity needs could cause an individual asset class to be temporarily below the minimum allowable range or above the maximum allowable range. In such rare cases, using the high-level rebalancing ranges, the CIO will have the flexibility to exceed the individual allowable ranges if the deviation is related to market actions or Fund liquidity needs, if the CIO believes bringing an individual asset class back within its allowable range would not be economically prudent. If, however, the CIO determines an individual asset class needs to be brought back into its allowable range, staff will establish an action plan. In any event, the CIO will communicate the deviation to the Board on a timely basis.

Rationale for Requested Action

Market volatility and related market actions, as well as Fund liquidity needs, may cause individual equity and/or fixed income related asset classes to exceed their allowable ranges. However, the overall equity and/or fixed income exposure may be within the aggregated allowable range. The addition of two high-level rebalancing ranges, one for equity exposures (public and private equity) and one for fixed income exposures (fixed income and cash), gives the CIO flexibility to manage the rebalancing process in the best economic interests of the total fund given the current market conditions and allows for easier management of the asset allocation.

Authority for Requested Action

The Board is authorized to approve these recommendations pursuant to the provisions of *Code of Virginia* §§ 51.1-124.22 and -124.30.

The above action is approved.

A. Scott Andrews, Chair
VRS Board of Trustees

Date

Report

The Benefits and Actuarial Committee met on October 17, 2022, and took up the following matters:

APPROVAL OF MINUTES

The Committee approved the minutes of its April 19, 2022, meeting.

ELECTION OF COMMITTEE VICE CHAIR

The Committee unanimously approved the nomination of John Bennett to serve as Vice Chairman.

GABRIEL, ROEDER, SMITH & COMPANY (GRS) 2022 ACTUARIAL VALUATION RESULTS FOR FIVE STATEWIDE RETIREMENT PLANS, GROUP LIFE INSURANCE, AND STATE AND TEACHER RETIREE HEALTH INSURANCE CREDIT PLANS

Jim Anderson and Becky Stouffer from the VRS plan actuary, Gabriel, Roeder, Smith & Company (GRS), presented the June 30, 2022, actuarial valuations for the Five Statewide Retirement Plans, Group Life Insurance and the State and Teacher Health Insurance Credit. The VRS actuary conducts annual valuations as of the close of the fiscal year (June 30). In odd-numbered years the valuations are used to establish employer contribution rates. The results in even-numbered years are shared with the Board of Trustees to inform the Board of any emerging trends or indications of the magnitude and direction of contribution rates.

The market value return for the total fund of 0.60% fell short of the long-term assumed rate of return of 6.75%. Despite lower-than-expected returns for fiscal year 2022, recognition of prior gains led to improved funded status for all pension plans on an actuarial basis. In addition, the \$750 million one-time infusion from the 2022 Appropriation Act served to increase funded status by approximately 0.80% for most plans. Fiscal year 2022 also included higher than expected cost-of-living increases and pay increases for most employer groups exceeded assumed increases which led to higher-than-expected liabilities.

The OPEB plans also benefited from the receipt of a portion of the \$750 million one-time contribution, which increased the funded status by approximately 0.85% for the HIC plans and GLI. Each OPEB plan saw an increase in funded status similar to pensions.

Due to a recently implemented allocation methodology for the HIC benefits, the State and Teacher HIC plans saw a reduction in the employer cost for the informational valuation. The new methodology allocates a prorated portion of HIC liability to each employer a member worked for that offered the HIC benefit.

The group life plan saw a slight increase in the employer rate mainly due to an increase in the active life coverage rate from 14.7 cents per \$1,000 of coverage to 16.2 cents per \$1,000 that became effective on July 1, 2022.

GRS also provided a summary of the recently modified Actuarial Standards of Practice 4 (ASOP 4) which will require plans to disclose plan liabilities using a low-default-risk obligation measure (LDRM). While

this requirement will not impact contributions or funding, it is an item to be added to the Risk Assessment section of the reports beginning in 2023.

The Committee recommended approval of the following action to the full Board of Trustees:

Request for Board Action: *The Virginia Retirement System Board of Trustees accepts the June 30, 2022, Actuarial Valuations conducted by the VRS plan actuary, Gabriel, Roeder, Smith & Company, for the Five Statewide Retirement Plans, Group Life Insurance, and the Health Insurance Credit plans for both State and Teachers.*

FUNDING POLICY AMENDMENTS

Following the GRS presentation of the actuarial valuations, Rory Badura, Senior Staff Actuary, presented the proposed amendments to the VRS Funding Policy. The Funding Policy memorializes the methods by which the Board has elected to govern required funding for pension and OPEB plans with the goal of ensuring that future contributions, along with current asset plans, are sufficient to provide for all benefits expected to be paid when due.

Staff is proposing modifications to the Funding Policy to explicitly set out amortization periods for unfunded liabilities generated by elected plan amendments to be 10 years rather than 20 years in the amortization period section of the policy. For HIC elections, any employer would be required to pay an initial contribution equal to the greater of two years of expected benefit payments or the amount required to reach at least 25% funded for its HIC plan, with the remainder of the unfunded liability amortized over no more than 10 years.

The proposed changes ensure that employers electing the HIC have initial funds available to pay benefits and to establish at least a minimum funded status at the outset and that the amortization period for all elected plan amendments be shortened to 10 years. This change mirrors the current requirement that an employer electing to participate in VRS must be at least 75% funded for pension benefits at the time of the election, and that any benefit enhancements to not reduce the funded status below 75%.

The Committee recommended approval of the following action to the full Board of Trustees:

Request for Board Action: *The Board approves the changes to the VRS Funding Policy Statement presented at this meeting and attached to this RBA. The changes reflect a new requirement that when electing the health insurance credit (HIC), employers will be required to pay an initial contribution equal to the greater of two years of expected benefit payments or the amount required to reach at least a 25 percent funded status for its HIC plan, with the remainder of the unfunded liability amortized over no more than 10 years, as well as requiring that the amortization period for unfunded liabilities generated by all elected plan amendments be set at 10 years rather than the current 20 years.*

INFORMATION ITEM

Upcoming B&A Committee Meeting:

The Committee will meet on November 14, 2022, at 1:00 p.m. to receive the valuations for the local plans, VLDP, VSDP and the Line of Duty Act fund. In addition, staff will be finalizing the 2023 meeting schedule in the coming weeks.

Submitted to the Board of Trustees on October 18, 2022.

William A. Garrett, Chair
Benefits and Actuarial Committee



**Accept the Plan Actuary’s Valuations as of
June 30, 2022, for the Five Statewide Retirement Plans,
Group Life Insurance, and Health Insurance Credit Plans
for State and Teachers.**

Requested Action

The Virginia Retirement System Board of Trustees accepts the June 30, 2022 Actuarial Valuations conducted by the VRS plan actuary, Gabriel, Roeder, Smith & Company, for the Five Statewide Retirement Plans, Group Life Insurance, and the Health Insurance Credit plans for both State and Teachers.

Description/Background

The VRS plan actuary conducts actuarial valuations annually as of the close of the fiscal year (June 30). The results of the valuations are used to establish employer contribution rates in odd-numbered years. The results in even-numbered years are shared with the Board of Trustees to inform the Board of any emerging trends or indications of the magnitude and direction of contribution rates.

Authority for Requested Action

Code of Virginia § 51.1-124.22(A)(3) authorizes the Board to employ an actuary as its technical advisor for the administration of the Retirement System.

The above action is approved.

A. Scott Andrews, Chair
VRS Board of Trustees

Date



June 30, 2022 Annual Actuarial Valuation Results

**Presented by: Becky Stouffer, ASA, MAAA, FCA and
Jim Anderson, FSA, EA, MAAA, FCA**



We are Glad to be Here!

- First GRS valuation performed for Virginia Retirement System in 20 years
- GRS replicated Cavanaugh Macdonald 2021 actuarial results within tolerances
- Today's focus: 2022 Valuations
- GRS incorporated “Best Practice” approaches
 - Tweaks more than major changes



Agenda

- Big Picture – Pension & OPEB
- Highlights of 2022 Pension Valuations
- Highlights of 2022 OPEB Valuations
- Looking Ahead
- Appendix





BIG PICTURE

BIG PICTURE – PENSION/OPEB

Big Picture – October Meeting Content

Pension	Other Post-Employment Benefits (OPEB)
Virginia Retirement System <ul style="list-style-type: none"> • State Employees • Teachers 	Health Insurance Credit (HIC) <ul style="list-style-type: none"> • State Employees • Teachers
Virginia Law Officers (VaLORS)	Group Life Insurance
State Police Officers (SPORS)	
Judicial (JRS)	

November Meeting Content: Political Subdivision Pension & OPEB Results

HIC – Constitutional Officers, Social Services Employees, Registrars

Virginia Disability Programs (VSDP, VLDP), Line of Duty Act Fund



Big Picture: Actuarial Valuation Results

- June 30, 2022 Actuarial Valuations of VRS Pension and OPEB plans are informational
 - Measure funding progress as of June 30, 2022
 - Develop inputs for use in June 30, 2023 valuations

Odd year valuations determine contribution rates for 2 years



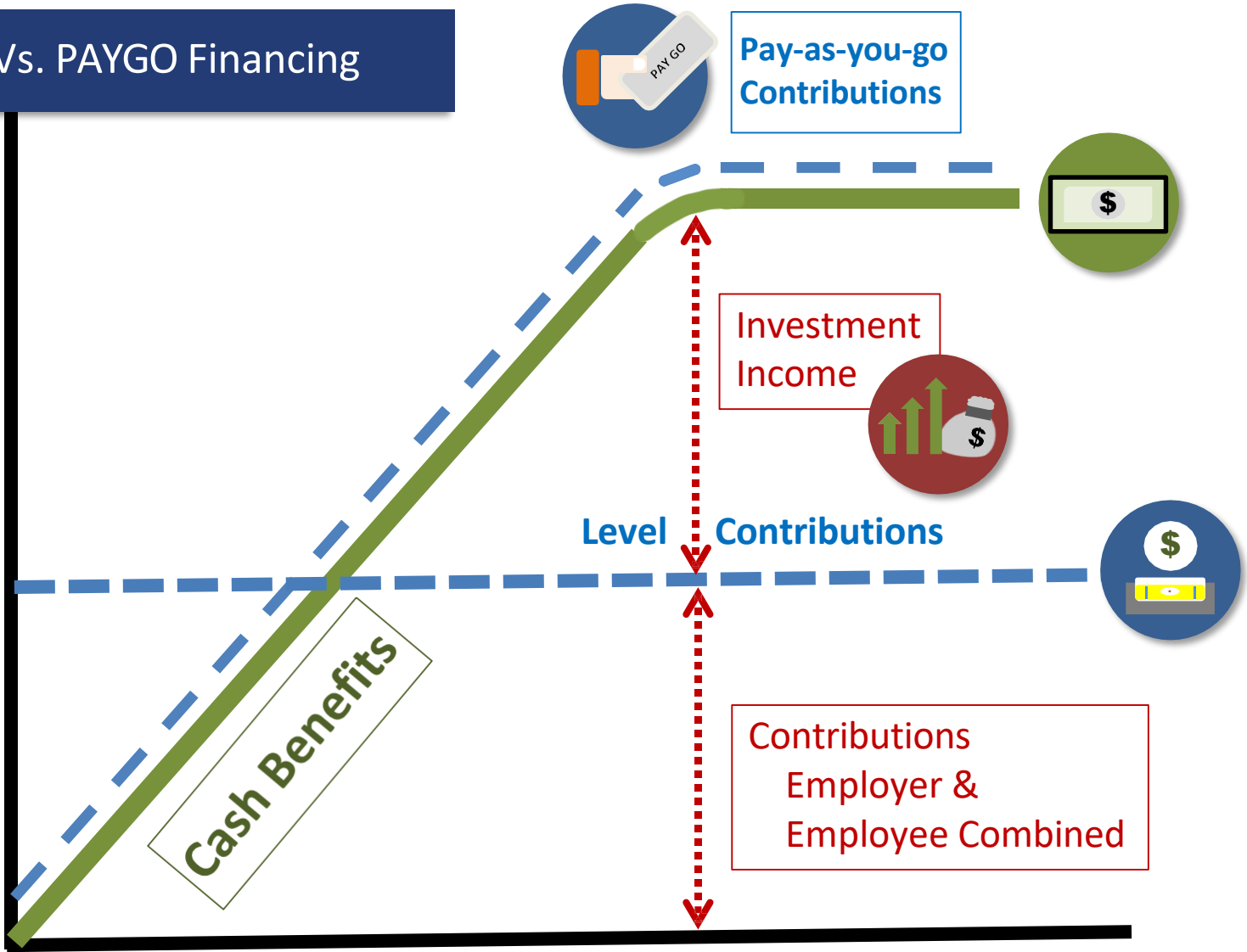
Big Picture: General Funding Objectives

- Intergenerational equity with respect to plan costs
- Stable or increasing ratio of assets to liabilities
- Stable pattern of contribution rates



Pre-funding Vs. PAYGO Financing

% of Active Employee Pays



Level Contributions

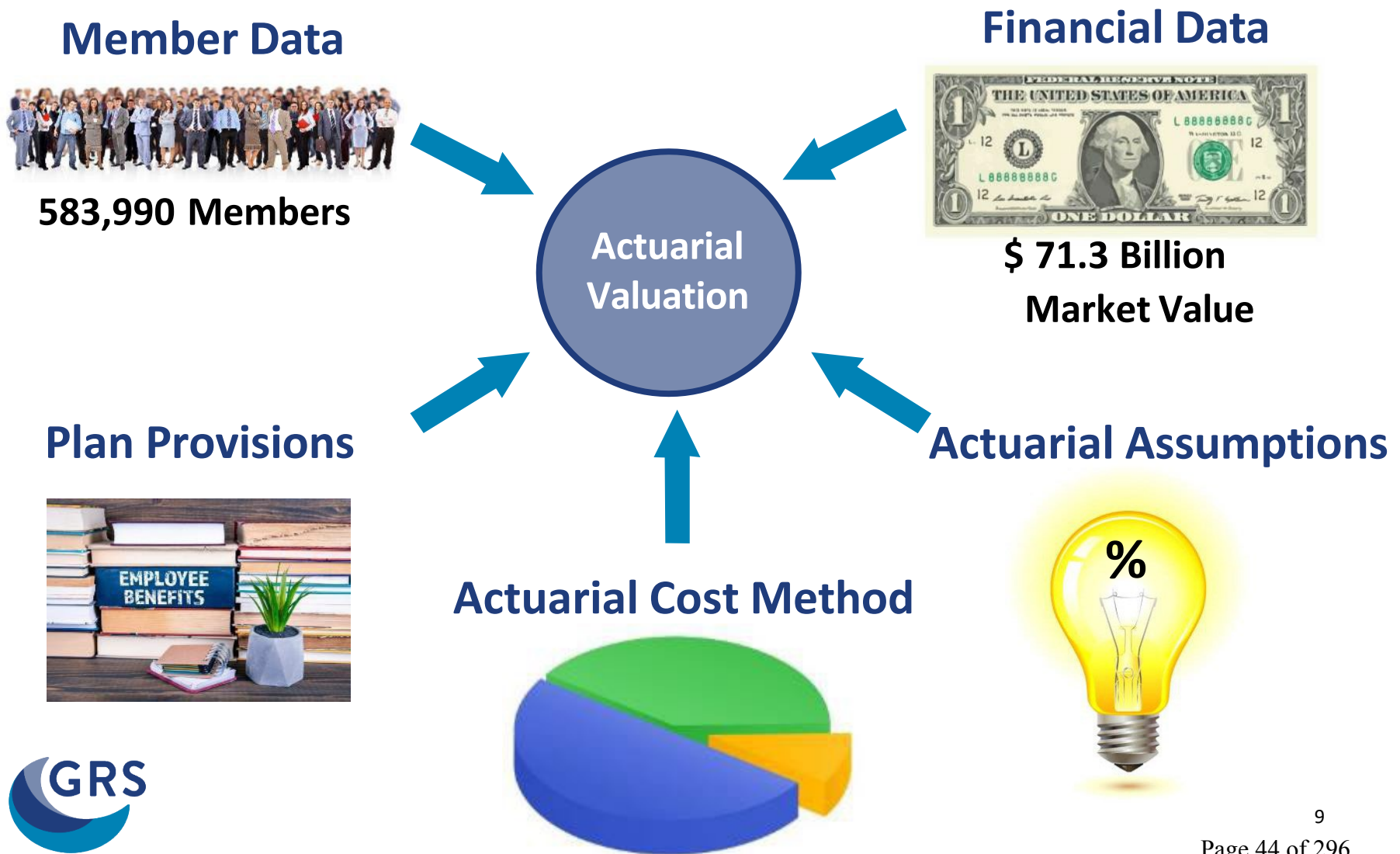
Contributions Employer & Employee Combined


Start

50 Years of Time



Actuarial Valuation Process – Statewide Pension, not including Political Subdivisions



Three spotlights are positioned at the top of the frame, casting beams of light onto a white podium on a stage. The background is a solid blue color.

JUNE 30, 2022

VALUATION RESULTS HIGHLIGHTS

Active Participants at June 30, 2022

System	Plan 1	Plan 2	Hybrid	Total 2022	Total 2021	Percent Change
State	26,621	13,083	34,344	74,048	73,686	0.5%
Teachers	58,598	27,974	66,784	153,356	149,793	2.4%
SPORS	969	916	-	1,885	1,947	-3.2%
VaLORS	2,123	5,166	-	7,289	7,823	-6.8%
JRS	154	45	262	461	453	1.8%
Pol. Sub.	TBD	TBD	TBD	TBD	108,613	TBD
Total	TBD	TBD	TBD	TBD	342,315	TBD



Actives: Changes in Average Salary

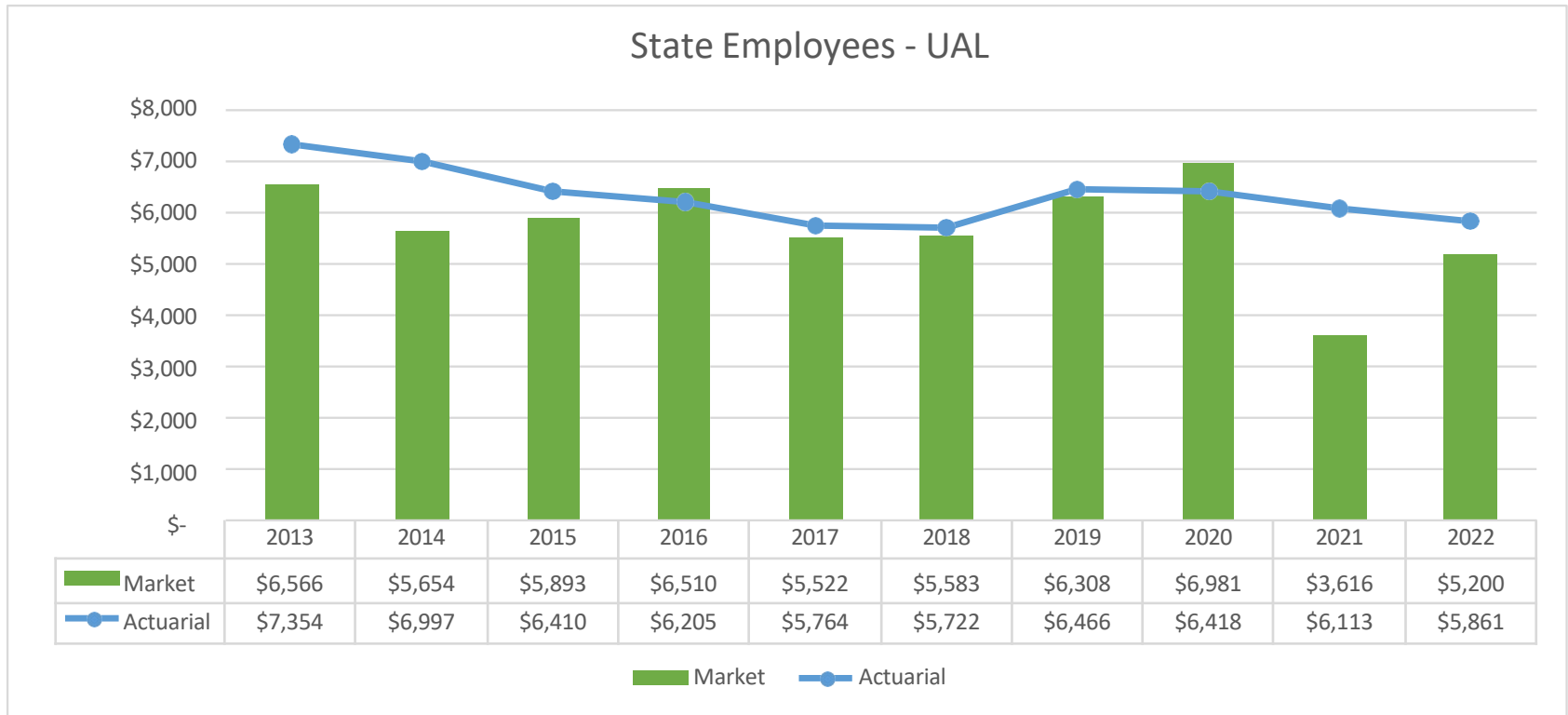
System	2021	2022	Percent Change
State	\$ 62,350	\$ 66,799	7.1%
Teachers	57,125	60,405	5.7%
SPORS	73,341	84,463	15.2%
VaLORS	44,879	51,103	13.9%
JRS	174,669	175,152	0.3%

State & Teachers: 5% increase in 2022 and another 5% increase budgeted for June 2023

SPORS and VaLORS: targeted and compression increases



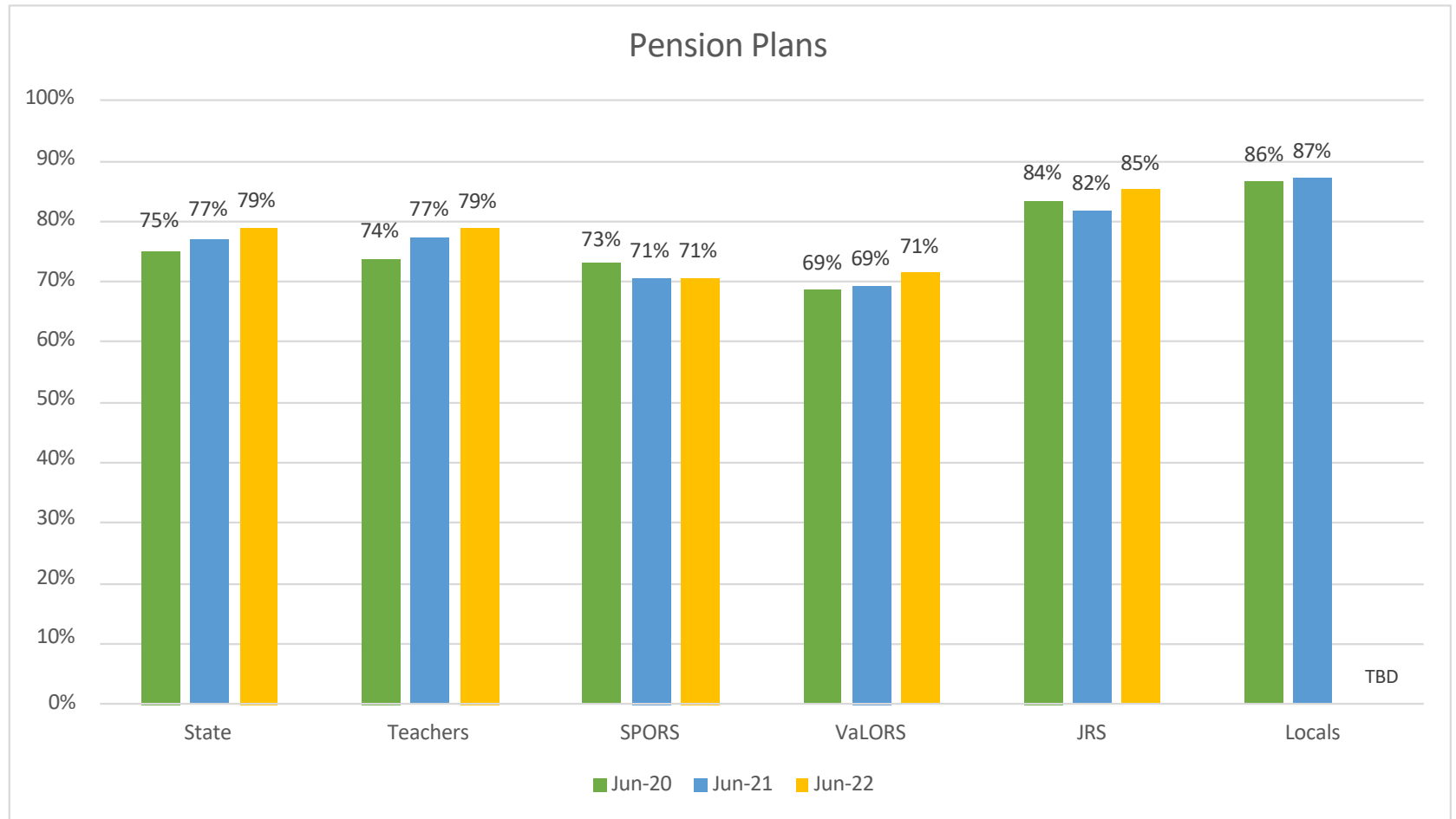
Why We Smooth Asset Returns



Unfunded liabilities will trend to Market Value basis over time
 Other VRS Retirement Plans have similar patterns



Funded Status (AVA) – Pension Plans



Calculated Employer Contributions

- Will vary significantly for System, Plan and Employer based on:

Benefit Features

Demographics

Funded Status

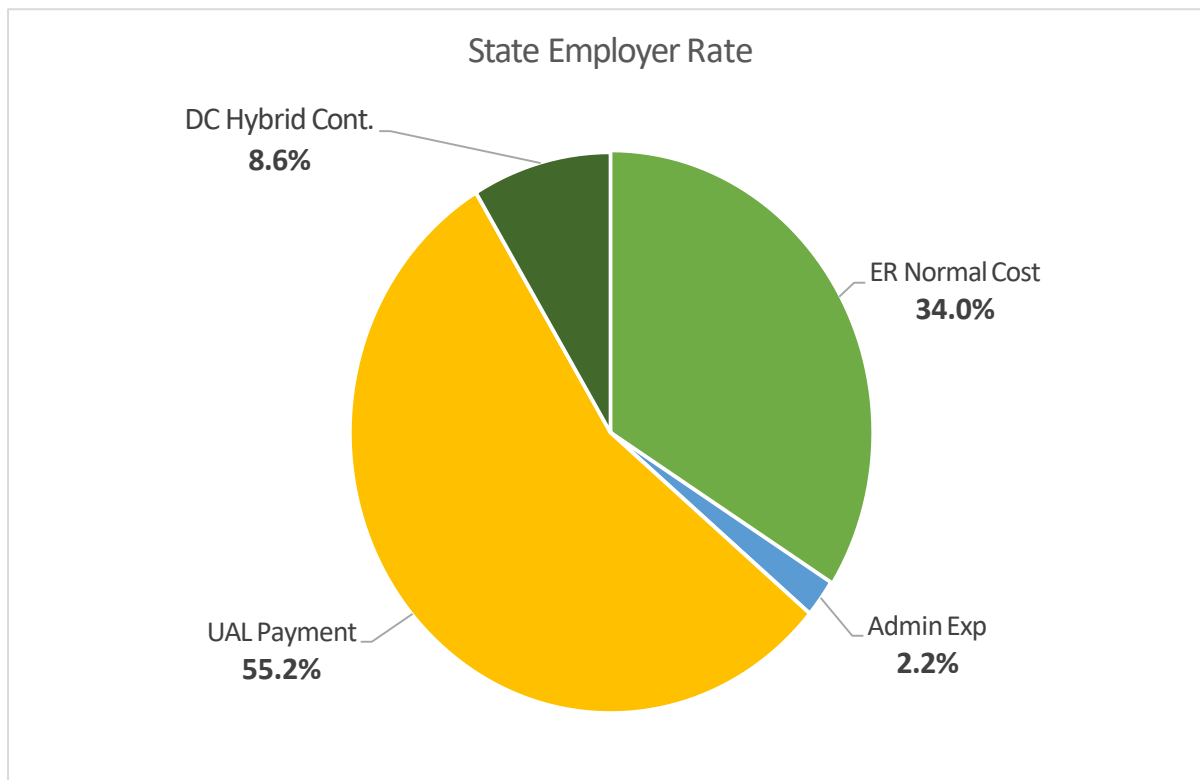


- Two Components:

Normal Cost – this represents the cost of the current year benefit earned by each active member

Amortization of Unfunded Liability – uses a systematic method (funding policy) to pay off the unfunded liability for each employer

Calculated Employer Pension Contributions – State Employees



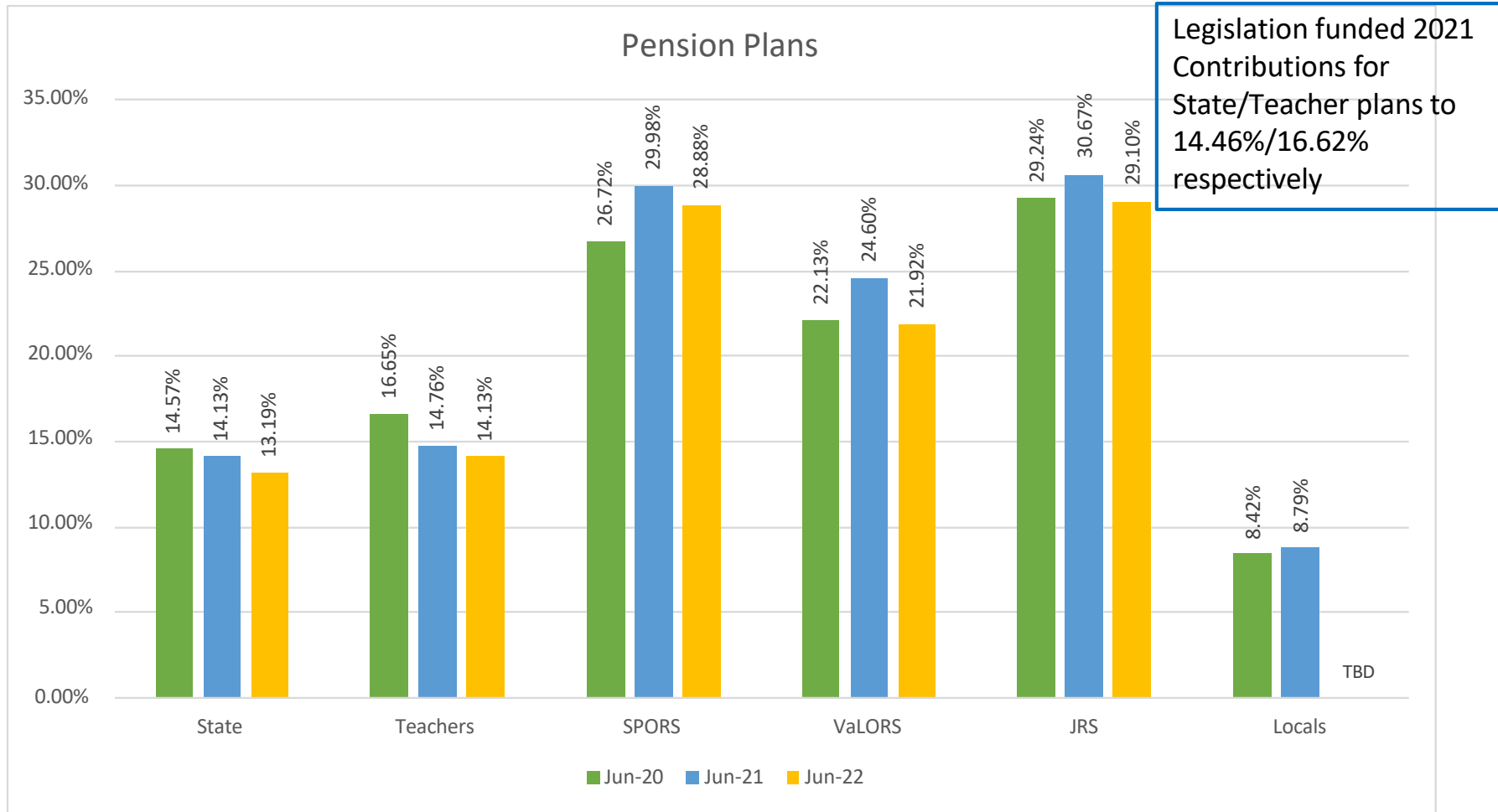
Normal Cost ultimately decreases to Plan 2/Hybrid level

Component	% of Pay
ER Normal Cost	4.5%
Admin Exp	0.3%
UAL Payment	7.3%
DC Hybrid Cont.	1.1%

UAL amortization payment = majority of the contribution for pension plans (other than JRS)



Actuarially Determined Employer Contribution Rates – Pension Plans



Pension Results Commentary

- Liability changes
 - COLA:
 - COLA for Plan 1 = 3.85% vs. 2.5% assumption;
 - COLA for Plan 2 / Hybrid = 3.0% vs. 2.25% assumption
 - Resulting liability loss (\$millions)

	State	Teachers	SPORS	VaLORS	JRS
COLA Impact	\$192	\$358	\$9	\$17	\$6

Pension Results Commentary

- Liability changes
 - Pay Increases > expected (except for JRS)
 - Resulting liability loss (\$millions)

	State	Teachers	SPORS	VaLORS	JRS
Salary Impact	\$344	\$896	\$58	\$60	(\$7)

Pension Results Commentary

- Demographic changes
 - Active population across all plans has almost returned to pre-pandemic levels
 - Increasing amount of in-actives, both vested and non-vested
- Other

Pension Results Commentary

- Impact of additional \$699 million infusion in June 2022

	Additional Contribution	Funded Status Impact	Contrib. Rate Impact
State	\$219,156,316	+0.81%	-0.32%
Teachers	\$442,371,087	+0.81%	-0.32%
SPORS	\$10,957,816	+0.80%	-0.49%
VaLORS	\$19,886,407	+0.81%	-0.39%
JRS	\$6,250,014	+0.86%	-0.56%

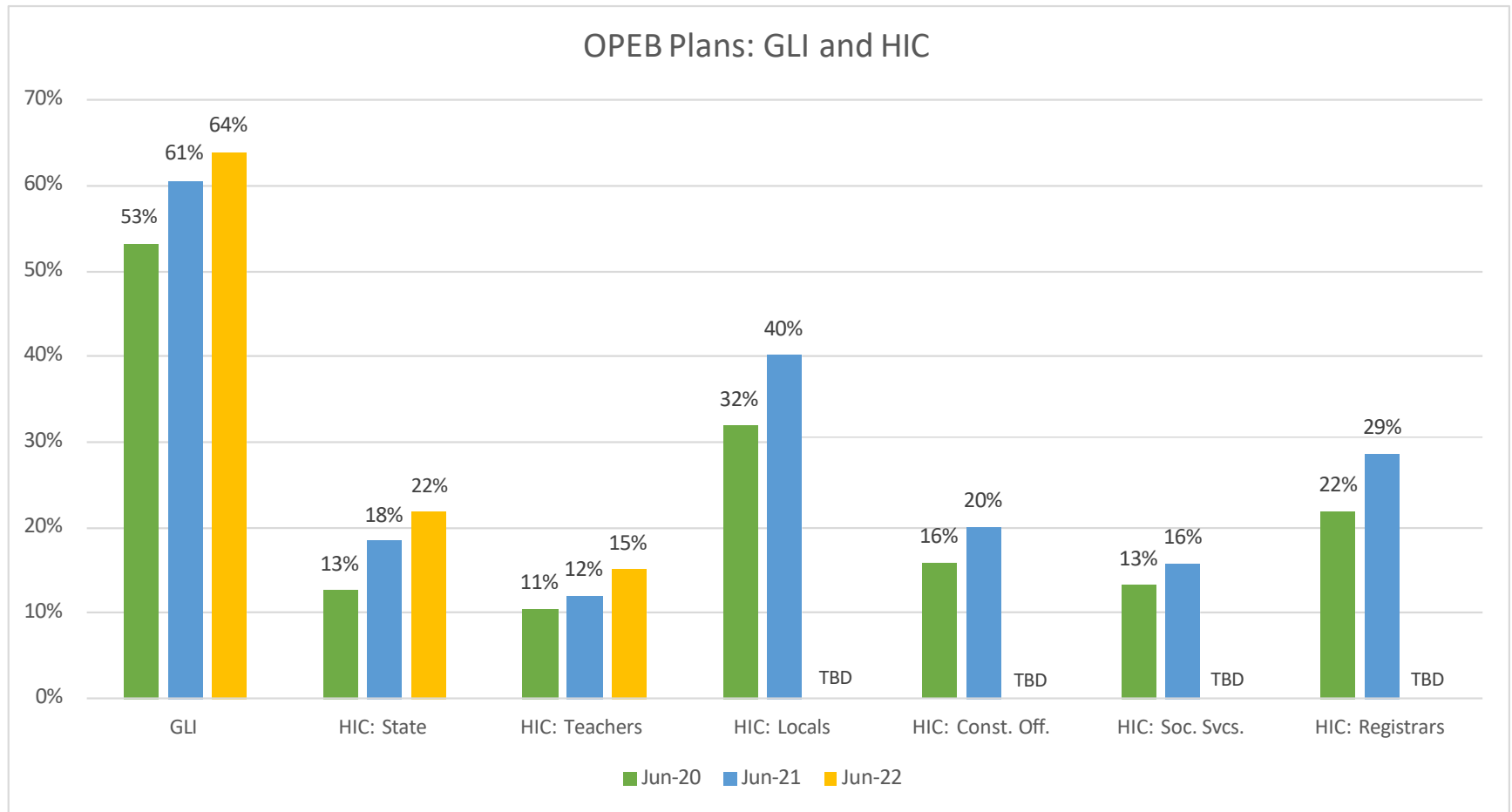


OPEB: HIC Allocation to Employers

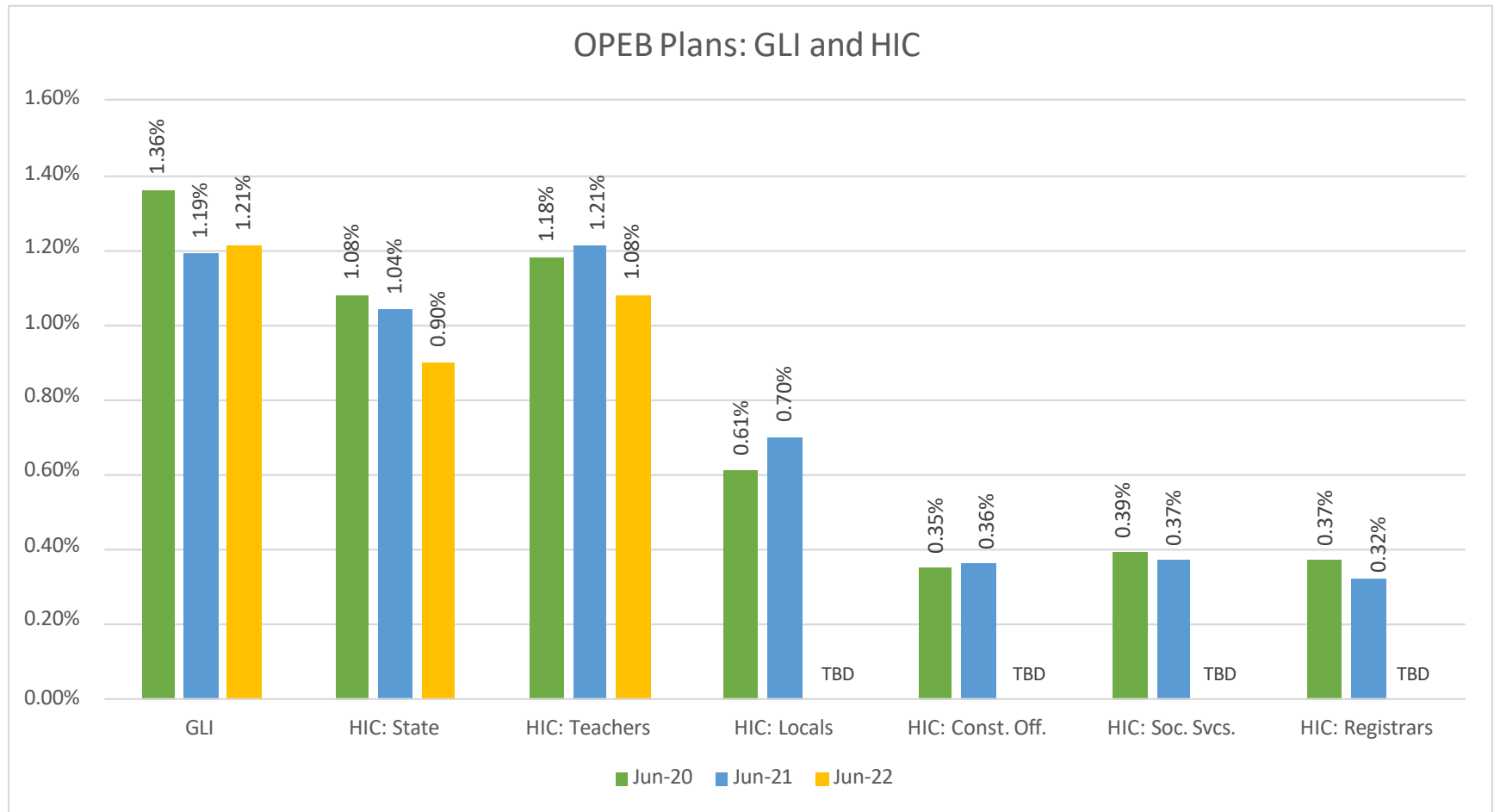
- Health Insurance Credit actual benefit payments charged back to the employer(s)
 - For each disbursement for each payee
- Prior allocation: charged last employer with HIC benefit based on total service
- Revised allocation: allocate to all employers the retiree worked for based on
 - Service
 - Accrual level



Funded Status (AVA) – OPEB Plans



Actuarially Determined Employer Contribution Rates – OPEB Plans



OPEB Results Commentary

- Impact of additional \$51 million infusion in June 2022

	Additional Contribution	Funded Status Impact	Contrib. Rate Impact
HIC - State	\$8,522,746	+0.85%	-0.00%
HIC - Teachers	\$12,013,013	+0.84%	-0.01%
GLI	\$30,438,378	+0.84%	-0.01%
HIC - Constit. Off.	\$275,975	TBD	TBD
HIC - Soc. Svcs.	\$121,754	TBD	TBD
HIC – Registrars	\$6,494	TBD	TBD



OPEB Results Commentary

- GLI: increased active life insurance rate
 - effective 7/1/22 = 16.2 cents per \$1,000
 - Increase from 14.7 cents per \$1,000
- HIC: instituted new HIC allocation methodology
 - State AAL Loss = \$13.3 million
 - Teachers AAL Loss = \$10.0 million



Pension Projections

State Employees and Teachers

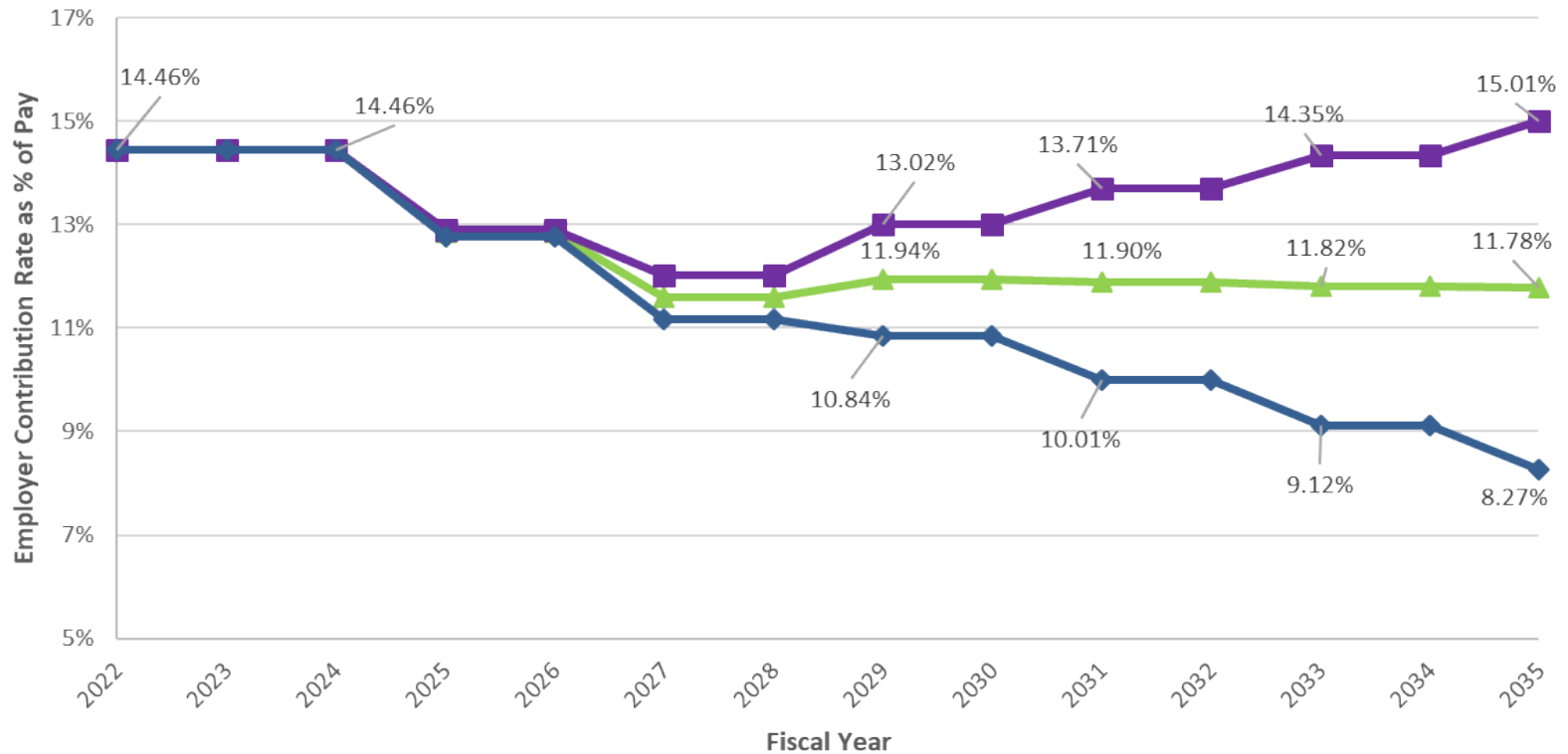
- The following pages show projected pension contributions & funded status
 - Liabilities are calculated at 6.75%
 - Investment returns shown at assumed 6.75% rate, and 5.75%/7.75% for sensitivity
- Contribution rates include:
 - Defined Benefit portion
 - Defined Contribution portion (will be decoupled from Employer Rate in future years)



Projected Employer Contribution Rates Including Defined Contribution Hybrid

State Employees

Investment Return Sensitivity

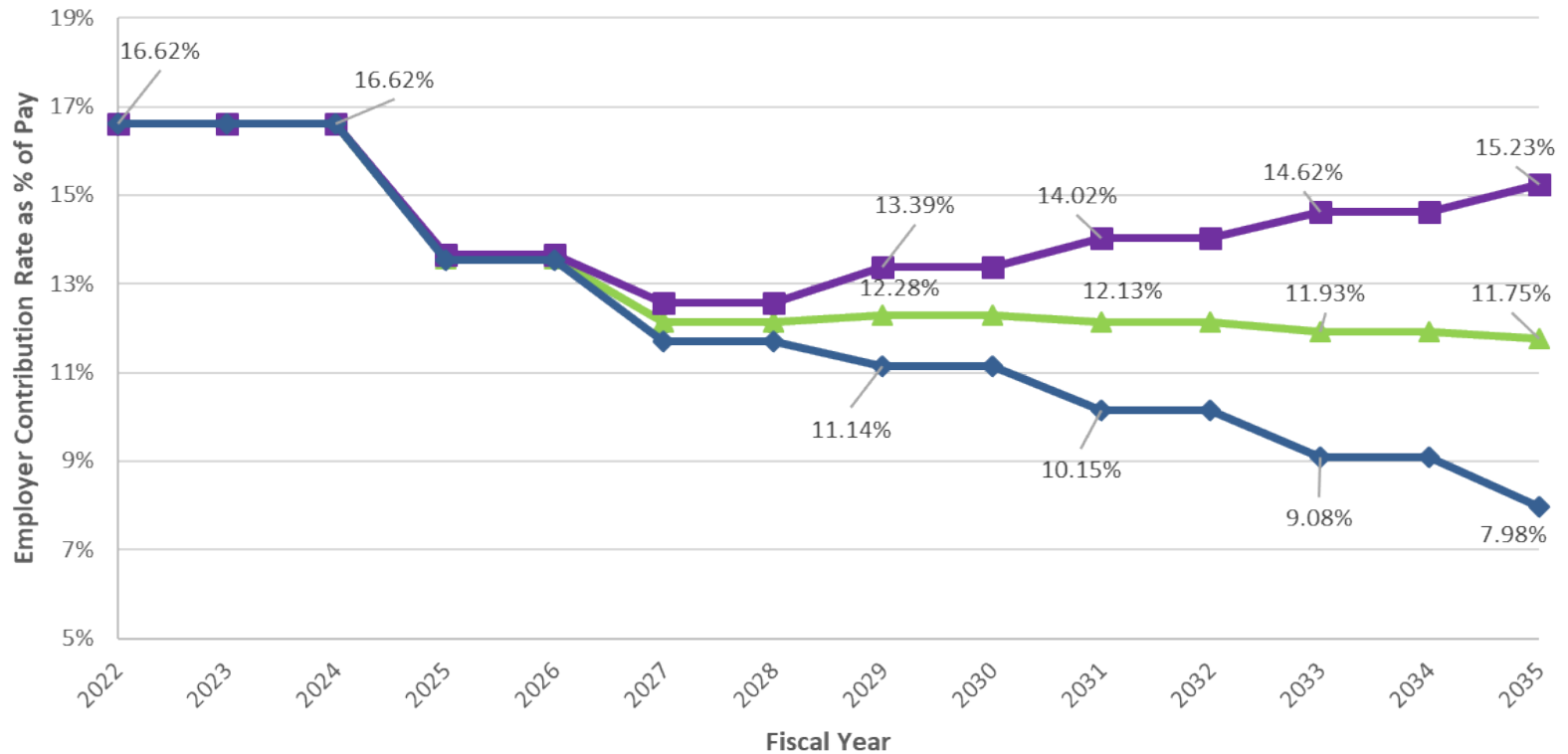


▲ State (6.75% Return)
 ■ State (5.75% Return)
 ◆ State (7.75% Return)

Projected Employer Contribution Rates Including Defined Contribution Hybrid

Teachers

Investment Return Sensitivity

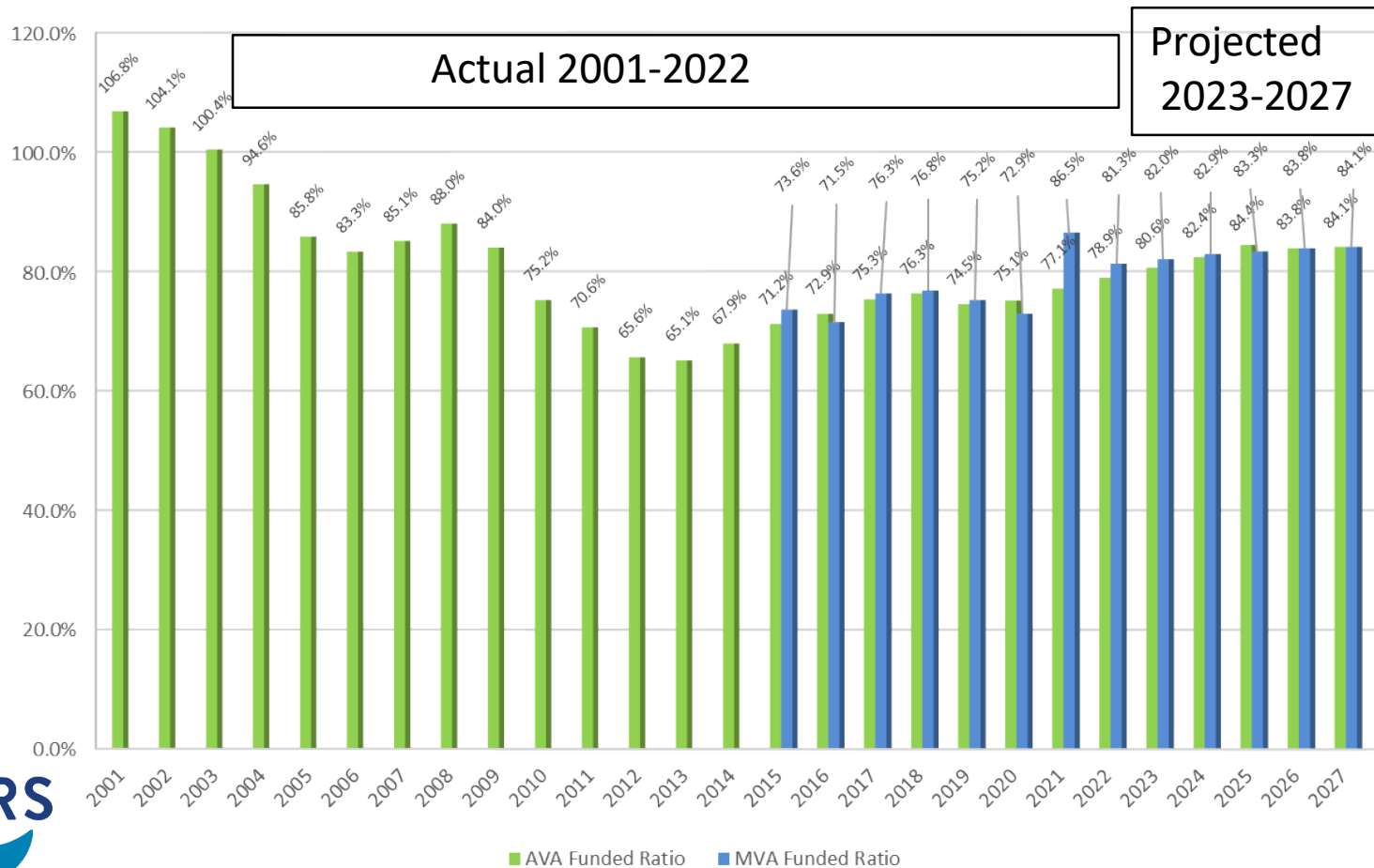


—▲ Teachers (6.75% Return)
 —■ Teachers (5.75% Return)
 —◆ Teachers (7.75% Return)

Projected Pension Funded Status

State Employees

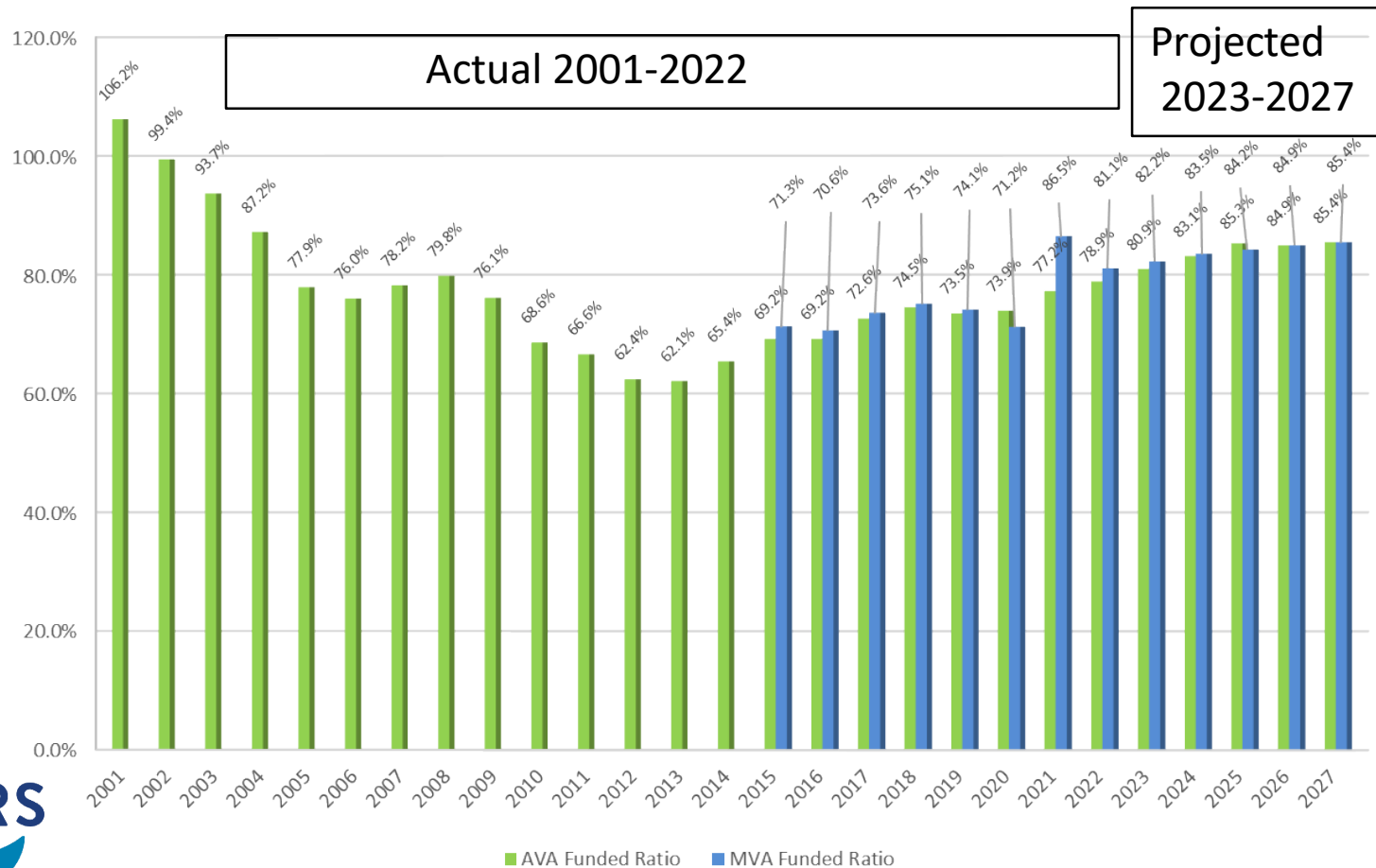
Projected Funded Status



Projected Pension Funded Status

Teachers

Projected Funded Status



Conclusion



1. Improved Funded Status on Actuarial Asset Basis

- Despite lower than expected returns for fiscal year 2022, recognition of prior gains led to improved funded status

2. Contributions

- Lower for Pension
- Lower for OPEB

3. Looking Forward:

- Planned additional funding for 2023-2024 based on 2022 appropriation act
- Market volatility/inflation
- Continued monitoring of payroll growth and head count

Disclaimers

- This presentation expresses the views of the authors and does not necessarily express the views of Gabriel, Roeder, Smith & Company.
- Future actuarial measurements may differ significantly from the current measurements presented in this report due to such factors as the following: plan experience differing from that anticipated by the economic or demographic assumptions; changes in economic or demographic assumptions; increases or decreases expected as part of the natural operation of the methodology used for these measurements (such as the end of an amortization period or additional cost or contribution requirements based on the plan's funded status); and changes in plan provisions or applicable law.

Disclaimers

- This presentation is intended to be used in conjunction with the forthcoming actuarial valuation reports. This presentation should not be relied on for any purpose other than the purposes described in the valuation reports.
- This presentation shall not be construed to provide tax advice, legal advice or investment advice.
- Jim Anderson and Becky Stouffer are independent of the plan sponsor, are Members of the American Academy of Actuaries (MAAA), and meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinions contained herein.



Amendments to VRS Funding Policy Statement.

Requested Action

The Board approves the changes to the VRS Funding Policy Statement presented at this meeting and attached to this RBA. The changes reflect a new requirement that when electing the health insurance credit (HIC), employers will be required to pay an initial contribution equal to the greater of two years of expected benefit payments or the amount required to reach at least a 25 percent funded status for its HIC plan, with the remainder of the unfunded liability amortized over no more than 10 years, as well as requiring that the amortization period for unfunded liabilities generated by all elected plan amendments be set at 10 years rather than the current 20 years.

Description/Background

VRS staff recommends this change to the VRS Funding Policy Statement in order to ensure that employers electing the HIC have initial funds available to pay benefits and to establish at least a minimum funded status at the outset and that the amortization period for all elected plan amendments be shortened to 10 years. This change mirrors the current requirement that an employer electing to participate in VRS must be at least 75% funded for pension benefits at the time of the election, and that any benefit enhancements do not reduce the employer's funded status below 75%. The Funding Policy Statement requires prepayment of benefit enhancements or granted service to ensure the minimum funded status, and will now also require employers electing HIC to pay an initial contribution equal to the greater of two years of expected benefit payments or the amount required to reach at least 25 percent funded for its HIC plan, with the remainder of the unfunded liability amortized over no more than 10 years.

Rationale for Requested Action

The VRS Funding Policy Statement memorializes the methods by which the Board has elected to fund each plan, and the proposed amendments to the policy statement allow for the change to the HIC and plan amendment election requirements.

Authority for Requested Action

Article X, § 11 of the *Constitution of Virginia* requires that VRS benefits be funded using methods that are consistent with generally accepted actuarial principles, and *Code of Virginia* § 51.1-124.22(A)(8) authorizes the Board to promulgate regulations and procedures and make determinations necessary to carry out the provisions of Title 51.1.

The above action is approved.

A. Scott Andrews, Chair
VRS Board of Trustees

Date

VRS Funding Policy Statement¹

1. Introduction

A plan funding policy determines how much should be contributed each year by employers and participants to provide for the secure funding of benefits in a systematic fashion.

The principal goal of a funding policy is to ensure that future contributions along with current plan assets are sufficient to provide for all benefits expected to be paid to members and their beneficiaries when due. The funding policy should seek to manage and control future contribution volatility to the extent reasonably possible, consistent with other policy goals. The actuarially determined contribution should be calculated in a manner that fully funds the long-term costs of promised benefits, while balancing the goals of 1) keeping contributions relatively stable and 2) equitably allocating the costs over the employees' period of active service.

The current funding policy used by the VRS Board sets contribution rates using the Entry Age Normal cost method, an investment return assumption of 6.75%, an inflation assumption of 2.5%, and a closed 20-year amortization period for unfunded liabilities (Legacy unfunded liabilities as of 6/30/13 are amortized over a closed 30-year amortization period.)

Article X, § 11 of the *Constitution of Virginia* provides that the Virginia Retirement System benefits shall be funded using methods which are consistent with generally accepted actuarial principles. Until 2012, the Annual Required Contribution (ARC) as described in the Governmental Accounting Standards Board's (GASB's) Statements No. 25 and No. 27 was a de facto funding policy for many public-sector retirement systems, including the Virginia Retirement System.

The Board sets contribution rates for all local employers under this policy. However, with respect to the plans for state employees and the teacher plan, while the rates developed under the Board's policy are the certified contribution rates, the Governor and the General Assembly determine the funding that they will provide through the state budget process toward the Board certified contribution rates for the State and Teachers and other statewide OPEB plans. Beginning in FY 2013, § 51.1-145.K1 of the Code of Virginia set out guidelines for the General Assembly to follow for the funding of the contribution rates certified by the VRS Board, phasing in from approximately 67% of Board-certified rate to 100% of the Board-certified rate over the next four biennia. These statutory guidelines do not apply to funding levels for Other Postemployment Benefits (OPEBs) administered by VRS.

¹ Adopted October 17, 2013; amended November 14, 2013, June 7, 2016, November 15, 2017, November 20, 2019, and October 18, 2022.

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In June 2012, GASB revised public pension accounting standards and has communicated an important message in the process: accounting standards are no longer funding standards. However, GASB did not address how employers should calculate the annual required contribution (ARC). To assist state and local government employers, several national groups developed policy guidelines for funding standards. This document is the result of an extensive review of the current funding policy, industry standards and best practices, and the development and approval of funding policy assumptions effective with the June 30, 2013 valuation. A copy of Request for Board Action 2013-07-18 adopting the funding policy assumptions is attached. This Funding Policy is intended to provide guidance to future Boards on how to set employer contribution rates and support the plan's primary goals of contribution and budgetary predictability, accumulation of required assets over time to provide for all benefits earned and achievement of intergenerational equity.

In June 2015, GASB adopted two new statements regarding OPEBs. GASB statement 74, *Financial Reporting for Postemployment Benefits Other than Pension Plans*, and GASB statement 75, *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*. These statements replace GASB 43 and GASB 45. As was the case with GASB 67 and 68, these new statements represent a significant change to the methods used to account for postemployment benefits and provide for a clear separation between accounting for and funding of OPEBs. The new standards require the adoption of a new funding policy for OPEB plans. The current VRS funding policy has been modified to accommodate funding requirements for the VRS OPEB plans.

The VRS OPEB plans include the Health Insurance Credit Program, Group Life Insurance Program, the Virginia Sickness and Disability Program (VSDP), the Virginia Local Disability Program (VLDP) and the Long Term Care benefits associated with the VSDP and VLDP. The Line of Duty Act Fund is also a defined benefit OPEB plan, although it is not a benefit exclusively for VRS members.²

² As of April 2016 all VRS OPEBs already incorporate the actuarial methods outlined in the Funding Policy, with the following exceptions:

- Health Insurance Credit Program for Political Subdivisions will incorporate a five-year asset smoothing method for funding valuations effective with the June 30, 2016 actuarial valuation.
- The Long Term Care valuation will incorporate the Entry-Age Normal cost method and five-year smoothing method for funding valuations effective with the June 30, 2016 actuarial valuation.
- Line of Duty Act Program (LODA) is currently not prefunded and as set forth in the *Code* shall be funded on a current disbursement basis or in other words is considered a "pay-as-you-go" plan. As such, the plan has no unfunded liabilities and uses market value of assets for valuation purposes. In the event that the General Assembly takes action to begin prefunding this program, the Board of Trustees would move to adopt the various funding provisions contained in this document including moving the program to a five-year asset smoothing method for funding valuations effective with any decision to prefund the LODA program.

These changes were approved by the Board of Trustees at its June 7, 2016 meeting, and were incorporated into this amended Funding Policy. Where a particular actuarial method was already in use, the Funding Policy notes that the Board confirms the actuarial methods for OPEBs.

The Funding Policy addresses the following general policy objectives:

- Ensure funding of plans is based on actuarially determined contributions;
- Build funding discipline into the policy to ensure promised benefits can be paid;
- Maintain intergenerational equity so the cost of employee benefits is paid by the generation of individuals who receive services;
- Make employer costs a consistent percentage of payroll; and
- Require clear reporting to show how and when plans will be adequately funded.

This document serves as the Funding Policy for VRS. It has been prepared by VRS in collaboration with the Board and the VRS Plan Actuary and is effective as of the June 30, 2013 valuation, and modified to accommodate the OPEB plans effective as of the June 30, 2016 valuation.

2. Authority

The Virginia Retirement System is administered in accordance with Title 51.1, chapters 1, 2, 2.1, 3 and 4 of the *Code of Virginia*. The contribution to be paid by members of VRS is fixed at a level that covers only part of the cost of accruing benefits. The balance of the cost is paid by employers within the Trust Fund (the “Fund”).

The OPEB plans are administered in accordance with Title 51.1, chapters 5, 11, 11.1, and 14 of the *Code of Virginia*. The cost associated with OPEBs is generally borne by the employer and benefits are paid from the various trust funds. An exception to this practice is the Group Life Insurance Program. The Board determines the amount each insured shall contribute for the cost of insurance and by statute this amount is capped at \$0.70 per month for each \$1,000 of annual salary. Each employer determines whether this cost will be paid by the member or funded by the employer. The balance of the cost is paid by employers within the Fund. The Group Life Insurance plan, however, is a cost-sharing plan so all employers are charged the same rate.

The Funding Policy focuses on the pace at which these liabilities are funded and, in so far as is practical, the measures to ensure that employers pay for their own liabilities.

The Funding Policy is authorized by a framework that includes:

- Article X, § 11 of the *Constitution of Virginia*
- Title 51.1 of the *Code of Virginia*

This is the framework within which the VRS Plan Actuary carries out valuations to set employer contribution rates and provide recommendations to the Board when other funding decisions are required. The Funding Policy applies to all employers participating in the Fund.

The methods and assumptions used in the VRS funding policy are periodically reviewed as part of the quadrennial experience study as required under § 51.1-124.22(A)(4). As such, the content of this document may be updated to reflect changes approved by the VRS Board of Trustees.

Deleted: November 20, 2019

3. Contributions

The Funding Policy provides for periodic employer contributions set at actuarially determined rates in accordance with recognized actuarial principles (§51.1-145(A)). Originally based on parameters set out in GASB 25/27 and GASB 43/45, the contribution should include the employer's normal cost and provisions for amortizing any unfunded actuarial accrued liability (UAAL) in accordance with the requirements originally defined in GASB 25/27 and GASB 43/45.

Member and employer contributions for retirement are required by §§ 51.1-144 and -145 of the *Code of Virginia*. Chapters 5, 11, 11.1, and 14 of Title 51.1 of the *Code of Virginia* and the applicable provisions in each year's Appropriation Act relate to contribution requirements for OPEB plans administered by VRS.

Employer contributions are normally made up of two main elements³:

- a) the estimated cost of future benefits being accrued, referred to as the "normal cost"; and
- b) an adjustment for the funding position of accrued benefits relative to the Fund's actuarially adjusted assets, or the "amortization payment UAAL." If there is a surplus there may be a contribution reduction; if there is a deficit, there will be a contribution addition, with the amount of surplus or deficit being spread over a number of years.

Items a) and b) above are then combined and expressed as a percentage of covered payroll.

Employer contribution rates are set each biennium and are in effect for the entire biennium. Valuations in the "off" years are for informational purposes only. Generally, employers with well-funded pension plans consistently pay their annual required contribution in full.

Where this process as applied to a political subdivision would, in the Plan Actuary's opinion, not be expected to maintain the plan's solvency, the VRS staff, working with the Plan Actuary, may determine alternative funding requirements that would maintain the political subdivision's solvency while also meeting the other objectives of this Funding Policy Statement.

With respect to statewide plans, if unfunded liabilities exist in a plan, the Board may recommend alternative contribution rates in excess of the actuarially determined rates if opportunities exist to accelerate paydown of unfunded liabilities. Examples of alternative rates could potentially include approaches such as maintaining rates from the prior year if rates drop in subsequent rate setting or maintaining a higher level contribution rate until a certain funded status is achieved.

³ Contributions also include administrative expenses.

4. Funding Target

VRS operates the same target funding level for all ongoing employers of 100% of its accrued liabilities valued on an ongoing basis. This means that contribution rates are set with the intent of funding 100% of a member's benefits during a member's working lifetime. The Line of Duty Act Fund is an exception, as employer contributions are currently determined by the Board on a current disbursement basis per statute. As such, the target funding level for all ongoing employers for LODA is at or near 0% of its accrued liabilities.

Funded Status is defined as the ratio of the actuarial value of assets to the value placed on the benefits, or plan's liabilities, by the VRS Plan Actuary. The VRS Plan Actuary reports on the funded status of each plan in the system in each annual valuation.

5. Actuarial Cost Method

The actuarial cost method is the means by which the total present value of all future benefits for current active and retired participants is allocated to each year of service (i.e., the "normal cost" for each year) including past years (i.e., the "actuarial accrued liability"). There are several available actuarial cost methods, but most governmental plans use the entry age normal (EAN) cost method while a significant minority use the projected unit credit (PUC) method. In the past, VRS has used the EAN method for most of the plans it administers.

Although the EAN and PUC cost methods are both considered reasonable under actuarial standards of practice and GASB 25 and GASB 43 in most circumstances, it is important for plan stakeholders to understand the implications of either method. EAN tends to recognize actuarial liabilities sooner than PUC, and it also tends to result in a more stable normal cost pattern over time for pay-related benefits, even in the face of demographic shifts. The more stable normal cost pattern over time should help in reducing the risk of higher levels of future contributions.

Under the PUC method, the plan's normal cost is the present value of the benefits "earned" during the year, but based on projected pay levels at retirement. For an individual participant, the PUC normal costs increase each year because the present value increases as the participant gets a year closer to retirement. In contrast, under the EAN method, the normal cost is specifically determined to remain a level percentage of pay over each participant's career.

Because EAN normal cost rates are level for each participant, the normal cost pattern for the entire plan under EAN is more stable for pay-related benefits in the face of demographic shifts in the workforce. It is this normal cost stability that makes the EAN method the preferred funding method for pay-related benefits of public plans.

GASB has reaffirmed its decision to require governmental pension plans to base their financial statement reporting on the EAN method. For comparability, GASB has also decided to require governmental OPEB plans, which may not provide pay-related benefits, to base their financial statement reporting on the EAN method.

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Effective with the June 30, 2013 valuation, the Board has adopted the Entry-Age Normal cost method in deriving plan liabilities. This is a continuation of the Board's existing cost method. Effective with the June 30, 2016 valuation, the Board has adopted the Entry-Age Normal cost method for all OPEB plans.

6. Asset Valuation Method

Because investment markets are volatile and because pension plans typically have long investment horizons, asset-smoothing techniques can be an effective tool to manage contribution volatility and provide a more consistent measure of plan funding over time. Asset-smoothing methods reduce the effect of short-term market volatility on contributions, while still tracking the overall movement of the market value of plan assets, by recognizing the effects of investment gains and losses over a period of years. This is also in keeping with § 51.1-145(A), which requires that contribution rates be determined in a manner so as to remain relatively level from year to year.

Determining the ideal asset-smoothing policy involves balancing the two goals of ensuring fairness across generations and controlling contribution volatility for plan sponsors. A very long smoothing period will greatly reduce contribution volatility, but this may mean the impact of recent investment experience is deferred to future generations. However, a very short smoothing period (or none at all) may result in contribution requirements that fluctuate dramatically from year to year.

Such volatility may also result from an asset-smoothing method that constrains how far the smoothed value differs from the market value by imposing a market value "corridor." A corridor is typically expressed as a ratio of the smoothed value of assets to the market value of assets. Actuarial standards of practice and related actuarial studies seek to identify asset-smoothing methods that achieve a reasonable balance between how long it takes to recognize investment experience (the smoothing period) and how much smoothing is allowed in the meantime (the corridor). The resulting smoothing periods are in the range of three to 10 years (with five the most common) and a corridor wide enough to allow the smoothing method to function except in the most extreme conditions.

While the smoothing period for governmental plans is not limited by federal laws or regulations, the Actuarial Standards Board has set out principles for asset smoothing in ASOP No. 44. Under these principles, when a smoothed asset valuation method is used, the actuary should select a method so that the smoothed asset values fall within a reasonable range of the corresponding market values and any differences between the actuarial value and market value of assets should be recognized within a reasonable period.

Effective with the June 30, 2013 valuation, the Board has adopted a five-year asset smoothing period, which also includes a corridor that will restrict the smoothed value from falling below 80% of the true market value or exceeding 120% of the true market value. This is a continuation of the Board's existing asset valuation method. Effective with the June 30, 2016 valuation, the Board has adopted the same asset smoothing period and corridors for the OPEB plans, with the exception of the LODA program, which, by statute, does not prefund benefits. In the event a change to the statutory contribution requirements

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of the LODA program necessitate an asset valuation method, the same asset smoothing period and corridors should be applied to the LODA program at that time.

7. Amortization Method

Amortization of unfunded liabilities is a major component of the annual contribution. Amortization policies involve a balance between controlling contribution volatility and ensuring a fair allocation of costs among generations. The Plan Actuary uses the specific amortization periods adopted by the Board for all employers when developing a method over which to pay down any unfunded liabilities that may exist. The amortization period should allow adjustments to contributions to be made over periods that appropriately balance intergenerational equity against the goal of keeping contributions level as a percentage of payroll over time as required by § 51.1-145.

Amortization of the unfunded actuarial accrued liability (UAAL) determines how current and future UAAL will be paid off or “amortized,” and so includes how changes in benefits or actuarial assumptions that affect the actuarial accrued liability should be funded over time. Even more than with asset smoothing methods, amortization policies involve a balance between controlling contribution volatility and ensuring a fair allocation of costs among generations. Longer amortization periods help keep contributions stable, but excessively long periods may inappropriately shift costs to future generations. In seeking to achieve an appropriate balance between these two important policy goals, a comprehensive amortization policy will involve the following distinct elements:

- Payment basis
- Payment structure
- Amortization period

A. Payment Basis: Level Dollar vs. Level Percent of Pay

One of the first considerations is whether amortization payments will be set at a level dollar amount (similar to a home mortgage) or as a level percent of pay. The great majority of public pension plans use level-percent-of-pay amortization where the payments toward the UAAL increase each year at the same rate as is assumed for payroll growth. Compared with the level-dollar approach, payments start at a lower dollar amount under the level percent approach, but then increase in proportion to payroll. The level-dollar method is more conservative in that it funds the UAAL faster in the early years. However, the level-percent-of-pay approach is consistent with the pay-related structure of benefits under most public plans. Moreover, because the normal cost is also determined as a level percent of pay, level percent amortization provides a total cost that remains level as a percentage of pay. In contrast, level-dollar amortization of UAAL will produce a total cost that decreases as a percentage of pay over the amortization period. A plan should balance these considerations in choosing between level-percent and level-dollar amortization. Section 51.1-145(A) of the *Code of Virginia* provides in part that “[t]he total annual employer contribution for each employer, expressed as a percentage of the annual membership payroll, shall be determined in a manner so as to remain relatively level from year to year....”

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Effective with the June 30, 2013 valuation the Board has elected to use the level percent of pay payment basis. This is consistent with historical VRS practice. Effective with the June 30, 2016 valuation the Board confirms the continued use of the level percent of pay payment basis put in effect June 30, 2013 for the OPEB plans when an actuarially determined contribution is calculated.

B. Payment Structure

Amortization policy must also consider how amortization payments should be structured. For example, a determination needs to be made as to whether the entire UAAL should be aggregated and amortized as a single amount, or whether the plan should track individual bases for each source of UAAL or surplus each year, and amortize these separately. Amortization periods can be fixed, open or “rolling” (with the amortization period restarted each year).

Although use of a single amortization base provides simplicity, use of separate amortization bases for each source of UAAL has the advantage of tracking separately each new portion of UAAL and providing another mechanism to stabilize contribution rates. Under this approach, over time there will be a series of bases, one for each year’s gain or loss as well as for any other changes in UAAL. This provides useful information to stakeholders, as they can view the history of the sources of a plan’s UAAL in any year. The use of separate amortization bases should help balance the annual ups and downs in the UAAL. In practice, the number of bases will be limited by the length of the amortization period as eventually bases will be fully amortized, and so will no longer be part of the UAAL.

Fixed amortization periods identify a date certain by which each portion of the UAAL will be funded. This can be contrasted with open or rolling amortization, whereby the plan “resets” its amortization period every year. This is analogous to a homeowner who refinances his mortgage each year. Although both methods are common in current practice, fixed amortization periods have the advantage of providing stakeholders with a clearer understanding of the ultimate funding target (full funding) and the path to get there. It is the structure required for private sector pensions, and is increasingly common for public pension plans.

Effective with the June 30, 2013 valuation the Board has elected to use individual bases for each source of UAAL or surplus each year and to use fixed amortization periods rather than open or rolling periods. This is a change from past VRS practice but is consistent with industry best practices. Effective with the June 30, 2016 valuation the Board confirms the continued use of individual bases for each source of UAAL or surplus each year and the use of fixed amortization periods rather than open or rolling periods put in effect June 30, 2013 for all OPEB plans, with the exception of the LODA program, which, by statute, is currently not prefunded. For the purposes of accounting disclosures under GASB 43 and 45, the LODA program will continue to use an open period. In the event a change to the statutory contribution requirements of the LODA program necessitate a payment structure, individual bases for each source of UAAL or surplus each year and fixed amortization periods, rather than open or rolling periods, will be used by the LODA program at that time.

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C. Amortization period

Amortization period is a determination of the appropriate period of time over which amortization should occur. The answer can depend on the source of the UAAL being amortized, as discussed below:

UAAL Due to Actuarial Gains/ Losses

Actuarial gains and losses arise when there is a difference between the actuary's estimates (assumptions) and the actual experience of the plan. They can result from demographic experience (e.g., the number of new retirees is higher or lower than expected), investment experience (e.g., returns that are higher or lower than expected), or other economic experience (e.g., payroll growth that is higher or lower than expected). In determining the appropriate period for amortizing gains and losses, plan sponsors should strike a balance between reducing contribution volatility (which would lead to longer amortization periods) and maintaining a closer relationship between contributions and routine changes in the UAAL (which would lead to shorter amortization periods). For many plans, amortization periods in the range of 15 to 20 years for gains and losses would assist plans in achieving a balance between these objectives.

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UAAL Due to Changes in Actuarial Assumptions

Assumption changes will result in an increase or decrease in the UAAL. Unlike gains and losses, which reflect actual past experience, assumptions are modified when future expectations about plan experience change. This amounts to taking the effect of future expected gains or losses and building it into the cost today. For that reason, and because of the long-term nature of assumption changes, a plan could be justified in using a longer amortization period than that used for actuarial gains or losses, perhaps in the range of 15 to 25 years.

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Amortization of UAAL Due to Plan Amendments

Because plan amendments are under the control of the plan sponsor, managing contribution volatility is generally not a consideration for plan amendments. This means that the primary rationale in selecting the period is to support intergenerational equity by matching the amortization period to the demographics of the participants receiving the benefit. This leads to shorter, demographically based amortization periods. For active participants, this could be the average future working lifetime of the active participants receiving the benefit improvement, while for retirees, this could be the average life expectancy of the retired participants receiving the benefit improvement. This approach would usually result in no longer than a 15-year amortization period for benefit improvements.

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An equitable amortization policy should ensure that the UAAL will be paid off in a reasonable period of time. Long amortization periods can make paying down the UAAL appear more affordable, but, because interest charges accrue and compound on the unpaid UAAL, it is prudent to set amortization periods that are not excessively long. This is especially important where level

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percent of pay amortization is used.

In an effort to balance the need to pay down the current unfunded liability while managing already increasing contribution rates, the Board elected to manage the paydown of any unfunded liabilities created prior to June 30, 2013 over a 30-year closed period. In an effort to better manage intergenerational equity and to build funding discipline into the VRS policy, the Board also decided that future unfunded liabilities would be best amortized over 20-year closed periods.

With long amortization periods, the UAAL may increase during the early years of amortization period, even though contributions are being made to amortize the UAAL. This phenomenon, known as “negative amortization”, occurs only with level percent of pay amortization. This happens because, under level percent of pay amortization, the lower early payments can actually be less than interest on the outstanding balance, so that the outstanding balance increases instead of decreases. For typical public plans, this happens whenever the average amortization period is longer than approximately 20 years.

While there is nothing inherently wrong with negative amortization in the context of a public plan, stakeholders should be aware of its consequences, especially for amortization periods substantially longer than 20 years. Negative amortization is a particular concern for plans using open, or rolling, amortization periods. As described above, plans that use open/rolling amortization methods “reset” to a new amortization period every year. By contrast, a plan using a closed amortization commits to paying down the UAAL over a fixed period.

Effective with the June 30, 2013 valuation the Board has elected to amortize the legacy unfunded liability as of June 30, 2013, over a closed 30-year period. New sources of unfunded liability will be explicitly amortized over closed 20-year periods. The amortization period for the deferred contributions from the 2010-2012 biennium will remain a 10-year closed period. These amortization periods reflect a shift to closed amortization periods and tiered successive 20-year closed periods for new sources of unfunded liability. This is a change from past VRS practice of using a 20-year rolling method. Effective with the June 30, 2016 valuation the Board confirms the continuation of the amortizations put in effect June 30, 2013 for all OPEB plans, with the exception of the LODA program, which, by statute, is currently not prefunded. For the purposes of accounting disclosures under GASB 43 and 45, the LODA program will continue to use an open 30- year period. In the event a change to the statutory contribution requirements of the LODA program necessitate an amortization period, the LODA program will, at that time, explicitly amortize new sources of unfunded liability over closed 20-year periods.

Effective November 20, 2019, the Board amends this policy to clarify that amortization periods of explicit bases may be shortened in an effort to pay off unfunded liabilities of either pensions or OPEBs earlier than originally scheduled.

Effective October 18, 2022, the Board amends this policy to set the amortization period for unfunded liabilities generated by elected plan amendments to be 10 years rather than 20 years.

8. Actuarial Assumptions

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Setting actuarial assumptions is critical to the funding of a plan. Forward-looking assumptions about plan demographics, wages, inflation, investment returns and more drive the measurement of liabilities and costs, and therefore affect funding. Unlike the selection of funding methods, which involves a fair degree of policy discretion, the selection of assumptions should be based solely on best estimates of actual future experience. While it may be tempting to set assumptions based on how they might affect current contribution requirements, such “results-based assumption setting” should be avoided. ***It is the plan’s actual experience that ultimately determines the cost of the benefits, so the assumptions should try to anticipate actual experience.*** Periodic reexamination of plan assumptions is an essential part of any plan’s actuarial processes. As a general rule, many plans conduct an experience study every three to five years, an interval that should help ensure that assumptions remain appropriate in the face of evolving conditions and experience. VRS reviews assumptions every four years as required under § 51.1-124.22(A)(4).

All assumptions should be consistent with Actuarial Standards of Practice and reflect professional judgment regarding future outcomes.

VRS plans to continue experience studies once every four years as required by § 51.1-124.22(A)(4) to determine whether changes in the actuarial assumptions are appropriate.

Appendix A contains a chart summarizing some of the current assumptions used for the various benefit plans managed by the VRS.

Appendix B is RBA 2013-07-18, which documents the approval of VRS funding policy assumptions.

Appendix C is RBA 2013-11-26, which documents the approval of revisions to the VRS funding policy assumptions for political subdivisions.

Appendix D is RBA 2016-06-15, which documents the approval of VRS funding policy methods and assumptions with regard to the OPEB plans.

Appendix E is RBA 2016-06-16, which documents the Board’s approval of changes to actuarial methods for certain OPEB plans.

Appendix F is RBA 2017-04-9, which documents the approval of VRS funding policy assumptions.

Appendix G is RBA 2019-10-13, which documents approval of a discount rate of 6.75% for actuarial valuations effective with the June 30, 2019 valuations.

Appendix H is RBA 2019 -11 -, which documents the approval of the use of shortened amortization periods for unfunded liabilities and maintaining prior contribution rates to assist in paying unfunded liabilities.

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9. Additional Considerations

Where the Funding Policy Statement as applied to a political subdivision would, in the Plan Actuary's opinion, not be expected to maintain the plan's solvency, the Board authorizes the VRS staff, working with the Plan Actuary, to determine alternative funding requirements that would maintain the plan's solvency while also meeting the other objectives as stated in the Board's funding policy.

1. **Additional Funding Contribution** - The Additional Funding Charge is the contribution rate needed, if necessary, to allow the local system to use the plan's assumed Investment Return Rate as its Single Equivalent Interest Rate (SEIR) under GASB Statement No. 67. The additional funding contribution rate, if needed, allows for the use of the 6.75% investment return as the single equivalent investment return assumption for purposes of the GASB 67/68 statements. To determine the SEIR, the Fiduciary Net Position (FNP) must be projected into the future for as long as there are anticipated benefits payable under the plan's provisions applicable to the members and beneficiaries of the system on the Measurement Date. If the FNP is not projected to be depleted at any point in the future, the long term expected rate of return on plan investments expected to be used to finance the benefit payments may be used as the SEIR. If the FNP is projected to be depleted, an Additional Funding Charge is developed to avoid depletion.
2. **Surcharge for "At Risk" Plans** – Political subdivision plans identified as potentially "at-risk" due to low funded levels may require an additional surcharge or shortened amortization periods to bring the funding level of the plan to a sustainable level as determined by the Plan Actuary.
3. **Limitation on Benefit Enhancements Increasing Liability** - ~~Benefit enhancements to a political subdivision pension plan that would have the effect of increasing the plan's liabilities by reason of increases in benefits, establishment of new benefits, changing the rate of benefit accrual, or changing the rate at which benefits become non-forfeitable may take effect during any plan year if the political subdivision's current funded ratio for such plan year would be at least 75 percent after taking into account such amendment.~~

In order to increase benefits in circumstances where the funded ratio would be less than 75 percent after taking into account the amendment, the political subdivision would be required to make a lump sum contribution in the amount necessary to bring the funding level to 75 percent as of the effective date of the change, in addition to any increase in annual funding due to plan enhancements.

Any accrued liability generated by the plan amendment that is not covered by the lump sum contribution will be amortized over no more than 10 years.

4. **Pension Plans for New Employers** – **Any new employer must have a funded status of at least 75 percent for pension benefits.** Any past service that is granted by the employer or purchased at the time the employer joins VRS must be at least 75 percent funded at the join date with the remaining amount amortized over no more than 10 years.

5. Health Insurance Credit (HIC) Elections –

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Any employer (new and existing VRS employers) that elects the HIC benefit is required to pay an initial contribution equal to the greater of two years of expected benefit payments or the amount required to reach at least 25 percent funded for its HIC plan, with the remainder of the unfunded liability amortized over no more than 10 years.

10. Conclusion

In funding defined benefit pension plans and OPEBs, governments must satisfy a range of objectives. In addition to the fundamental objective of funding the long-term costs of promised benefits to plan participants, governments also work to:

1. Keep employer's contributions relatively stable from year to year
2. Allocate pension costs on an equitable basis
3. Manage pension risks
4. Pay off unfunded liabilities over reasonable time periods

This Funding Policy was developed to help decision-makers understand the tradeoffs involved in reaching these goals and to document the reasoning that underlies the Board's decisions.

Adopted October 17, 2013

Amended November 14, 2013, June 7, 2016, November 15, 2017, ~~November 20, 2019,~~ and October 18, 2022

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Amended October 18, 2022

VRS Funding Policy Statement¹

1. Introduction

A plan funding policy determines how much should be contributed each year by employers and participants to provide for the secure funding of benefits in a systematic fashion.

The principal goal of a funding policy is to ensure that future contributions along with current plan assets are sufficient to provide for all benefits expected to be paid to members and their beneficiaries when due. The funding policy should seek to manage and control future contribution volatility to the extent reasonably possible, consistent with other policy goals. The actuarially determined contribution should be calculated in a manner that fully funds the long-term costs of promised benefits, while balancing the goals of 1) keeping contributions relatively stable and 2) equitably allocating the costs over the employees' period of active service.

The current funding policy used by the VRS Board sets contribution rates using the Entry Age Normal cost method, an investment return assumption of 6.75%, an inflation assumption of 2.5%, and a closed 20-year amortization period for unfunded liabilities (Legacy unfunded liabilities as of 6/30/13 are amortized over a closed 30-year amortization period.)

Article X, § 11 of the *Constitution of Virginia* provides that the Virginia Retirement System benefits shall be funded using methods which are consistent with generally accepted actuarial principles. Until 2012, the Annual Required Contribution (ARC) as described in the Governmental Accounting Standards Board's (GASB's) Statements No. 25 and No. 27 was a de facto funding policy for many public-sector retirement systems, including the Virginia Retirement System.

The Board sets contribution rates for all local employers under this policy. However, with respect to the plans for state employees and the teacher plan, while the rates developed under the Board's policy are the certified contribution rates, the Governor and the General Assembly determine the funding that they will provide through the state budget process toward the Board certified contribution rates for the State and Teachers and other statewide OPEB plans. Beginning in FY 2013, § 51.1-145.K1 of the Code of Virginia set out guidelines for the General Assembly to follow for the funding of the contribution rates certified by the VRS Board, phasing in from approximately 67% of Board-certified rate to 100% of the Board-certified rate over the next four biennia. These statutory guidelines do not apply to funding levels for Other Postemployment Benefits (OPEBs) administered by VRS.

¹ Adopted October 17, 2013; amended November 14, 2013, June 7, 2016, November 15, 2017, November 20, 2019, and October 18, 2022.

In June 2012, GASB revised public pension accounting standards and has communicated an important message in the process: accounting standards are no longer funding standards. However, GASB did not address how employers should calculate the annual required contribution (ARC). To assist state and local government employers, several national groups developed policy guidelines for funding standards. This document is the result of an extensive review of the current funding policy, industry standards and best practices, and the development and approval of funding policy assumptions effective with the June 30, 2013 valuation. A copy of Request for Board Action 2013-07-18 adopting the funding policy assumptions is attached. This Funding Policy is intended to provide guidance to future Boards on how to set employer contribution rates and support the plan's primary goals of contribution and budgetary predictability, accumulation of required assets over time to provide for all benefits earned and achievement of intergenerational equity.

In June 2015, GASB adopted two new statements regarding OPEBs. GASB statement 74, *Financial Reporting for Postemployment Benefits Other than Pension Plans*, and GASB statement 75, *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*. These statements replace GASB 43 and GASB 45. As was the case with GASB 67 and 68, these new statements represent a significant change to the methods used to account for postemployment benefits and provide for a clear separation between accounting for and funding of OPEBs. The new standards require the adoption of a new funding policy for OPEB plans. The current VRS funding policy has been modified to accommodate funding requirements for the VRS OPEB plans.

The VRS OPEB plans include the Health Insurance Credit Program, Group Life Insurance Program, the Virginia Sickness and Disability Program (VSDP), the Virginia Local Disability Program (VLDP) and the Long Term Care benefits associated with the VSDP and VLDP. The Line of Duty Act Fund is also a defined benefit OPEB plan, although it is not a benefit exclusively for VRS members.²

² As of April 2016 all VRS OPEBs already incorporate the actuarial methods outlined in the Funding Policy, with the following exceptions:

- Health Insurance Credit Program for Political Subdivisions will incorporate a five-year asset smoothing method for funding valuations effective with the June 30, 2016 actuarial valuation.
- The Long Term Care valuation will incorporate the Entry-Age Normal cost method and five-year smoothing method for funding valuations effective with the June 30, 2016 actuarial valuation.
- Line of Duty Act Program (LODA) is currently not prefunded and as set forth in the *Code* shall be funded on a current disbursement basis or in other words is considered a "pay-as-you-go" plan. As such, the plan has no unfunded liabilities and uses market value of assets for valuation purposes. In the event that the General Assembly takes action to begin prefunding this program, the Board of Trustees would move to adopt the various funding provisions contained in this document including moving the program to a five-year asset smoothing method for funding valuations effective with any decision to prefund the LODA program.

These changes were approved by the Board of Trustees at its June 7, 2016 meeting, and were incorporated into this amended Funding Policy. Where a particular actuarial method was already in use, the Funding Policy notes that the Board confirms the actuarial methods for OPEBs.

The Funding Policy addresses the following general policy objectives:

- Ensure funding of plans is based on actuarially determined contributions;
- Build funding discipline into the policy to ensure promised benefits can be paid;
- Maintain intergenerational equity so the cost of employee benefits is paid by the generation of individuals who receive services;
- Make employer costs a consistent percentage of payroll; and
- Require clear reporting to show how and when plans will be adequately funded.

This document serves as the Funding Policy for VRS. It has been prepared by VRS in collaboration with the Board and the VRS Plan Actuary and is effective as of the June 30, 2013 valuation, and modified to accommodate the OPEB plans effective as of the June 30, 2016 valuation.

2. Authority

The Virginia Retirement System is administered in accordance with Title 51.1, chapters 1, 2, 2.1, 3 and 4 of the *Code of Virginia*. The contribution to be paid by members of VRS is fixed at a level that covers only part of the cost of accruing benefits. The balance of the cost is paid by employers within the Trust Fund (the “Fund”).

The OPEB plans are administered in accordance with Title 51.1, chapters 5, 11, 11.1, and 14 of the *Code of Virginia*. The cost associated with OPEBs is generally borne by the employer and benefits are paid from the various trust funds. An exception to this practice is the Group Life Insurance Program. The Board determines the amount each insured shall contribute for the cost of insurance and by statute this amount is capped at \$0.70 per month for each \$1,000 of annual salary. Each employer determines whether this cost will be paid by the member or funded by the employer. The balance of the cost is paid by employers within the Fund. The Group Life Insurance plan, however, is a cost-sharing plan so all employers are charged the same rate.

The Funding Policy focuses on the pace at which these liabilities are funded and, in so far as is practical, the measures to ensure that employers pay for their own liabilities.

The Funding Policy is authorized by a framework that includes:

- Article X, § 11 of the *Constitution of Virginia*
- Title 51.1 of the *Code of Virginia*

This is the framework within which the VRS Plan Actuary carries out valuations to set employer contribution rates and provide recommendations to the Board when other funding decisions are required. The Funding Policy applies to all employers participating in the Fund.

The methods and assumptions used in the VRS funding policy are periodically reviewed as part of the quadrennial experience study as required under § 51.1-124.22(A)(4). As such, the content of this document may be updated to reflect changes approved by the VRS Board of Trustees.

3. Contributions

The Funding Policy provides for periodic employer contributions set at actuarially determined rates in accordance with recognized actuarial principles (§51.1-145(A)). Originally based on parameters set out in GASB 25/27 and GASB 43/45, the contribution should include the employer's normal cost and provisions for amortizing any unfunded actuarial accrued liability (UAAL) in accordance with the requirements originally defined in GASB 25/27 and GASB 43/45.

Member and employer contributions for retirement are required by §§ 51.1-144 and -145 of the *Code of Virginia*. Chapters 5, 11, 11.1, and 14 of Title 51.1 of the *Code of Virginia* and the applicable provisions in each year's Appropriation Act relate to contribution requirements for OPEB plans administered by VRS.

Employer contributions are normally made up of two main elements³:

- a) the estimated cost of future benefits being accrued, referred to as the "normal cost"; and
- b) an adjustment for the funding position of accrued benefits relative to the Fund's actuarially adjusted assets, or the "amortization payment UAAL." If there is a surplus there may be a contribution reduction; if there is a deficit, there will be a contribution addition, with the amount of surplus or deficit being spread over a number of years.

Items a) and b) above are then combined and expressed as a percentage of covered payroll.

Employer contribution rates are set each biennium and are in effect for the entire biennium. Valuations in the "off" years are for informational purposes only. Generally, employers with well-funded pension plans consistently pay their annual required contribution in full.

Where this process as applied to a political subdivision would, in the Plan Actuary's opinion, not be expected to maintain the plan's solvency, the VRS staff, working with the Plan Actuary, may determine alternative funding requirements that would maintain the political subdivision's solvency while also meeting the other objectives of this Funding Policy Statement.

With respect to statewide plans, if unfunded liabilities exist in a plan, the Board may recommend alternative contribution rates in excess of the actuarially determined rates if opportunities exist to accelerate paydown of unfunded liabilities. Examples of alternative rates could potentially include approaches such as maintaining rates from the prior year if rates drop in subsequent rate setting or maintaining a higher level contribution rate until a certain funded status is achieved.

³ Contributions also include administrative expenses.

4. Funding Target

VRS operates the same target funding level for all ongoing employers of 100% of its accrued liabilities valued on an ongoing basis. This means that contribution rates are set with the intent of funding 100% of a member's benefits during a member's working lifetime. The Line of Duty Act Fund is an exception, as employer contributions are currently determined by the Board on a current disbursement basis per statute. As such, the target funding level for all ongoing employers for LODA is at or near 0% of its accrued liabilities.

Funded Status is defined as the ratio of the actuarial value of assets to the value placed on the benefits, or plan's liabilities, by the VRS Plan Actuary. The VRS Plan Actuary reports on the funded status of each plan in the system in each annual valuation.

5. Actuarial Cost Method

The actuarial cost method is the means by which the total present value of all future benefits for current active and retired participants is allocated to each year of service (i.e., the "normal cost" for each year) including past years (i.e., the "actuarial accrued liability"). There are several available actuarial cost methods, but most governmental plans use the entry age normal (EAN) cost method while a significant minority use the projected unit credit (PUC) method. In the past, VRS has used the EAN method for most of the plans it administers.

Although the EAN and PUC cost methods are both considered reasonable under actuarial standards of practice and GASB 25 and GASB 43 in most circumstances, it is important for plan stakeholders to understand the implications of either method. EAN tends to recognize actuarial liabilities sooner than PUC, and it also tends to result in a more stable normal cost pattern over time for pay-related benefits, even in the face of demographic shifts. The more stable normal cost pattern over time should help in reducing the risk of higher levels of future contributions.

Under the PUC method, the plan's normal cost is the present value of the benefits "earned" during the year, but based on projected pay levels at retirement. For an individual participant, the PUC normal costs increase each year because the present value increases as the participant gets a year closer to retirement. In contrast, under the EAN method, the normal cost is specifically determined to remain a level percentage of pay over each participant's career.

Because EAN normal cost rates are level for each participant, the normal cost pattern for the entire plan under EAN is more stable for pay-related benefits in the face of demographic shifts in the workforce. It is this normal cost stability that makes the EAN method the preferred funding method for pay-related benefits of public plans.

GASB has reaffirmed its decision to require governmental pension plans to base their financial statement reporting on the EAN method. For comparability, GASB has also decided to require governmental OPEB plans, which may not provide pay-related benefits, to base their financial statement reporting on the EAN method.

Effective with the June 30, 2013 valuation, the Board has adopted the Entry-Age Normal cost method in deriving plan liabilities. This is a continuation of the Board's existing cost method. Effective with the June 30, 2016 valuation, the Board has adopted the Entry-Age Normal cost method for all OPEB plans.

6. Asset Valuation Method

Because investment markets are volatile and because pension plans typically have long investment horizons, asset-smoothing techniques can be an effective tool to manage contribution volatility and provide a more consistent measure of plan funding over time. Asset-smoothing methods reduce the effect of short-term market volatility on contributions, while still tracking the overall movement of the market value of plan assets, by recognizing the effects of investment gains and losses over a period of years. This is also in keeping with § 51.1-145(A), which requires that contribution rates be determined in a manner so as to remain relatively level from year to year.

Determining the ideal asset-smoothing policy involves balancing the two goals of ensuring fairness across generations and controlling contribution volatility for plan sponsors. A very long smoothing period will greatly reduce contribution volatility, but this may mean the impact of recent investment experience is deferred to future generations. However, a very short smoothing period (or none at all) may result in contribution requirements that fluctuate dramatically from year to year.

Such volatility may also result from an asset-smoothing method that constrains how far the smoothed value differs from the market value by imposing a market value "corridor." A corridor is typically expressed as a ratio of the smoothed value of assets to the market value of assets. Actuarial standards of practice and related actuarial studies seek to identify asset-smoothing methods that achieve a reasonable balance between how long it takes to recognize investment experience (the smoothing period) and how much smoothing is allowed in the meantime (the corridor). The resulting smoothing periods are in the range of three to 10 years (with five the most common) and a corridor wide enough to allow the smoothing method to function except in the most extreme conditions.

While the smoothing period for governmental plans is not limited by federal laws or regulations, the Actuarial Standards Board has set out principles for asset smoothing in ASOP No. 44. Under these principles, when a smoothed asset valuation method is used, the actuary should select a method so that the smoothed asset values fall within a reasonable range of the corresponding market values and any differences between the actuarial value and market value of assets should be recognized within a reasonable period.

Effective with the June 30, 2013 valuation, the Board has adopted a five-year asset smoothing period, which also includes a corridor that will restrict the smoothed value from falling below 80% of the true market value or exceeding 120% of the true market value. This is a continuation of the Board's existing asset valuation method. Effective with the June 30, 2016 valuation, the Board has adopted the same asset smoothing period and corridors for the OPEB plans, with the exception of the LODA program, which, by statute, does not prefund benefits. In the event a change to the statutory contribution requirements

of the LODA program necessitate an asset valuation method, the same asset smoothing period and corridors should be applied to the LODA program at that time.

7. Amortization Method

Amortization of unfunded liabilities is a major component of the annual contribution. Amortization policies involve a balance between controlling contribution volatility and ensuring a fair allocation of costs among generations. The Plan Actuary uses the specific amortization periods adopted by the Board for all employers when developing a method over which to pay down any unfunded liabilities that may exist. The amortization period should allow adjustments to contributions to be made over periods that appropriately balance intergenerational equity against the goal of keeping contributions level as a percentage of payroll over time as required by § 51.1-145.

Amortization of the unfunded actuarial accrued liability (UAAL) determines how current and future UAAL will be paid off or “amortized,” and so includes how changes in benefits or actuarial assumptions that affect the actuarial accrued liability should be funded over time. Even more than with asset smoothing methods, amortization policies involve a balance between controlling contribution volatility and ensuring a fair allocation of costs among generations. Longer amortization periods help keep contributions stable, but excessively long periods may inappropriately shift costs to future generations. In seeking to achieve an appropriate balance between these two important policy goals, a comprehensive amortization policy will involve the following distinct elements:

- Payment basis
- Payment structure
- Amortization period

A. Payment Basis: Level Dollar vs. Level Percent of Pay

One of the first considerations is whether amortization payments will be set at a level dollar amount (similar to a home mortgage) or as a level percent of pay. The great majority of public pension plans use level-percent-of-pay amortization where the payments toward the UAAL increase each year at the same rate as is assumed for payroll growth. Compared with the level-dollar approach, payments start at a lower dollar amount under the level percent approach, but then increase in proportion to payroll. The level-dollar method is more conservative in that it funds the UAAL faster in the early years. However, the level-percent-of-pay approach is consistent with the pay-related structure of benefits under most public plans. Moreover, because the normal cost is also determined as a level percent of pay, level percent amortization provides a total cost that remains level as a percentage of pay. In contrast, level-dollar amortization of UAAL will produce a total cost that decreases as a percentage of pay over the amortization period. A plan should balance these considerations in choosing between level-percent and level-dollar amortization. Section 51.1-145(A) of the *Code of Virginia* provides in part that “[t]he total annual employer contribution for each employer, expressed as a percentage of the annual membership payroll, shall be determined in a manner so as to remain relatively level from year to year....”

Effective with the June 30, 2013 valuation the Board has elected to use the level percent of pay payment basis. This is consistent with historical VRS practice. Effective with the June 30, 2016 valuation the Board confirms the continued use of the level percent of pay payment basis put in effect June 30, 2013 for the OPEB plans when an actuarially determined contribution is calculated.

B. Payment Structure

Amortization policy must also consider how amortization payments should be structured. For example, a determination needs to be made as to whether the entire UAAL should be aggregated and amortized as a single amount, or whether the plan should track individual bases for each source of UAAL or surplus each year, and amortize these separately. Amortization periods can be fixed, open or “rolling” (with the amortization period restarted each year).

Although use of a single amortization base provides simplicity, use of separate amortization bases for each source of UAAL has the advantage of tracking separately each new portion of UAAL and providing another mechanism to stabilize contribution rates. Under this approach, over time there will be a series of bases, one for each year’s gain or loss as well as for any other changes in UAAL. This provides useful information to stakeholders, as they can view the history of the sources of a plan’s UAAL in any year. The use of separate amortization bases should help balance the annual ups and downs in the UAAL. In practice, the number of bases will be limited by the length of the amortization period as eventually bases will be fully amortized, and so will no longer be part of the UAAL.

Fixed amortization periods identify a date certain by which each portion of the UAAL will be funded. This can be contrasted with open or rolling amortization, whereby the plan “resets” its amortization period every year. This is analogous to a homeowner who refinances his mortgage each year. Although both methods are common in current practice, fixed amortization periods have the advantage of providing stakeholders with a clearer understanding of the ultimate funding target (full funding) and the path to get there. It is the structure required for private sector pensions, and is increasingly common for public pension plans.

Effective with the June 30, 2013 valuation the Board has elected to use individual bases for each source of UAAL or surplus each year and to use fixed amortization periods rather than open or rolling periods. This is a change from past VRS practice but is consistent with industry best practices. Effective with the June 30, 2016 valuation the Board confirms the continued use of individual bases for each source of UAAL or surplus each year and the use of fixed amortization periods rather than open or rolling periods put in effect June 30, 2013 for all OPEB plans, with the exception of the LODA program, which, by statute, is currently not prefunded. For the purposes of accounting disclosures under GASB 43 and 45, the LODA program will continue to use an open period. In the event a change to the statutory contribution requirements of the LODA program necessitate a payment structure, individual bases for each source of UAAL or surplus each year and fixed amortization periods, rather than open or rolling periods, will be used by the LODA program at that time.

C. Amortization period

Amortization period is a determination of the appropriate period of time over which amortization should occur. The answer can depend on the source of the UAAL being amortized, as discussed below:

UAAL Due to Actuarial Gains/ Losses

Actuarial gains and losses arise when there is a difference between the actuary's estimates (assumptions) and the actual experience of the plan. They can result from demographic experience (e.g., the number of new retirees is higher or lower than expected), investment experience (e.g., returns that are higher or lower than expected), or other economic experience (e.g., payroll growth that is higher or lower than expected). In determining the appropriate period for amortizing gains and losses, plan sponsors should strike a balance between reducing contribution volatility (which would lead to longer amortization periods) and maintaining a closer relationship between contributions and routine changes in the UAAL (which would lead to shorter amortization periods). For many plans, amortization periods in the range of 15 to 20 years for gains and losses would assist plans in achieving a balance between these objectives.

UAAL Due to Changes in Actuarial Assumptions

Assumption changes will result in an increase or decrease in the UAAL. Unlike gains and losses, which reflect actual past experience, assumptions are modified when future expectations about plan experience change. This amounts to taking the effect of future expected gains or losses and building it into the cost today. For that reason, and because of the long-term nature of assumption changes, a plan could be justified in using a longer amortization period than that used for actuarial gains or losses, perhaps in the range of 15 to 25 years.

Amortization of UAAL Due to Plan Amendments

Because plan amendments are under the control of the plan sponsor, managing contribution volatility is generally not a consideration for plan amendments. This means that the primary rationale in selecting the period is to support intergenerational equity by matching the amortization period to the demographics of the participants receiving the benefit. This leads to shorter, demographically based amortization periods. For active participants, this could be the average future working lifetime of the active participants receiving the benefit improvement, while for retirees, this could be the average life expectancy of the retired participants receiving the benefit improvement. This approach would usually result in no longer than a 15-year amortization period for benefit improvements.

An equitable amortization policy should ensure that the UAAL will be paid off in a reasonable period of time. Long amortization periods can make paying down the UAAL appear more affordable, but, because interest charges accrue and compound on the unpaid UAAL, it is prudent to set amortization periods that are not excessively long. This is especially important where level

percent of pay amortization is used.

In an effort to balance the need to pay down the current unfunded liability while managing already increasing contribution rates, the Board elected to manage the paydown of any unfunded liabilities created prior to June 30, 2013 over a 30-year closed period. In an effort to better manage intergenerational equity and to build funding discipline into the VRS policy, the Board also decided that future unfunded liabilities would be best amortized over 20-year closed periods.

With long amortization periods, the UAAL may increase during the early years of amortization period, even though contributions are being made to amortize the UAAL. This phenomenon, known as “negative amortization”, occurs only with level percent of pay amortization. This happens because, under level percent of pay amortization, the lower early payments can actually be less than interest on the outstanding balance, so that the outstanding balance increases instead of decreases. For typical public plans, this happens whenever the average amortization period is longer than approximately 20 years.

While there is nothing inherently wrong with negative amortization in the context of a public plan, stakeholders should be aware of its consequences, especially for amortization periods substantially longer than 20 years. Negative amortization is a particular concern for plans using open, or rolling, amortization periods. As described above, plans that use open/rolling amortization methods “reset” to a new amortization period every year. By contrast, a plan using a closed amortization commits to paying down the UAAL over a fixed period.

Effective with the June 30, 2013 valuation the Board has elected to amortize the legacy unfunded liability as of June 30, 2013, over a closed 30-year period. New sources of unfunded liability will be explicitly amortized over closed 20-year periods. The amortization period for the deferred contributions from the 2010-2012 biennium will remain a 10-year closed period. These amortization periods reflect a shift to closed amortization periods and tiered successive 20-year closed periods for new sources of unfunded liability. This is a change from past VRS practice of using a 20-year rolling method. Effective with the June 30, 2016 valuation the Board confirms the continuation of the amortizations put in effect June 30, 2013 for all OPEB plans, with the exception of the LODA program, which, by statute, is currently not prefunded. For the purposes of accounting disclosures under GASB 43 and 45, the LODA program will continue to use an open 30- year period. In the event a change to the statutory contribution requirements of the LODA program necessitate an amortization period, the LODA program will, at that time, explicitly amortize new sources of unfunded liability over closed 20-year periods.

Effective November 20, 2019, the Board amends this policy to clarify that amortization periods of explicit bases may be shortened in an effort to pay off unfunded liabilities of either pensions or OPEBs earlier than originally scheduled.

Effective October 18, 2022, the Board amends this policy to set the amortization period for unfunded liabilities generated by elected plan amendments to be 10 years rather than 20 years.

8. Actuarial Assumptions

Setting actuarial assumptions is critical to the funding of a plan. Forward-looking assumptions about plan demographics, wages, inflation, investment returns and more drive the measurement of liabilities and costs, and therefore affect funding. Unlike the selection of funding methods, which involves a fair degree of policy discretion, the selection of assumptions should be based solely on best estimates of actual future experience. While it may be tempting to set assumptions based on how they might affect current contribution requirements, such “results-based assumption setting” should be avoided. ***It is the plan’s actual experience that ultimately determines the cost of the benefits, so the assumptions should try to anticipate actual experience.*** Periodic reexamination of plan assumptions is an essential part of any plan’s actuarial processes. As a general rule, many plans conduct an experience study every three to five years, an interval that should help ensure that assumptions remain appropriate in the face of evolving conditions and experience. VRS reviews assumptions every four years as required under § 51.1-124.22(A)(4).

All assumptions should be consistent with Actuarial Standards of Practice and reflect professional judgment regarding future outcomes.

VRS plans to continue experience studies once every four years as required by § 51.1-124.22(A)(4) to determine whether changes in the actuarial assumptions are appropriate.

Appendix A contains a chart summarizing some of the current assumptions used for the various benefit plans managed by the VRS.

Appendix B is RBA 2013-07-18, which documents the approval of VRS funding policy assumptions.

Appendix C is RBA 2013-11-26, which documents the approval of revisions to the VRS funding policy assumptions for political subdivisions.

Appendix D is RBA 2016-06-15, which documents the approval of VRS funding policy methods and assumptions with regard to the OPEB plans.

Appendix E is RBA 2016-06-16, which documents the Board’s approval of changes to actuarial methods for certain OPEB plans.

Appendix F is RBA 2017-04-9, which documents the approval of VRS funding policy assumptions.

Appendix G is RBA 2019-10-13, which documents approval of a discount rate of 6.75% for actuarial valuations effective with the June 30, 2019 valuations.

Appendix H is RBA 2019 -11 -, which documents the approval of the use of shortened amortization periods for unfunded liabilities and maintaining prior contribution rates to assist in paying unfunded liabilities.

9. Additional Considerations

Where the Funding Policy Statement as applied to a political subdivision would, in the Plan Actuary's opinion, not be expected to maintain the plan's solvency, the Board authorizes the VRS staff, working with the Plan Actuary, to determine alternative funding requirements that would maintain the plan's solvency while also meeting the other objectives as stated in the Board's funding policy.

1. **Additional Funding Contribution** - The Additional Funding Charge is the contribution rate needed, if necessary, to allow the local system to use the plan's assumed Investment Return Rate as its Single Equivalent Interest Rate (SEIR) under GASB Statement No. 67. The additional funding contribution rate, if needed, allows for the use of the 6.75% investment return as the single equivalent investment return assumption for purposes of the GASB 67/68 statements. To determine the SEIR, the Fiduciary Net Position (FNP) must be projected into the future for as long as there are anticipated benefits payable under the plan's provisions applicable to the members and beneficiaries of the system on the Measurement Date. If the FNP is not projected to be depleted at any point in the future, the long term expected rate of return on plan investments expected to be used to finance the benefit payments may be used as the SEIR. If the FNP is projected to be depleted, an Additional Funding Charge is developed to avoid depletion.
2. **Surcharge for "At Risk" Plans** – Political subdivision plans identified as potentially "at-risk" due to low funded levels may require an additional surcharge or shortened amortization periods to bring the funding level of the plan to a sustainable level as determined by the Plan Actuary.
3. **Limitation on Benefit Enhancements Increasing Liability** - Benefit enhancements to a political subdivision pension plan that would have the effect of increasing the plan's liabilities by reason of increases in benefits, establishment of new benefits, changing the rate of benefit accrual, or changing the rate at which benefits become non-forfeitable may take effect during any plan year if the political subdivision's current funded ratio for such plan year would be at least 75 percent after taking into account such amendment.

In order to increase benefits in circumstances where the funded ratio would be less than 75 percent after taking into account the amendment, the political subdivision would be required to make a lump sum contribution in the amount necessary to bring the funding level to 75 percent as of the effective date of the change, in addition to any increase in annual funding due to plan enhancements.

Any accrued liability generated by the plan amendment that is not covered by the lump sum contribution will be amortized over no more than 10 years.

4. **Pension Plans for New Employers** –
Any new employer must have a funded status of at least 75 percent for pension benefits.
Any past service that is granted by the employer or purchased at the time the employer joins VRS must be at least 75 percent funded at the join date with the remaining amount amortized over no more than 10 years.
5. **Health Insurance Credit (HIC) Elections** –

Any employer (new and existing VRS employers) that elects the HIC benefit is required to pay an initial contribution equal to the greater of two years of expected benefit payments or the amount required to reach at least 25 percent funded for its HIC plan, with the remainder of the unfunded liability amortized over no more than 10 years.

10. Conclusion

In funding defined benefit pension plans and OPEBs, governments must satisfy a range of objectives. In addition to the fundamental objective of funding the long-term costs of promised benefits to plan participants, governments also work to:

1. Keep employer's contributions relatively stable from year to year
2. Allocate pension costs on an equitable basis
3. Manage pension risks
4. Pay off unfunded liabilities over reasonable time periods

This Funding Policy was developed to help decision-makers understand the tradeoffs involved in reaching these goals and to document the reasoning that underlies the Board's decisions.

Adopted October 17, 2013

Amended November 14, 2013, June 7, 2016, November 15, 2017, November 20, 2019, and October 18, 2022

Report

The Administration and Personnel Committee met on October 18, 2022 and discussed the following:

APPROVAL OF MINUTES

The Committee approved the minutes of its September 14, 2022 meeting.

REVISIONS TO THE INVESTMENT PROFESSIONALS' PAY PLAN

Michael Cooper, Chief Operating Officer, reviewed changes to the Investment Professionals' Pay Plan. The revisions are based on the recent McLagan Investment Pay Review and include decreasing the Senior Investment Analyst investment compensation target from 25% to 20% and increasing the Investment Analyst investment compensation target from 5% to 10%.

The Committee recommends approval of the following action to the full Board:

Request for Board Action: *The VRS Board of Trustees approves an amended Investment Professionals' Pay Plan ("Pay Plan"), effective October 18, 2022.*

APPOINTMENT AND REAPPOINTMENT OF INVESTMENT ADVISORY COMMITTEE (IAC) MEMBERS

Ron Schmitz, Chief Investment Officer, advised the Committee of IAC member terms that are expiring. Theodore Economou, Thomas Gayner and Lawrence Kochard are interested in continuing to serve on the IAC. Palmer Garson has agreed to fill the expiring term held by Deborah Allen-Hewitt.

The Committee recommends approval of the following action to the full Board:

Request for Board Action: *The VRS Board of Trustees approves the reappointment of Theodore Economou, Thomas Gayner and Lawrence Kochard to the Investment Advisory Committee, each for a two-year term ending September 13, 2024, February 19, 2025 and February 16, 2025, respectively, and appoint Palmer P. Garson for a two-year term ending October 16, 2024.*

REVIEW REVISED GOVERNANCE POLICY AND COMMITTEE CHARTERS

Cindy Wilkinson, Director of Policy, Planning and Compliance, reviewed proposed revisions to the Board's governance policy and Committee charters. At its last meeting, the A&P Committee agreed to a staff recommendation to rename the committee to the Administration, Finance and Talent Management Committee (AFT). The revisions to the governance documents update the Committee's name. Ms. Wilkinson advised the Committee that the Board is required to review the changes twice before taking final action.

Submitted to the Board of Trustees on October 18, 2022.

A. Scott Andrews, Chair
Administration and Personnel Committee



Approve changes to Investment Professionals' Pay Plan.

Requested Action

The Virginia Retirement System Board of Trustees approves an amended Investment Professionals' Pay Plan ("Pay Plan"), effective October 18, 2022.

Description/Background

The VRS Board of Trustees approved the current Pay Plan on June 23, 2022.

The proposed amendment accounts for a change in the incentive compensation calculation for certain Investments staff based on the McLagan Investment Pay Review dated April 2022, to better align with market indicators. The changes include:

- Decreasing the Senior Investment Analyst investment compensation target from 25% to 20%.
- Increasing the Investment Analyst investment compensation target from 5% to 10%.

A blacklined version of the revised Pay Plan is attached.

Authority for Requested Action

Code of Virginia § 51.1-124.22(A)(11) authorizes the Board to establish and administer a compensation plan for officers and employees of the Retirement System.

The above action is approved.

A. Scott Andrews, Chair
VRS Board of Trustees

Date



**VIRGINIA RETIREMENT SYSTEM
INVESTMENT PROFESSIONALS'
PAY PLAN
Effective October 18, 2022**

Investment Professionals' Pay Plan Effective October 18, 2022

OVERVIEW & PAY PHILOSOPHY

The Virginia Retirement System's (VRS) Board of Trustees has designed this investment professionals' pay plan after working with an independent compensation consultant. In addition, the Board has adopted benchmarks, recommended by an independent investment consultant, to be used as part of this pay plan.

This pay plan includes three core elements:

- Base Salary (described in Section I of this document)
- Incentive Pay Plan (described in Section II)
- Deferred Compensation Plan for VRS Investment Management Personnel (DCPIP) (described in Section III)

Overall, this pay plan is designed to:

- Attract, motivate and retain skilled investment professionals by offering competitive compensation opportunities.
- Directly align compensation with long-term, superior relative and absolute investment performance.
- Reinforce risk management priorities and standards.
- Attract and retain senior investment professionals by deferring a portion of incentive compensation on a tax-deferred basis.
- Benefit all stakeholders – VRS' beneficiaries, VRS' employees, and Virginia's taxpayers – through a compensation plan that is clear, aligned with performance, competitive and cost effective.

Importantly, this pay plan anchors on two broad and long-standing philosophical principles:

1. VRS should pay base salaries consistent with the 75th percentile of a peer group of other leading public funds. The primary guidelines for determining VRS' leading public fund peer group will be (1) funds of similar size (AUM) as VRS and (2) funds with significant (>25%) assets managed internally. Additional criteria the Board may consider is asset allocation / diverse portfolio similar to VRS, degree of delegation to the CIO and staff, use of outside investment consultants, and Board pay decision making authority.
2. VRS should provide incentive compensation opportunities such that, in combination with base salary, total compensation levels approximate the median (50th percentile) of a blended group weighted 75% to the total compensation levels of leading peer group public funds and 25% to the total compensation levels of a broad range of private-sector firms that employ investment professionals.

I. Base Salary

SALARY RANGES

This pay plan establishes a salary range for each job class taking into account its relative importance to VRS and the salaries paid for comparable types of jobs in other leading public funds. Minimum, midpoint, and maximum salary rates define the salary range for each job class/position. The midpoint of each job class/position approximates the 75th percentile of salaries of a peer group of leading public pension funds. Actual salaries can be higher or lower than the midpoint depending on factors such as job performance, professional education and certifications, the willingness to assume new and higher-level duties and responsibilities, the ability to learn quickly and apply new knowledge and skills, being a team player, and the length of time in the position.

Each position's salary range includes a defined:

- **Minimum** - the lowest base salary paid for a job within the job class/position.

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- **Midpoint** - represents the market salary paid to a fully qualified employee, who has the institutional knowledge and practical experience to fulfill independently all of the responsibilities of the job/position.
- **Maximum** - the highest salary rate for the job class/position.

Grade	Position	Salary Range (\$ Thousands)		
		Min (\$)	Mid (\$)	Max (\$)
10	Chief Investment Officer/Chief Managing Director	325	430	540
9	Managing Director	275	365	455
8	Program Director	235	315	395
7	Director – Strategy, Research, Risk and/or Investment Decision Support	205	275	345
6	Senior Portfolio Manager	205	275	345
5	Portfolio Manager	160	215	270
4	Senior Investment Officer	135	180	225
3	Investment Officer	105	140	175
2	Senior Investment Analyst	80	105	130
1	Investment Analyst	65	85	105

In considering the above salary range, it important to note the following:

- **Market Pay Reviews:** The VRS normally conducts a comparative market total pay study generally every two to three years to ensure competitiveness of the salary and incentive structures. Typically, the VRS conducts the study in the 1st quarter of the calendar year with an effective date of July 1 (the beginning of the fiscal year).
- **Changes in Salary Ranges:** The Board must approve changes to the salary scale and incentive structure.

Salary Adjustments

Oversight & Administration

VRS will implement pay actions consistent with the provisions of the Appropriation Act. The VRS Board, however, approves across-the-board performance-based salary increases, market-based salary increases and incentive pools, for VRS investment professionals, consistent with the Code of Virginia and the Appropriation Act. The Chief Investment Officer (CIO) approves salary adjustments for individual investment professionals and, as described later in this document, sign-on bonuses, incentive payments, and relocation expenses subject to the limitations in the Code of Virginia and other applicable state or federal law and regulation.

Merit Increases

- Salary increases are based on meeting individual performance standards. The supervisor completes the evaluation after the end of the fiscal year. If a participant in the investment employees’ pay plan does not meet overall performance standards, then the participant is ineligible for performance increases to their base salary and market adjustments to their base salary for that performance cycle. Performance cycles are on a fiscal year basis (July 1 through June 30) and typically begin with an effective date of performance plans in the first quarter of the new fiscal year.
- The CIO will receive base salary increases as approved by the VRS Board of Trustees and in accordance with the terms in the CIO’s Employment Agreement, with approved effective dates established by the VRS Board of Trustees.

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Starting Salaries

The starting salary for a new employee considers the rates presently paid to other employees in the department and those in the same job class (when applicable), the candidate's education, skills, work experience, and salary history. The starting salary normally does not exceed the salary grade midpoint.

Reallocation

Occurs when a job classification is reviewed by Human Resources and it is determined that the job duties and responsibilities have changed significantly enough to place the job in a different job title and job class. Unless the CIO authorizes an exception, this would not exceed a 15% increase. However, the individual's salary will always be at least at the minimum of the range of the new job, regardless of the amount of the increase.

In-grade Adjustments

Occur to ensure competitiveness, retention, and to recognize increased skills, abilities, knowledge, obtainment of a degree or certification, or significant increases in responsibilities within the job class. Unless the CIO authorizes an exception, adjustments will not exceed a 10% increase.

Promotions

Promotions occur when an individual moves into a position in a higher job class. Promotions can be competitive (selected through a recruitment and hiring process) or non-competitive (through a job reclassification or reallocation). Unless the CIO approves an exception, promotions will not exceed a 15% increase. However, the individual's salary will always be at least at the minimum of the range of the new job, regardless of the amount of the increase.

Downward Assignment

Downward adjustment occurs when an employee changes positions whether voluntarily, or because of unsatisfactory performance, resulting in a downward change in job class. A reduction in salary may occur based on a review of the salary and range and the circumstances associated with the downward move. In downward assignments, an individual's salary cannot exceed the maximum of the new salary range.

II. Incentive Pay Plan

PLAN ADMINISTRATION

The VRS Board of Trustees, the Plan Administrator, through the Administration and Personnel (A&P) Committee, administers the Incentive Plan (Plan) and retains full and complete discretion:

- To increase or decrease incentives for any and/or all Plan participants.
- To modify, amend or rescind any aspect of the Plan at any time for any and/or all Plan participants.
- While the Plan Administrator remains mindful of the value that staff adds to the organization and supportive of the pay plan, the Plan Administrator also specifically reserves the right to cancel, reduce, or delay the amount of any incentives payable under this plan when, in the sole discretion of the Plan Administrator, extreme budgetary pressures, economic, market or other conditions are such that the Plan Administrator deems such action necessary under the circumstances.
- Consistent with the preceding paragraph, payment of incentives under this plan is not guaranteed.

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The Plan Administrator may delegate certain aspects of this Plan’s day-to-day operation to the VRS CIO and the VRS Director of Human Resources. However, any substantive Plan-related questions or issues impacting incentive payouts for the CIO require the Plan Administrator’s prior approval.

PLAN ELIGIBILITY

Incumbents in the positions listed below are eligible to participate in this incentive plan, provided they:

- Are active VRS employees.
- Work for VRS at least forty hours per week. Plan participants who work less than full-time may be eligible to receive a prorated incentive payment. Wage employees are not eligible to participate in the plan.
- Receive an individual performance evaluation of at least “meets expectations” for the relevant performance year (i.e., the year preceding the normally scheduled year of payment).
- Remain in compliance with the VRS Investment Department Code of Ethics and Standards of Professional Conduct Policy.

Positions Eligible to Participate in the Investment Professional’s Pay Plan
Chief Investment Officer/Chief Managing Director
Managing Director – Portfolio Solutions Group
Managing Director – Private Market Assets and DC Plans
Managing Director – Public Market Assets
Program Director
Director – Strategy, Research, Risk and/or Investment Decision Support
Senior Portfolio Manager
Portfolio Manager
Senior Investment Officer
Investment Officer
Senior Investment Analyst
Investment Analyst

The CIO will determine the design of the incentive plan structure for the positions supporting the Defined Contribution Plans, with both quantitative and qualitative elements.

Generally, employees on an approved leave of absence are considered active employees. The CIO will resolve all questions regarding eligibility, or in the case of the CIO, eligibility will be determined by the Board.

Participation in this Plan in any one year does not confer the right to participate in this Plan in any other year or to receive Plan payouts for the current and/or any future year. Participation in this Plan does not confer the right to continued employment. Subject to the provisions of this Plan, only active VRS employees may receive payments under this Plan.

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OVERALL INCENTIVE PLAN MECHANICS

As described in more detail throughout this document, under the terms of this Plan:

- Eligible Plan participants will be assigned an incentive opportunity, expressed as a percentage of their actual earned base salary.
- Incentive opportunities vary by position, with the level of such opportunities increasing with the degree to which the position directly affects VRS' investment performance.
- Incentives are weighted or allocated to separate Plan components, described below, with the specific components and weightings varying by position:
 1. Total Fund relative investment performance
 2. Asset Class relative investment performance
 3. Average of Asset Class Multipliers (for positions that support multiple asset classes)
 4. Qualitative – focuses on individual achievement of assigned objectives.
- After year-end, payouts under each Plan component would be determined based on performance.
- Each participant's preliminary award would equal the sum of all of their performance adjusted Plan components.
- Final awards would equal preliminary awards adjusted, up or down, based on the Total Fund's one-year absolute return. Specifically, there will be no adjustment for returns between 0% and the assumed rate of return, currently 6.75%. There will be a positive one-for-one adjustment for returns in excess of the assumed rate of return (e.g., if Total Fund one-year actual absolute return equals +9.75%, then the preliminary awards will be increased by 3%). There will be a negative one-for-one adjustment for a return less than 0% (e.g., if Total Fund one-year actual absolute return equals -15%, then the preliminary awards will be reduced by 15%). This adjustment is specifically intended to systematically take into account, in the shorter term, the effect of market cycles on the health of the pension plan by providing a mechanism to reflect the impact of up and down markets on incentive compensation.
 - 50% of eligible senior staff-members' awards (up to IRS limits) will be deferred into tax-qualified accounts. See section III, Defined Contribution Incentive Plan for VRS Investment Management Personnel (DCPIP). While deferred, awards are subject to the Total Fund's annual absolute return.
 - All other awards paid in cash.

Generally, a Participant must be employed on the date of payment of the award. However, see INCENTIVE PLAN PROVISIONS, *Termination of Employment Due to Death, Disability or Retirement*.

INCENTIVE OPPORTUNITIES

Incentive opportunities will vary by position based on multiple criteria:

- The position's potential effect on the VRS' investment performance.
- Competitive market pay requirements.
- Internal equity considerations.
- Other factors determined by the CIO or, in the case of the Chief Investment Officer's position, by VRS' Board.

Actual awards can vary based on performance.

For the fiscal year ending June 30, 2023, and all subsequent years, unless as otherwise determined, the Plan's incentive opportunities are as follows:

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Incentive Levels	
VRS Position	Incentive¹ (% Salary)
Chief Investment Officer	70 ²
Chief Managing Director	70 ²
Managing Director – Portfolio Solutions Group	65 ²
Managing Director – Private Market Assets and DC Plans	65 ²
Managing Director – Public Market Assets	65 ²
Program Director	60 ²
Director – Strategy, Research, Risk and/or Investment Decision Support	50
Senior Portfolio Manager	50
Portfolio Manager	40
Senior Investment Officer	30
Investment Officer	30
Senior Investment Analyst	20
Investment Analyst	10

¹Performance-adjusted preliminary awards can vary from zero to two times the incentive.

²A portion, up to 50%, of the positions' earned incentives is subject to mandatory deferral.

INCENTIVE WEIGHTINGS

Each participant's incentive award will be weighted or allocated to separate, stand-alone Plan components. Importantly, all participants have a portion of their incentive opportunities weighted:

- To the Total Fund Plan component – which helps reinforce the importance of collective success as measured by the Total Fund's relative investment results.
- To the Qualitative Plan component – this helps reinforce achievement of specific initiatives and professional development.

Described below are the specific Plan weightings and the approach for determining awards under each of these Plan components.

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Incentive Weightings by Plan Component					
VRS Position	Total Fund %	Asset Class Multipliers %	Asset Class %	Qualitative %	Total
		(% of total incentive weighted to each component)			
Chief Investment Officer/Chief Managing Director	60	20 ¹		20	100
Managing Director – Portfolio Solutions Group	60	20 ¹		20	100
Managing Director – Private Market Assets and DC Plans	40	40 ²		20	100
Managing Director – Public Market Assets	40	40 ³		20	100
Program Director	30	50 ⁴	50	20	100
Director – Strategy, Research, Risk and/or Investment Decision Support	30	50 ¹		20	100
Senior Portfolio Manager	20		60	20	100
Portfolio Manager	20		60	20	100
Senior Investment Officer	20	60 ⁴	60	20	100
Investment Officer	20	60 ⁴	60	20	100
Senior Investment Analyst	20	30 ⁴	30	50	100
Investment Analyst	20	30 ⁴	30	50	100

¹Average multiplier based on the multipliers of all asset classes under the incumbent's purview.

²The MD Private Market Assets and DC Plans average multiplier is based on the multipliers of private market asset classes under the incumbent's purview.

³The MD Public Market Assets average multiplier is based on the multipliers of the public market asset classes under the incumbent's purview.

⁴These positions may support a specific asset class or multiple asset classes. If the position supports a specific asset class, then the multiplier is based on the asset class multiplier. If the position supports multiple asset classes, then the multiplier is based on the average of the multipliers of the asset classes supported.

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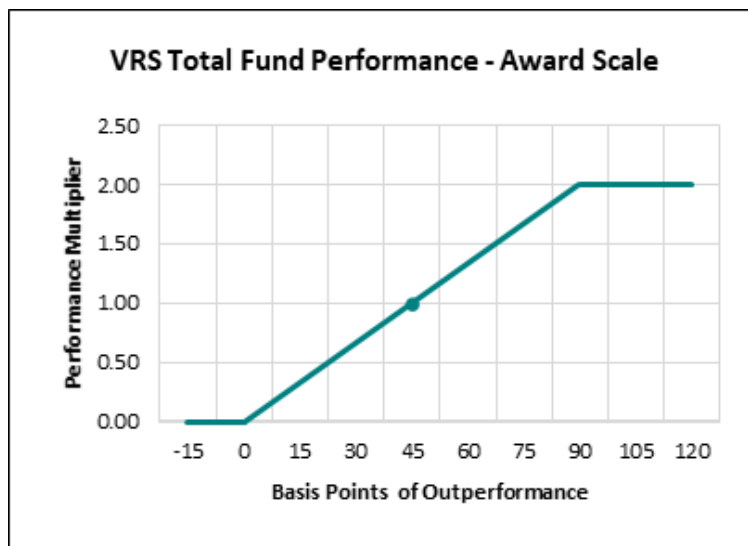
QUANTITATIVE PLAN COMPONENTS

These Plan components link participants' incentive compensation to relative investment performance or, more specifically, the extent by which the Total Fund and/or Asset Class performance exceeds passive benchmarks (indices) as measured over trailing three- and five-year annualized periods (each weighted 50%).

For purposes of this Plan:

- Measurement of relative investment performance is net of third-party fees, which consist of investment management fees and performance fees paid to investment managers, custodian fees, legal fees, internal investment staff administrative expenses, and miscellaneous fees.
- A performance-award scale defines the linkage between relative investment performance and a corresponding Performance Multiplier. Illustrating this approach at the Total Fund level, when VRS' relative investment performance:
 - Equals zero or less (i.e., no relative value added), then the VRS Performance Multiplier will equal zero and there will be no incentive payouts under this Plan component.
 - Equals 45 bps, then the VRS Performance Multiplier will equal 1.00 and there will be a 100% payout of this Plan component.
 - Equals 90 bps or more, then the VRS Performance Multiplier will equal 2.00 and there will be a 200% payout of this Plan component.
 - Is anywhere between zero and 90 bps, then the VRS Performance Multiplier is determined on an interpolated, straight-line basis.

Note: The Board approved the Verus recommended excess return objective (45 basis points) for the Total Fund at the June 15, 2020 meeting with an effective date of July 1, 2020. For implementation purposes, the Total Fund excess return objective will be a blend of the former excess return objective (30 basis points) to be used until June 30, 2020, and the new excess return objective (45 basis points) to be used from July 1, 2020 onward.



- Selected participants whose responsibilities span multiple asset classes may have a portion of their incentive weighted to a component that is determined based on the average multipliers of asset

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classes they support. The intent of this Plan component is to recognize and reward superior relative investment performance, regardless of the level of the associated assets.

The Board is responsible for setting the basis point outperformance standards for the Total Fund. The CIO is responsible for setting the basis point outperformance standards for individual asset classes, subject to the Board's final review and approval.

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QUALITATIVE PLAN COMPONENT

The qualitative incentive multiplier can range from 0.00 to 2.00 at the CIO’s discretion. The CIO obtains input from applicable senior staff regarding individual performance levels to help determine the qualitative rating. The qualitative rating is separate and distinct from the individual’s annual performance evaluation rating requirement for plan eligibility. This Plan component links participants’ incentive compensation to achievement of individual and/or position-specific performance objectives and VRS’ overall performance objectives. Actual awards under this plan component will reflect:

- Position and/or incumbent-specific performance criteria.
- Achievement of key VRS performance objectives, including:
 - Building an effective organization
 - Enhancing investment excellence
 - Developing staff

The Board will annually determine the CIO’s qualitative incentive multiplier after assessing attainment of the qualitative performance objectives, considering input and recommendations provided by the A&P Committee.

DETERMINING PRELIMINARY AWARDS

After the end of each fiscal year, a preliminary award will be determined for each Plan participant by aggregating all of their performance multiplier-adjusted weighted Plan components. In particular:

- Performance multipliers will be determined for each Plan component based on actual results.
- Preliminary payouts under each weighted Plan component will be determined by multiplying the incentive dollars weighted to that component by the associated performance multiplier.
- Total preliminary awards would be determined by adding up all of that participant’s weighted Plan components.

Illustrated below is this approach for a position with an incentive of \$80,000.

Plan Component	Weighted Portion of Incentive		Performance Multiplier		
Total Fund	\$16,000	X	1.50	=	\$24,000
Asset Class	48,000	X	1.00	=	48,000
Qualitative	16,000	X	1.20	=	19,200

Preliminary Award **\$91,200**

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DETERMINING FINAL AWARDS

Final awards, if any, would be determined after each fiscal year-end by adjusting the sum of each participant's preliminary award, up or down, based on VRS' one-year absolute return for the most recently completed fiscal year. Specifically, there will be no adjustment for returns between 0% and the assumed rate of return, currently 6.75%. There will be a positive one-for-one adjustment for returns in excess of the assumed rate of return. There will be a negative one-for-one adjustment for returns less than 0%. Illustrated below is the process for determining final awards.

Scenario #1: The Total Fund's One-Year Absolute Return Is +5%

Plan Component	Weighted Portion of Incentive		Performance Multiplier		
Total Fund	\$16,000	X	1.50	=	\$24,000
Asset Class	48,000	X	1.00	=	48,000
Qualitative	16,000	X	1.20	=	19,200

Preliminary Award \$91,200
 X no adjustment 0%

Final Award \$91,200

Scenario #2: The Total Fund's One-Year Absolute Return Is 9.75%

Plan Component	Weighted Portion of Incentive		Performance Multiplier		Actual Award
Total Fund	\$16,000	X	1.50	=	\$24,000
Asset Class	48,000	X	1.00	=	48,000
Qualitative	16,000	X	1.20	=	19,200

Preliminary Award \$91,200

X 1+ Total Fund's One-Year Rate of Return
 Less Assumed Rate of Return 103%

Final Award \$93,936

Scenario #3: The Total Fund's One-Year Absolute Return Is -15%

Plan Component	Weighted Portion of Incentive		Performance Multiplier		Actual Award
Total Fund	\$16,000	X	1.50	=	\$24,000
Asset Class	48,000	X	1.00	=	48,000
Qualitative	16,000	X	1.20	=	19,200

Preliminary Award \$91,200

X 1+ Total Fund's One-Year Rate of Return 85%

Final Award \$77,520

PAYING OUT FINAL AWARDS

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Board Review

Prior to payout of any and/or all awards, the CIO will present a schedule of aggregate incentives to the Board of Trustees, through the A&P Committee, in advance. This report will include, in aggregate, the awards, the multipliers awarded for each component, the actual dollar awards earned for each component and the total awards. Internal Audit and Human Resources will review the calculations. As requested by the A&P Committee, the CIO will provide additional information prior to the Board approving the payout of any and/or all awards.

Final Award Payout

Final awards will be paid out as follows:

- For VRS' most senior staff (i.e., incumbents in positions at or above the level of Program Director) when awards are paid, 50% of total award amounts up to the specified Internal Revenue Code (IRC) § 415(c)(1)(A) plan limits will be deferred into the DCPIP plan. All other amounts paid in cash. Section III of this document describes the terms of the § 415(c)(1)(A) plan.
- For all other Plan participants, awards paid 100% in cash.

Timing of Cash Payouts

When the Board approves incentive awards, the VRS will make payments between July 1 and December 31 after VRS' fiscal year end.

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INCENTIVE PLAN PROVISIONS

- ***New employees, promoted employees and other employees who transfer into another position covered in this pay plan:***
 - Employees who join the VRS Investment Department after the commencement of the fiscal year may be eligible to participate in the Plan. Incentives will be computed on the incentive percentage and their actual earned salary for the year.
 - Promoted employees and employees who transfer into another position covered in this pay plan will have their incentives calculated based on their actual earned salary for the year and a proportional incentive percentage for each position held during the fiscal year.
- ***Minimum Individual Performance Standard:*** Employees with an individual performance rating of "Does Not Meet Expectations" are not eligible to receive any incentive payment under the Plan.
- ***Termination of Employment Due to Death, Disability, or Retirement:*** Terminated employees may be eligible to receive a time-weighted portion of their final award for the current performance year. Plan participants who terminate employment due to death or disability or who retire during a fiscal year will be eligible to receive a time-weighted portion of their Board approved award (1/12 for each complete month worked in their last year of service). The incentive payments for the year in which death, disability or retirement occurs shall be paid 100% in cash to such employee or his representative between July 1 and December 31 following the end of the fiscal year in which such death, disability or retirement occurs.
- ***Termination for all Other Reasons:*** Except as specifically determined by the CIO for all positions other than the CIO, and by the A&P Committee for the CIO's position, participants who terminate employment with VRS for all other reasons prior to the normally scheduled date of payout forfeit all rights under the plan.
- ***Clawback:*** In the event of termination for malfeasance related to duties as an investment professional, VRS retains the right to seek repayment for any and/or all paid incentive awards.

III. Defined Contribution Incentive Plan for VRS Investment Management Personnel (DCPIP)

PARTICIPATION

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This plan covers VRS investment professionals at or above the level of Program Director. Such positions currently include CIO, Managing Director, and Program Director. The Board retains the discretion to modify, at any time, the positions that are eligible to participate in this plan.

AMOUNTS SUBJECT TO ANNUAL DEFERRAL

- Deferrals into this plan only occur in years when VRS' Board decides, at its full and complete discretion, to allow payment of incentive awards.
- Commencing with (and including fiscal 2013), in years when VRS' Board decides to pay incentive awards, 50% of participants' final awards up to specified IRC § 415(c)(1)(A) limits will be deferred into this plan. All other amounts paid in cash.

INVESTMENT RETURN

Participants' deferred accounts in the DCPIP and the § 415(m) plan will earn an "investment return" (positive or negative) equaling the current annual rate of return of the VRS Fund. However, upon attaining age 55, the DCPIP permits members of the Investment Management Committee who have established accounts in the Commonwealth of Virginia 457 Deferred Compensation Plan, to transfer a portion into the Virginia Cash Match Plan. This transfer right allows DCPIP participants at age 55 or at any time after attaining age 55, to select any combination of the investment options then offered by the Cash Match Plan. Notwithstanding the transfer right, members of the Investment Management Committee at age 55 or older must leave at least a minimal balance amount in their DCPIP account, to avoid having to re-open the account. The VRS Defined Contribution Plan Administrator will assist participants with these transfers.

FUND TRANSFERS AND DISTRIBUTIONS

Participants of the DCPIP cannot transfer funds from the § 415(m) plan into the Cash Match Plan because the § 415(m) plan is a non-qualified "excess plan" not permitted to be held in trust for the exclusive benefit of the plan participants. The § 415(m) plan closed as of June 30, 2013, except for the CIO. The distribution of the balance in the § 415(m) plan will be made in cash to the Participant.

The accumulated DCPIP trust balances will be distributed to the Participant upon termination of employment with the Commonwealth of Virginia. The participant may elect to receive the balance in the DCPIP either in cash or as a "roll-over" into another retirement or related benefit vehicle/trust, or a combination of both. All payouts/rollovers will be credited with earnings through the latest quarter end for which finalized performance is available, by the date of the payment.

All applicable laws and regulations will govern the creation, funding and distributions of the DCPIP and § 415(m) plan. Detailed plan documents are on file with the Human Resources Director and the Chief Financial Officer.

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TAXATION

Taxation of the amount contributed to the DCPIP and § 415(m) plans is deferred until distribution from the respective plan.

IV. Other Compensation Plan Information

Competitive Pay Increases

Competitive pay increases are an option available to retain a highly valued employee who has received a job offer from another employer. Requests for competitive pay increases should take into consideration the employee's experience, level of education, performance and contribution to the agency, and the salaries of other employees in comparable jobs. A written job offer must be received to provide a competitive pay increase.

Sign-on Bonuses

Investment professionals hired at the VRS may be eligible for sign-on bonuses, as described in the VRS Employee Sign-on Bonus Program Policy.

Relocation Expenses

Investment professionals hired at the VRS may be eligible for reimbursement of relocation expenses, if approved by the CIO. The reimbursement of the expenses must comply with the Department of Accounts Moving and Relocation Policy.

Employment at Will

The investment employees covered by this policy are exempt from the provisions of the Virginia Personnel Act and employment in these positions is at will. Just as the employee retains the right to resign at any time, the VRS has a similar right to end at will employment with or without cause. An at-will employee does not serve an introductory period. An at-will employee is not eligible to use the agency's grievance procedure to resolve employment disputes.

Investment employees covered by this policy are eligible for all other employment benefits and subject to agency policies that do not contradict their "at will" status.

409A Compliance

The intent of the Board is that payments and benefits under this plan either comply with Section 409A of the Internal Revenue Code and applicable guidance issued thereunder ("Code Section 409A") or qualify for an exemption from Code Section 409A and, accordingly, all provisions of this Plan shall be construed in a manner consistent with the requirements for avoiding taxes or penalties under Code Section 409A. The Board shall not take any action to accelerate or delay the payment of any monies and/or provision of any benefits in any matter which would not be in compliance with Code Section 409A to the extent Code Section 409A applies to such payment or benefit. Notwithstanding any of the provisions of this pay plan, the Board shall not be liable to the employee if any payment or benefit which is to be provided pursuant to this Plan and which is considered deferred compensation subject to Code Section 409A otherwise fails to comply with, or be exempt from, the requirements of Code Section 409A.

Investment Professionals' Pay Plan Effective October 18, 2022

CLASS STRUCTURE

The following descriptions are the summaries of VRS' investment professional job classes/positions:

Chief Investment Officer

The CIO manages and directs investment programs, determines appropriate program structure, implementation, and monitoring. The CIO manages investment professionals who are directly responsible for internal and external investment programs. The CIO heads the Executive and Management Committees, which are responsible for reviewing all investment recommendations. The CIO collaborates with the VRS Board-appointed Investment Advisory Committee (IAC) and delivers frequent reports and updates to the VRS Board.

Managing Director

The Managing Director is a senior investment position reporting directly to the CIO. This position serves on the Investment Executive and Management Committees. The Executive Committee is a department wide resource to the CIO for management and administrative issues. The Management Committee participates in asset allocation and manager/fund allocation decisions.

Program Director

The Program Director has deep asset class knowledge and carries full managerial responsibility for a VRS investment program, including all internally and externally managed assets. The Program Director may also support multiple asset classes. The Program Director participates on the Investment Management Committee and regularly presents information to the IAC and the Board. The Program Director, as applicable, operates within an explicit risk budget and has investment performance objectives that are regularly measured. The Program Director has full responsibility for negotiating on behalf of VRS.

Director - Strategy, Research, Risk and/or Investment Decision Support

Strategy – The position within Strategy identifies and evaluates relative value-based tilt opportunities that have the potential to 1) improve the fund's return without materially increasing the risk, 2) reduce the fund's risk without materially reducing the return, or 3) some combination of these objectives. In addition, staff within Strategy 1) review and evaluate the implications of macro-economic conditions, 2) analyze current conditions and opportunities within major asset classes and key asset class subsectors, 3) monitor and evaluate the tactical and strategic tilts of key VRS investment partners, and 4) identify strategy ideas including risk and return expectations for base case and alternative scenarios.

Research – The position within Research has responsibility to support both basic and applied research efforts for all VRS investment staff. This effort includes monitoring, coordinating, facilitating, and implementing current best practices and methods to ensure optimal investment performance and risk management at both the program and plan level.

Risk – The position within Risk has responsibility in the design, implementation, and management of the risk management program including project management (solicitation and queueing of projects from clients), guidance and coordination within the group, mathematical and statistical analysis of empirical problems, risk management, and high-level programming. Additionally, staff within Risk assist with the design and implementation of a diverse collection of strategies designed to have low or negative correlation to other VRS asset classes.

Investment Decision Support – The position within Investment Decision Support has responsibility for the design and delivery of investment program, risk management, strategy, and research analytic systems. As a component of this, staff is responsible for all investments data as well as the design, development and implementation of the quantitative infrastructure for the VRS investment programs. This includes a data

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warehouse, various data retrieval tools, quantitative analysis tools, program level reporting tools and support applications that retrieve, consolidate and report information.

Senior Portfolio Manager

The Senior Portfolio Manager positions have responsibility for multiple portfolio strategies and/or may supervise one or more Senior Investment Officers or Portfolio Managers. The Senior Portfolio Manager positions provide a potential career progression ladder for Portfolio Managers over time, considering the contributions, experience and sustained performance for the incumbents.

Portfolio Manager

The Portfolio Manager provides critical input to strategy development and is responsible for the more complicated and higher risk investments. The Portfolio Manager may delegate to the Senior Investment Officer certain portions of the investment program. The Portfolio Manager will begin to negotiate terms on behalf of VRS. The Portfolio Manager, from time to time, makes presentations and recommendations to the Management Committee, and perhaps the IAC and Board.

The Portfolio Manager supporting the Defined Contribution Plans is a senior investment position reporting directly to the Managing Director - Private Market Assets and DC Plans. This position provides critical input to the design, implementation, and monitoring of all investment related aspects of the VRS defined contribution plans (DC). Responsibilities include (1) evaluation and selection of new investment strategies, managers and/or funds, (2) negotiating terms on behalf of VRS, (3) monitoring and management of relationships with existing defined contribution investment managers, (4) implementing investment policy as determined by the VRS Board, (5) presenting to the Defined Contribution Plans Advisory Committee and the Board, and (6) any other projects or duties relating to the defined contribution program as may be assigned from time to time.

Senior Investment Officer

The Senior Investment Officer has higher level monitoring responsibilities that tend to involve higher risk and strategies that are more complicated. Some Senior Investment Officers may have day-to-day responsibilities for managing internal portfolios, subject to risk limits prescribed by the program director. The Senior Investment Officer will increasingly become involved in strategy development and formal recommendations to the Program Director.

Investment Officer

The Investment Officer, in addition to analytical responsibilities, may have direct responsibility for monitoring some portion of the existing portfolio, or some strategies or managers under consideration in the future. Such assignments will typically be in lower risk and less complicated strategies. The Investment Officer may continue to be involved in monitoring, compliance, and administration, but will also begin to make formal investment recommendations to the Program Director.

Senior Investment Analyst

The Senior Investment Analyst performs various types of analysis at the direction of more senior staff members. Analyst activities are geared around providing support for senior staff members more directly involved in the decision-making process. Such activities will include research, reporting, monitoring, compliance, and administration.

Investment Analyst

The Investment Analyst assists other investment professionals in their daily operations, including investment research and analysis, trading, and portfolio management. Analysts follow and report current market information relating to assigned sectors of the market. In addition, the Analyst conducts independent research on various topics, performs data maintenance, integrity, and report generation tasks.



**VIRGINIA RETIREMENT SYSTEM
INVESTMENT PROFESSIONALS'
PAY PLAN
Effective ~~July 10~~October 18, 2022**

Investment Professionals' Pay Plan

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OVERVIEW & PAY PHILOSOPHY

The Virginia Retirement System's (VRS) Board of Trustees has designed this investment professionals' pay plan after working with an independent compensation consultant. In addition, the Board has adopted benchmarks, recommended by an independent investment consultant, to be used as part of this pay plan.

This pay plan includes three core elements:

- Base Salary (described in Section I of this document)
- Incentive Pay Plan (described in Section II)
- Deferred Compensation Plan for VRS Investment Management Personnel (DCPIP) (described in Section III)

Overall, this pay plan is designed to:

- Attract, motivate and retain skilled investment professionals by offering competitive compensation opportunities.
- Directly align compensation with long-term, superior relative and absolute investment performance.
- Reinforce risk management priorities and standards.
- Attract and retain senior investment professionals by deferring a portion of incentive compensation on a tax-deferred basis.
- Benefit all stakeholders – VRS' beneficiaries, VRS' employees, and Virginia's taxpayers – through a compensation plan that is clear, aligned with performance, competitive and cost effective.

Importantly, this pay plan anchors on two broad and long-standing philosophical principles:

1. VRS should pay base salaries consistent with the 75th percentile of a peer group of other leading public funds. The primary guidelines for determining VRS' leading public fund peer group will be (1) funds of similar size (AUM) as VRS and (2) funds with significant (>25%) assets managed internally. Additional criteria the Board may consider is asset allocation / diverse portfolio similar to VRS, degree of delegation to the CIO and staff, use of outside investment consultants, and Board pay decision making authority.
2. VRS should provide incentive compensation opportunities such that, in combination with base salary, total compensation levels approximate the median (50th percentile) of a blended group weighted 75% to the total compensation levels of leading peer group public funds and 25% to the total compensation levels of a broad range of private-sector firms that employ investment professionals.

I. Base Salary

SALARY RANGES

This pay plan establishes a salary range for each job class taking into account its relative importance to VRS and the salaries paid for comparable types of jobs in other leading public funds.

Minimum, midpoint, and maximum salary rates define the salary range for each job class/position. The midpoint of each job class/position approximates the 75th percentile of salaries of a peer group of leading public pension funds. Actual salaries can be higher or lower than the midpoint depending on factors such as job performance, professional education and certifications, the willingness to assume new and higher-level duties and responsibilities, the ability to learn quickly and apply new knowledge and skills, being a team player, and the length of time in the position.

Each position's salary range includes a defined:

- **Minimum** - the lowest base salary paid for a job within the job class/position.

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- **Midpoint** - represents the market salary paid to a fully qualified employee, who has the institutional knowledge and practical experience to fulfill independently all of the responsibilities of the job/position.
- **Maximum** - the highest salary rate for the job class/position.

Grade	Position	Salary Range (\$ Thousands)		
		Min (\$)	Mid (\$)	Max (\$)
10	Chief Investment Officer/Chief Managing Director	325	430	540
9	Managing Director	275	365	455
8	Program Director	235	315	395
7	Director – Strategy, Research, Risk and/or Investment Decision Support	205	275	345
6	Senior Portfolio Manager	205	275	345
5	Portfolio Manager	160	215	270
4	Senior Investment Officer	135	180	225
3	Investment Officer	105	140	175
2	Senior Investment Analyst	80	105	130
1	Investment Analyst	65	85	105

In considering the above salary range, it important to note the following:

- **Market Pay Reviews:** The VRS normally conducts a comparative market total pay study generally every two to three years to ensure competitiveness of the salary and incentive structures. Typically, the VRS conducts the study in the 1st quarter of the calendar year with an effective date of July 1 (the beginning of the fiscal year).
- **Changes in Salary Ranges:** The Board must approve changes to the salary scale and incentive structure.

Salary Adjustments

Oversight & Administration

VRS will implement pay actions consistent with the provisions of the Appropriation Act. The VRS Board, however, approves across-the-board performance-based salary increases, market-based salary increases and incentive pools, for VRS investment professionals, consistent with the Code of Virginia and the Appropriation Act. The Chief Investment Officer (CIO) approves salary adjustments for individual investment professionals and, as described later in this document, sign-on bonuses, incentive payments, and relocation expenses subject to the limitations in the Code of Virginia and other applicable state or federal law and regulation.

Merit Increases

- Salary increases are based on meeting individual performance standards. The supervisor completes the evaluation after the end of the fiscal year. If a participant in the investment employees' pay plan does not meet overall performance standards, then the participant is ineligible for performance increases to their base salary and market adjustments to their base salary for that performance cycle. Performance cycles are on a fiscal year basis (July 1 through June 30) and typically begin with an effective date of performance plans in the first quarter of the new fiscal year.

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- The CIO will receive base salary increases as approved by the VRS Board of Trustees and in accordance with the terms in the CIO's Employment Agreement, with approved effective dates established by the VRS Board of Trustees.

Starting Salaries

The starting salary for a new employee considers the rates presently paid to other employees in the department and those in the same job class (when applicable), the candidate's education, skills, work experience, and salary history. The starting salary normally does not exceed the salary grade midpoint.

Reallocation

Occurs when a job classification is reviewed by Human Resources and it is determined that the job duties and responsibilities have changed significantly enough to place the job in a different job title and job class. Unless the CIO authorizes an exception, this would not exceed a 15% increase. However, the individual's salary will always be at least at the minimum of the range of the new job, regardless of the amount of the increase.

In-grade Adjustments

Occur to ensure competitiveness, retention, and to recognize increased skills, abilities, knowledge, obtainment of a degree or certification, or significant increases in responsibilities within the job class. Unless the CIO authorizes an exception, adjustments will not exceed a 10% increase.

Promotions

Promotions occur when an individual moves into a position in a higher job class. Promotions can be competitive (selected through a recruitment and hiring process) or non-competitive (through a job reclassification or reallocation). Unless the CIO approves an exception, promotions will not exceed a 15% increase. However, the individual's salary will always be at least at the minimum of the range of the new job, regardless of the amount of the increase.

Downward Assignment

Downward adjustment occurs when an employee changes positions whether voluntarily, or because of unsatisfactory performance, resulting in a downward change in job class. A reduction in salary may occur based on a review of the salary and range and the circumstances associated with the downward move. In downward assignments, an individual's salary cannot exceed the maximum of the new salary range.

II. Incentive Pay Plan

PLAN ADMINISTRATION

The VRS Board of Trustees, the Plan Administrator, through the Administration and Personnel (A&P) Committee, administers the Incentive Plan (Plan) and retains full and complete discretion:

- To increase or decrease incentives for any and/or all Plan participants.
- To modify, amend or rescind any aspect of the Plan at any time for any and/or all Plan participants.
- While the Plan Administrator remains mindful of the value that staff adds to the organization and supportive of the pay plan, the Plan Administrator also specifically reserves the right to cancel, reduce, or delay the amount of any incentives payable under this plan when, in the sole discretion of the Plan Administrator, extreme budgetary pressures, economic, market or other conditions are such that the Plan Administrator deems such action necessary under the circumstances.

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- Consistent with the preceding paragraph, payment of incentives under this plan is not guaranteed.

The Plan Administrator may delegate certain aspects of this Plan's day-to-day operation to the VRS CIO and the VRS Director of Human Resources. However, any substantive Plan-related questions or issues impacting incentive payouts for the CIO require the Plan Administrator's prior approval.

PLAN ELIGIBILITY

Incumbents in the positions listed below are eligible to participate in this incentive plan, provided they:

- Are active VRS employees.
- Work for VRS at least forty hours per week. Plan participants who work less than full-time may be eligible to receive a prorated incentive payment. Wage employees are not eligible to participate in the plan.
- Receive an individual performance evaluation of at least "meets expectations" for the relevant performance year (i.e., the year preceding the normally scheduled year of payment).
- Remain in compliance with the VRS Investment Department Code of Ethics and Standards of Professional Conduct Policy.

Positions Eligible to Participate in the Investment Professional's Pay Plan
Chief Investment Officer/Chief Managing Director
Managing Director – Portfolio Solutions Group
Managing Director – Private Market Assets and DC Plans
Managing Director – Public Market Assets
Program Director
Director – Strategy, Research, Risk and/or Investment Decision Support
Senior Portfolio Manager
Portfolio Manager
Senior Investment Officer
Investment Officer
Senior Investment Analyst
Investment Analyst

The CIO will determine the design of the incentive plan structure for the positions supporting the Defined Contribution Plans, with both quantitative and qualitative elements.

Generally, employees on an approved leave of absence are considered active employees. The CIO will resolve all questions regarding eligibility, or in the case of the CIO, eligibility will be determined by the Board.

Participation in this Plan in any one year does not confer the right to participate in this Plan in any other year or to receive Plan payouts for the current and/or any future year. Participation in this Plan does not confer the right to continued employment. Subject to the provisions of this Plan, only active VRS employees may receive payments under this Plan.

OVERALL INCENTIVE PLAN MECHANICS

As described in more detail throughout this document, under the terms of this Plan:

- Eligible Plan participants will be assigned an incentive opportunity, expressed as a percentage of their actual earned base salary.
- Incentive opportunities vary by position, with the level of such opportunities increasing with the degree to which the position directly affects VRS' investment performance.
- Incentives are weighted or allocated to separate Plan components, described below, with the specific components and weightings varying by position:
 1. Total Fund relative investment performance
 2. Asset Class relative investment performance
 3. Average of Asset Class Multipliers (for positions that support multiple asset classes)
 4. Qualitative – focuses on individual achievement of assigned objectives.
- After year-end, payouts under each Plan component would be determined based on performance.
- Each participant's preliminary award would equal the sum of all of their performance adjusted Plan components.
- Final awards would equal preliminary awards adjusted, up or down, based on the Total Fund's one-year absolute return. Specifically, there will be no adjustment for returns between 0% and the assumed rate of return, currently 6.75%. There will be a positive one-for-one adjustment for returns in excess of the assumed rate of return (e.g., if Total Fund one-year actual absolute return equals +9.75%, then the preliminary awards will be increased by 3%). There will be a negative one-for-one adjustment for a return less than 0% (e.g., if Total Fund one-year actual absolute return equals -15%, then the preliminary awards will be reduced by 15%). This adjustment is specifically intended to systematically take into account, in the shorter term, the effect of market cycles on the health of the pension plan by providing a mechanism to reflect the impact of up and down markets on incentive compensation.
 - 50% of eligible senior staff-members' awards (up to IRS limits) will be deferred into tax-qualified accounts. See section III, Defined Contribution Incentive Plan for VRS Investment Management Personnel (DCPIP). While deferred, awards are subject to the Total Fund's annual absolute return.
 - All other awards paid in cash.

Generally, a Participant must be employed on the date of payment of the award. However, see INCENTIVE PLAN PROVISIONS, *Termination of Employment Due to Death, Disability or Retirement*.

INCENTIVE OPPORTUNITIES

Incentive opportunities will vary by position based on multiple criteria:

- The position's potential effect on the VRS' investment performance.
- Competitive market pay requirements.
- Internal equity considerations.
- Other factors determined by the CIO or, in the case of the Chief Investment Officer's position, by VRS' Board.

Actual awards can vary based on performance.

For the fiscal year ending June 30, ~~2022~~ **2023**, and all subsequent years, unless as otherwise determined, the Plan's incentive opportunities are as follows:

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Incentive Levels	
VRS Position	Incentive ¹ (% Salary)
Chief Investment Officer	70 ²
Chief Managing Director	70 ²
Managing Director – Portfolio Solutions Group	65 ²
Managing Director – Private Market Assets and DC Plans	65 ²
Managing Director – Public Market Assets	65 ²
Program Director	60 ²
Director – Strategy, Research, Risk and/or Investment Decision Support	50
Senior Portfolio Manager	50
Portfolio Manager	40
Senior Investment Officer	30
Investment Officer	30
Senior Investment Analyst	25 <u>20</u>
Investment Analyst	5 <u>10</u>

¹Performance-adjusted preliminary awards can vary from zero to two times the incentive.

²A portion, up to 50%, of the positions' earned incentives is subject to mandatory deferral.

INCENTIVE WEIGHTINGS

Each participant's incentive award will be weighted or allocated to separate, stand-alone Plan components. Importantly, all participants have a portion of their incentive opportunities weighted:

- To the Total Fund Plan component – which helps reinforce the importance of collective success as measured by the Total Fund's relative investment results.
- To the Qualitative Plan component – this helps reinforce achievement of specific initiatives and professional development.

Described below are the specific Plan weightings and the approach for determining awards under each of these Plan components.

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Incentive Weightings by Plan Component					
VRS Position	Total Fund %	Asset Class Multipliers %	Asset Class %	Qualitative %	Total
		(% of total incentive weighted to each component)			
Chief Investment Officer/Chief Managing Director	60	20 ¹		20	100
Managing Director – Portfolio Solutions Group	60	20 ¹		20	100
Managing Director – Private Market Assets and DC Plans	40	40 ²		20	100
Managing Director – Public Market Assets	40	40 ³		20	100
Program Director	30	50 ⁴	50	20	100
Director – Strategy, Research, Risk and/or Investment Decision Support	30	50 ¹		20	100
Senior Portfolio Manager	20		60	20	100
Portfolio Manager	20		60	20	100
Senior Investment Officer	20	60 ⁴	60	20	100
Investment Officer	20	60 ⁴	60	20	100
Senior Investment Analyst	20	30 ⁴	30	50	100
Investment Analyst	20	30 ⁴	30	50	100

¹Average multiplier based on the multipliers of all asset classes under the incumbent's purview.

²The MD Private Market Assets and DC Plans average multiplier is based on the multipliers of private market asset classes under the incumbent's purview.

³The MD Public Market Assets average multiplier is based on the multipliers of the public market asset classes under the incumbent's purview.

⁴These positions may support a specific asset class or multiple asset classes. If the position supports a specific asset class, then the multiplier is based on the asset class multiplier. If the position supports multiple asset classes, then the multiplier is based on the average of the multipliers of the asset classes supported.

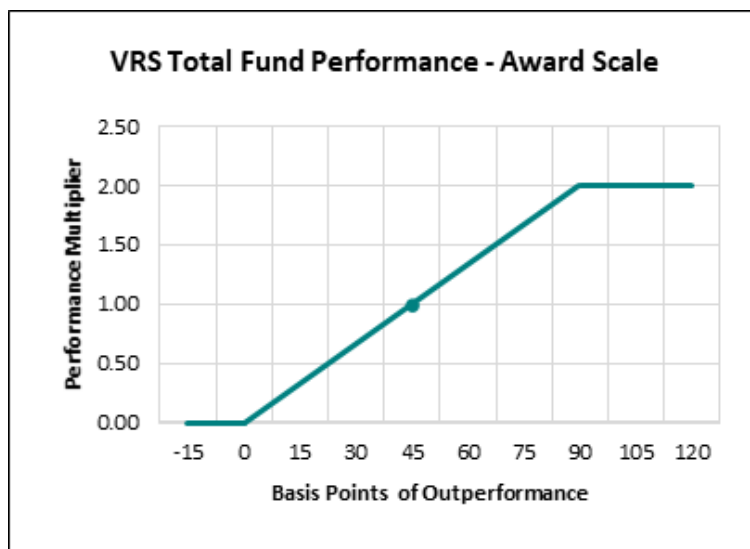
QUANTITATIVE PLAN COMPONENTS

These Plan components link participants' incentive compensation to relative investment performance or, more specifically, the extent by which the Total Fund and/or Asset Class performance exceeds passive benchmarks (indices) as measured over trailing three- and five-year annualized periods (each weighted 50%).

For purposes of this Plan:

- Measurement of relative investment performance is net of third-party fees, which consist of investment management fees and performance fees paid to investment managers, custodian fees, legal fees, internal investment staff administrative expenses, and miscellaneous fees.
- A performance-award scale defines the linkage between relative investment performance and a corresponding Performance Multiplier. Illustrating this approach at the Total Fund level, when VRS' relative investment performance:
 - Equals zero or less (i.e., no relative value added), then the VRS Performance Multiplier will equal zero and there will be no incentive payouts under this Plan component.
 - Equals 45 bps, then the VRS Performance Multiplier will equal 1.00 and there will be a 100% payout of this Plan component.
 - Equals 90 bps or more, then the VRS Performance Multiplier will equal 2.00 and there will be a 200% payout of this Plan component.
 - Is anywhere between zero and 90 bps, then the VRS Performance Multiplier is determined on an interpolated, straight-line basis.

Note: The Board approved the Verus recommended excess return objective (45 basis points) for the Total Fund at the June 15, 2020 meeting with an effective date of July 1, 2020. For implementation purposes, the Total Fund excess return objective will be a blend of the former excess return objective (30 basis points) to be used until June 30, 2020, and the new excess return objective (45 basis points) to be used from July 1, 2020 onward.



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- Selected participants whose responsibilities span multiple asset classes may have a portion of their incentive weighted to a component that is determined based on the average multipliers of asset classes they support. The intent of this Plan component is to recognize and reward superior relative investment performance, regardless of the level of the associated assets.

The Board is responsible for setting the basis point outperformance standards for the Total Fund. The CIO is responsible for setting the basis point outperformance standards for individual asset classes, subject to the Board's final review and approval.

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QUALITATIVE PLAN COMPONENT

The qualitative incentive multiplier can range from 0.00 to 2.00 at the CIO's discretion. The CIO obtains input from applicable senior staff regarding individual performance levels to help determine the qualitative rating. The qualitative rating is separate and distinct from the individual's annual performance evaluation rating requirement for plan eligibility. This Plan component links participants' incentive compensation to achievement of individual and/or position-specific performance objectives and VRS' overall performance objectives. Actual awards under this plan component will reflect:

- Position and/or incumbent-specific performance criteria.
- Achievement of key VRS performance objectives, including:
 - Building an effective organization
 - Enhancing investment excellence
 - Developing staff

The Board will annually determine the CIO's qualitative incentive multiplier after assessing attainment of the qualitative performance objectives, considering input and recommendations provided by the A&P Committee.

DETERMINING PRELIMINARY AWARDS

After the end of each fiscal year, a preliminary award will be determined for each Plan participant by aggregating all of their performance multiplier-adjusted weighted Plan components. In particular:

- Performance multipliers will be determined for each Plan component based on actual results.
- Preliminary payouts under each weighted Plan component will be determined by multiplying the incentive dollars weighted to that component by the associated performance multiplier.
- Total preliminary awards would be determined by adding up all of that participant's weighted Plan components.

Illustrated below is this approach for a position with an incentive of \$80,000.

Plan Component	Weighted Portion of Incentive		Performance Multiplier		
Total Fund	\$16,000	X	1.50	=	\$24,000
Asset Class	48,000	X	1.00	=	48,000
Qualitative	16,000	X	1.20	=	19,200

Preliminary Award **\$91,200**

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DETERMINING FINAL AWARDS

Final awards, if any, would be determined after each fiscal year-end by adjusting the sum of each participant's preliminary award, up or down, based on VRS' one-year absolute return for the most recently completed fiscal year. Specifically, there will be no adjustment for returns between 0% and the assumed rate of return, currently 6.75%. There will be a positive one-for-one adjustment for returns in excess of the assumed rate of return. There will be a negative one-for-one adjustment for returns less than 0%. Illustrated below is the process for determining final awards.

Scenario #1: The Total Fund's One-Year Absolute Return Is +5%

Plan Component	Weighted Portion of Incentive		Performance Multiplier		
Total Fund	\$16,000	X	1.50	=	\$24,000
Asset Class	48,000	X	1.00	=	48,000
Qualitative	16,000	X	1.20	=	19,200

Preliminary Award **\$91,200**
 X no adjustment _____ **0%**

Final Award **\$91,200**

Scenario #2: The Total Fund's One-Year Absolute Return Is 9.75%

Plan Component	Weighted Portion of Incentive		Performance Multiplier		Actual Award
Total Fund	\$16,000	X	1.50	=	\$24,000
Asset Class	48,000	X	1.00	=	48,000
Qualitative	16,000	X	1.20	=	19,200

Preliminary Award **\$91,200**

X 1+ Total Fund's One-Year Rate of Return
 Less Assumed Rate of Return _____ **103%**

Final Award **\$93,936**

Scenario #3: The Total Fund's One-Year Absolute Return Is -15%

Plan Component	Weighted Portion of Incentive		Performance Multiplier		Actual Award
Total Fund	\$16,000	X	1.50	=	\$24,000
Asset Class	48,000	X	1.00	=	48,000
Qualitative	16,000	X	1.20	=	19,200

Preliminary Award **\$91,200**

X 1+ Total Fund's One-Year Rate of Return _____ **85%**

Final Award **\$77,520**

PAYING OUT FINAL AWARDS

Board Review

Prior to payout of any and/or all awards, the CIO will present a schedule of aggregate incentives to the Board of Trustees, through the A&P Committee, in advance. This report will include, in aggregate, the awards, the multipliers awarded for each component, the actual dollar awards earned for each component and the total awards. Internal Audit and Human Resources will review the calculations. As requested by the A&P Committee, the CIO will provide additional information prior to the Board approving the payout of any and/or all awards.

Final Award Payout

Final awards will be paid out as follows:

- For VRS' most senior staff (i.e., incumbents in positions at or above the level of Program Director) when awards are paid, 50% of total award amounts up to the specified Internal Revenue Code (IRC) § 415(c)(1)(A) plan limits will be deferred into the DCPIP plan. All other amounts paid in cash. Section III of this document describes the terms of the § 415(c)(1)(A) plan.
- For all other Plan participants, awards paid 100% in cash.

Timing of Cash Payouts

When the Board approves incentive awards, the VRS will make payments between July 1 and December 31 after VRS' fiscal year end.

-

INCENTIVE PLAN PROVISIONS

- ***New employees, promoted employees and other employees who transfer into another position covered in this pay plan:***
 - Employees who join the VRS Investment Department after the commencement of the fiscal year may be eligible to participate in the Plan. Incentives will be computed on the incentive percentage and their actual earned salary for the year.
 - Promoted employees and employees who transfer into another position covered in this pay plan will have their incentives calculated based on their actual earned salary for the year and a proportional incentive percentage for each position held during the fiscal year.
- ***Minimum Individual Performance Standard:*** Employees with an individual performance rating of "Does Not Meet Expectations" are not eligible to receive any incentive payment under the Plan.
- ***Termination of Employment Due to Death, Disability, or Retirement:*** Terminated employees may be eligible to receive a time-weighted portion of their final award for the current performance year. Plan participants who terminate employment due to death or disability or who retire during a fiscal year will be eligible to receive a time-weighted portion of their Board approved award (1/12 for each complete month worked in their last year of service). The incentive payments for the year in which death, disability or retirement occurs shall be paid 100% in cash to such employee or his representative between July 1 and December 31 following the end of the fiscal year in which such death, disability or retirement occurs.
- ***Termination for all Other Reasons:*** Except as specifically determined by the CIO for all positions other than the CIO, and by the A&P Committee for the CIO's position, participants who terminate employment with VRS for all other reasons prior to the normally scheduled date of payout forfeit all rights under the plan.
- ***Clawback:*** In the event of termination for malfeasance related to duties as an investment professional, VRS retains the right to seek repayment for any and/or all paid incentive awards.

III. Defined Contribution Incentive Plan for VRS Investment Management Personnel (DCPIP)

PARTICIPATION

This plan covers VRS investment professionals at or above the level of Program Director. Such positions currently include CIO, Managing Director, and Program Director. The Board retains the discretion to modify, at any time, the positions that are eligible to participate in this plan.

AMOUNTS SUBJECT TO ANNUAL DEFERRAL

- Deferrals into this plan only occur in years when VRS' Board decides, at its full and complete discretion, to allow payment of incentive awards.
- Commencing with (and including fiscal 2013), in years when VRS' Board decides to pay incentive awards, 50% of participants' final awards up to specified IRC § 415(c)(1)(A) limits will be deferred into this plan. All other amounts paid in cash.

INVESTMENT RETURN

Participants' deferred accounts in the DCPIP and the § 415(m) plan will earn an "investment return" (positive or negative) equaling the current annual rate of return of the VRS Fund. However, upon attaining age 55, the DCPIP permits members of the Investment Management Committee who have established accounts in the Commonwealth of Virginia 457 Deferred Compensation Plan, to transfer a portion into the Virginia Cash Match Plan. This transfer right allows DCPIP participants at age 55 or at any time after attaining age 55, to select any combination of the investment options then offered by the Cash Match Plan. Notwithstanding the transfer right, members of the Investment Management Committee at age 55 or older must leave at least a minimal balance amount in their DCPIP account, to avoid having to re-open the account. The VRS Defined Contribution Plan Administrator will assist participants with these transfers.

FUND TRANSFERS AND DISTRIBUTIONS

Participants of the DCPIP cannot transfer funds from the § 415(m) plan into the Cash Match Plan because the § 415(m) plan is a non-qualified "excess plan" not permitted to be held in trust for the exclusive benefit of the plan participants. The § 415(m) plan closed as of June 30, 2013, except for the CIO. The distribution of the balance in the § 415(m) plan will be made in cash to the Participant.

The accumulated DCPIP trust balances will be distributed to the Participant upon termination of employment with the Commonwealth of Virginia. The participant may elect to receive the balance in the DCPIP either in cash or as a "roll-over" into another retirement or related benefit vehicle/trust, or a combination of both. All payouts/rollovers will be credited with earnings through the latest quarter end for which finalized performance is available, by the date of the payment.

All applicable laws and regulations will govern the creation, funding and distributions of the DCPIP and § 415(m) plan. Detailed plan documents are on file with the Human Resources Director and the Chief Financial Officer.

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TAXATION

Taxation of the amount contributed to the DCPIP and § 415(m) plans is deferred until distribution from the respective plan.

IV. Other Compensation Plan Information

Competitive Pay Increases

Competitive pay increases are an option available to retain a highly valued employee who has received a job offer from another employer. Requests for competitive pay increases should take into consideration the employee's experience, level of education, performance and contribution to the agency, and the salaries of other employees in comparable jobs. A written job offer must be received to provide a competitive pay increase.

Sign-on Bonuses

Investment professionals hired at the VRS may be eligible for sign-on bonuses, as described in the VRS Employee Sign-on Bonus Program Policy.

Relocation Expenses

Investment professionals hired at the VRS may be eligible for reimbursement of relocation expenses, if approved by the CIO. The reimbursement of the expenses must comply with the Department of Accounts Moving and Relocation Policy.

Employment at Will

The investment employees covered by this policy are exempt from the provisions of the Virginia Personnel Act and employment in these positions is at will. Just as the employee retains the right to resign at any time, the VRS has a similar right to end at will employment with or without cause. An at-will employee does not serve an introductory period. An at-will employee is not eligible to use the agency's grievance procedure to resolve employment disputes.

Investment employees covered by this policy are eligible for all other employment benefits and subject to agency policies that do not contradict their "at will" status.

409A Compliance

The intent of the Board is that payments and benefits under this plan either comply with Section 409A of the Internal Revenue Code and applicable guidance issued thereunder ("Code Section 409A") or qualify for an exemption from Code Section 409A and, accordingly, all provisions of this Plan shall be construed in a manner consistent with the requirements for avoiding taxes or penalties under Code Section 409A. The Board shall not take any action to accelerate or delay the payment of any monies and/or provision of any benefits in any matter which would not be in compliance with Code Section 409A to the extent Code Section 409A applies to such payment or benefit. Notwithstanding any of the provisions of this pay plan, the Board shall not be liable to the employee if any payment or benefit which is to be provided pursuant to this Plan and which is considered deferred compensation subject to Code Section 409A otherwise fails to comply with, or be exempt from, the requirements of Code Section 409A.

CLASS STRUCTURE

The following descriptions are the summaries of VRS' investment professional job classes/positions:

Chief Investment Officer

The CIO manages and directs investment programs, determines appropriate program structure, implementation, and monitoring. The CIO manages investment professionals who are directly responsible for internal and external investment programs. The CIO heads the Executive and Management Committees, which are responsible for reviewing all investment recommendations. The CIO collaborates with the VRS Board-appointed Investment Advisory Committee (IAC) and delivers frequent reports and updates to the VRS Board.

Managing Director

The Managing Director is a senior investment position reporting directly to the CIO. This position serves on the Investment Executive and Management Committees. The Executive Committee is a department wide resource to the CIO for management and administrative issues. The Management Committee participates in asset allocation and manager/fund allocation decisions.

Program Director

The Program Director has deep asset class knowledge and carries full managerial responsibility for a VRS investment program, including all internally and externally managed assets. The Program Director may also support multiple asset classes. The Program Director participates on the Investment Management Committee and regularly presents information to the IAC and the Board. The Program Director, as applicable, operates within an explicit risk budget and has investment performance objectives that are regularly measured. The Program Director has full responsibility for negotiating on behalf of VRS.

Director - Strategy, Research, Risk and/or Investment Decision Support

Strategy – The position within Strategy identifies and evaluates relative value-based tilt opportunities that have the potential to 1) improve the fund's return without materially increasing the risk, 2) reduce the fund's risk without materially reducing the return, or 3) some combination of these objectives. In addition, staff within Strategy 1) review and evaluate the implications of macro-economic conditions, 2) analyze current conditions and opportunities within major asset classes and key asset class subsectors, 3) monitor and evaluate the tactical and strategic tilts of key VRS investment partners, and 4) identify strategy ideas including risk and return expectations for base case and alternative scenarios.

Research – The position within Research has responsibility to support both basic and applied research efforts for all VRS investment staff. This effort includes monitoring, coordinating, facilitating, and implementing current best practices and methods to ensure optimal investment performance and risk management at both the program and plan level.

Risk – The position within Risk has responsibility in the design, implementation, and management of the risk management program including project management (solicitation and queueing of projects from clients), guidance and coordination within the group, mathematical and statistical analysis of empirical problems, risk management, and high-level programming. Additionally, staff within Risk assist with the design and implementation of a diverse collection of strategies designed to have low or negative correlation to other VRS asset classes.

Investment Decision Support – The position within Investment Decision Support has responsibility for the design and delivery of investment program, risk management, strategy, and research analytic systems. As a component of this, staff is responsible for all investments data as well as the design, development and implementation of the quantitative infrastructure for the VRS investment programs. This includes a data

warehouse, various data retrieval tools, quantitative analysis tools, program level reporting tools and support applications that retrieve, consolidate and report information.

Senior Portfolio Manager

The Senior Portfolio Manager positions have responsibility for multiple portfolio strategies and/or may supervise one or more Senior Investment Officers or Portfolio Managers. The Senior Portfolio Manager positions provide a potential career progression ladder for Portfolio Managers over time, considering the contributions, experience and sustained performance for the incumbents.

Portfolio Manager

The Portfolio Manager provides critical input to strategy development and is responsible for the more complicated and higher risk investments. The Portfolio Manager may delegate to the Senior Investment Officer certain portions of the investment program. The Portfolio Manager will begin to negotiate terms on behalf of VRS. The Portfolio Manager, from time to time, makes presentations and recommendations to the Management Committee, and perhaps the IAC and Board.

The Portfolio Manager supporting the Defined Contribution Plans is a senior investment position reporting directly to the Managing Director - Private Market Assets and DC Plans. This position provides critical input to the design, implementation, and monitoring of all investment related aspects of the VRS defined contribution plans (DC). Responsibilities include (1) evaluation and selection of new investment strategies, managers and/or funds, (2) negotiating terms on behalf of VRS, (3) monitoring and management of relationships with existing defined contribution investment managers, (4) implementing investment policy as determined by the VRS Board, (5) presenting to the Defined Contribution Plans Advisory Committee and the Board, and (6) any other projects or duties relating to the defined contribution program as may be assigned from time to time.

Senior Investment Officer

The Senior Investment Officer has higher level monitoring responsibilities that tend to involve higher risk and strategies that are more complicated. Some Senior Investment Officers may have day-to-day responsibilities for managing internal portfolios, subject to risk limits prescribed by the program director. The Senior Investment Officer will increasingly become involved in strategy development and formal recommendations to the Program Director.

Investment Officer

The Investment Officer, in addition to analytical responsibilities, may have direct responsibility for monitoring some portion of the existing portfolio, or some strategies or managers under consideration in the future. Such assignments will typically be in lower risk and less complicated strategies. The Investment Officer may continue to be involved in monitoring, compliance, and administration, but will also begin to make formal investment recommendations to the Program Director.

Senior Investment Analyst

The Senior Investment Analyst performs various types of analysis at the direction of more senior staff members. Analyst activities are geared around providing support for senior staff members more directly involved in the decision-making process. Such activities will include research, reporting, monitoring, compliance, and administration.

Investment Analyst

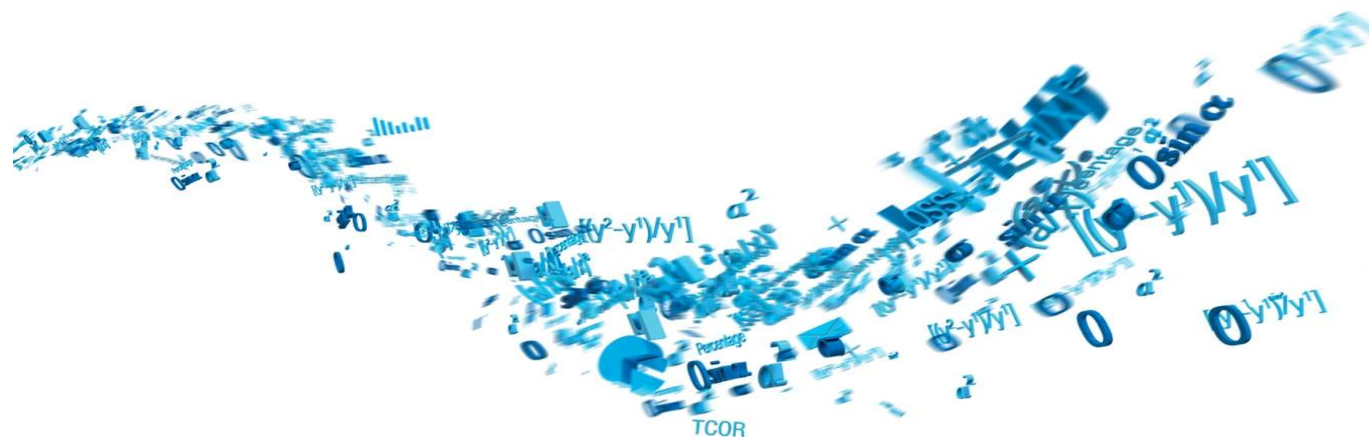
The Investment Analyst assists other investment professionals in their daily operations, including investment research and analysis, trading, and portfolio management. Analysts follow and report current market information relating to assigned sectors of the market. In addition, the Analyst conducts

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independent research on various topics, performs data maintenance, integrity, and report generation tasks.



Investment Compensation Program Review

April 2022

Competitive Market Trends

Public Funds

- YE 2020 salaries and total cash compensation stay the course (i.e., up low single digits for those that received pay increases).
- While many funds froze pay last year due to the pandemic, these freezes have been lifted as the labor market and asset levels have rebounded.
- Significant turnover for EDs and CIOs across leading public funds, mostly due to retirements and to departures to the private sector (e.g., Maryland SRPS, North Dakota, New Mexico PERA, PA PSERS, CalSTRS, MOSERS, CalPERS, Penn SERS).
- Many funds continue to struggle in their executive search efforts, often due to: prohibitions about use of search firms, pay-related limitations/constraints, perceptions of challenging internal politics, and a robust labor market in the private sector (e.g., asset management firms, OCIOs, E&Fs, family offices, etc.).
- Many funds explore remote long-term work opportunities

Private Sector

- YE 2021 Market: The BIG maybe. The best pay year in over 20 years: high-water-mark absolute pay, the highest year-over-year percentage change in pay funding. In particular, if financial markets remain flat through year-end, then within diversified firms:
 - Bonus pools should be up 20% or more, driving payouts of 30%+ for top-performing senior-level employees.
 - Profits should be up by about the same amount.
- Hiring has normalized – Covid-related restraints have been lifted
- The HR agenda is largely focused on:
 1. Defining what return-to-the office really means:
 - The tactical: What are the protocols related to masks, vaccines, office space, etc.?
 - The soft stuff: How to drive innovation, reinforce culture, and assimilate new hires?
 2. DE&I. While a top strategic priority, quantitative progress will likely continue to fall short of stated objectives, given:
 - Low turnover and net hiring trending at about +5%.
 - An especially tight labor market for women and diverse talent – especially in investments.
 3. Supporting business change, often focused on tech, alternatives and non-US operations.

Introduction & Methodology

- Virginia Retirement System Board of Trustees (“VRS”) asked McLagan to assess the competitiveness of VRS’ investment professionals’ pay levels versus their Board-approved targeted pay positioning. Specifically, for:
 - Salaries, VRS targets the 75th percentile of leading public pension funds.
 - Target total compensation, VRS targets median total cash (weighted 75% to leading public pension funds and 25% to a broad range of private sector firms).
- In reviewing its current pay levels, VRS would like to ensure that it continues to:
 - Attract, motivate and retain its skilled investment professionals.
 - Benefit all stakeholders through a compensation plan that is clear, aligned with performance, competitive and cost effective.
 - Directly align compensation with long-term investment performance.
- To complete this review, McLagan:
 - Reviewed background materials provided by VRS (e.g., plan documents, JLARC reviews, updated survey matches, etc.).
 - Assembled pay data from McLagan’s proprietary *2020 Investment Management Surveys* for VRS’ long-standing blended peer group (weighted 75% to leading public funds and 25% to a broad range of private sector firms).
- In addition, McLagan also reviewed VRS’ current incentive plan structure which can be found later in this document.

Pay Level Analysis

■ **Base Salary**

- In aggregate, VRS’ base salary spend for 50 investment professionals of \$9.9M was positioned -9% below the targeted \$10.9M 75th percentile.

	VRS Inv Prof		Targeted Pay Positioning	Competitive Market			VRS Variance vs. Targeted Positioning
	# of Incs	Spend		25th	50th	75th	
Base Salary	50	\$9,933	75th %ile Public Funds	\$8,768	\$9,829	\$10,953	-9%

■ **Target Total Compensation**

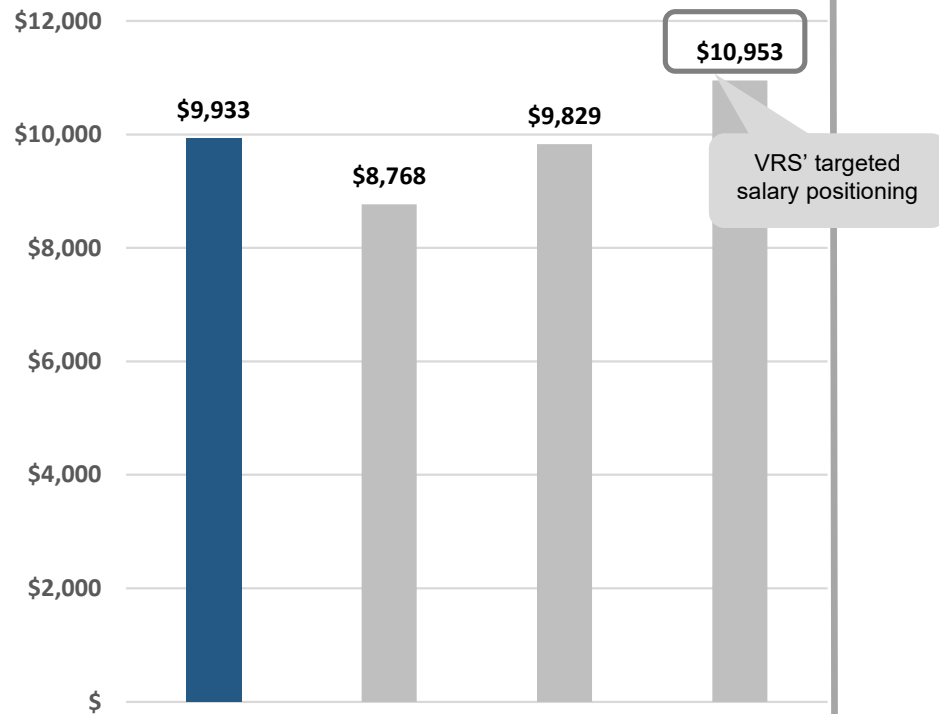
- VRS’ aggregate \$14.6M target total compensation (i.e., base salary + target incentives) fell 14% below the targeted \$17.0M median.

	VRS Inv Prof		Targeted Pay Positioning	Competitive Market			VRS Variance vs. Targeted Positioning
	# of Incs	Spend		25th	50th	75th	
Target Total Comp	50	\$14,623	Med 75% / 25% Blend	\$13,114	\$17,027	\$24,247	-14%

Overview – Base Salaries and Target Total Cash

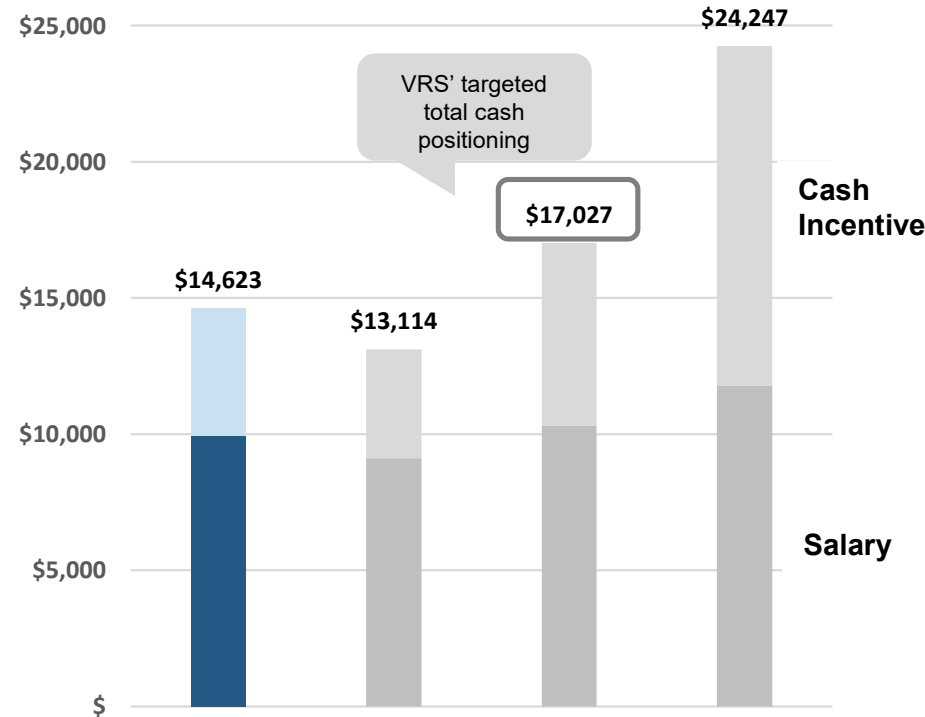
Aggregate spend for 50 VRS incumbents

VRS' Salaries vs. Leading Public Funds



	VRS	Leading Public Funds		
		25th	50th	75th
Salary	\$9,933	\$8,768	\$9,829	\$10,953
Variance		13%	1%	-9%

VRS' Target Total Cash vs. 75/25 Blend



	VRS	75th Pub Fund / 25% Priv Sect		
		25th	50th	75th
Salary	\$9,933	\$9,115	\$10,301	\$11,771
Cash Incentive	\$4,689	\$3,999	\$6,726	\$12,476
Total Cash	\$14,623	\$13,114	\$17,027	\$24,247
Variance		12%	-14%	-40%

Note: VRS' Pay Philosophy is to target base salaries at the 75th percentile of leading public funds with total cash compensation targeted at the median of the 75/25 blended peer group.

Pay Level Analysis Base Salaries

- In aggregate, VRS' salary spend is positioned 9% below the 75th percentile of other leading public funds. 76% of staff are paid below the 75th percentile.
- The incumbent-weighted positioning is driven by the more junior levels, whose aggregate salary spend fell 14%, 27% and 13% below the market 75th percentile, respectively.

VRS Investment Management	Salary	# EEs Matched	Leading Public Funds Base Salary			Positioning vs 75th Percentile		VRS vs 75th
			25th	50th	75th	% Under	% Over	
Chief Investment Officer	\$470	1	\$397	\$450	\$546	100%	0%	-14%
Managing Director	1,000	3	757	881	983	33%	67%	2%
Program Director	2,040	7	1,690	1,863	1,996	43%	57%	2%
Director	1,142	5	1,013	1,138	1,251	80%	20%	-9%
Senior Portfolio Manager	461	2	398	454	499	50%	50%	-7%
Portfolio Manager	2,518	13	2,201	2,494	2,800	77%	23%	-10%
Senior Investment Officer	1,088	7	1,000	1,119	1,270	86%	14%	-14%
Investment Officer	952	9	1,057	1,158	1,308	100%	0%	-27%
Senior Investment Analyst	262	3	256	273	302	100%	0%	-13%
Total	\$9,933	50	\$8,768	\$9,829	\$10,953	76%	24%	-9%

Base Salaries + Target Incentives

- While salaries are largely competitive across all levels, target total cash is less competitive. In aggregate, VRS' target total compensation spend fell 14% below the median of the 75/25 blended peer group.
- 88% of VRS incumbents have target total cash levels below the targeted median of the 75/25 blended peer group.
- It is important to note that all positions have the opportunity to earn more than median compensation for maximum levels of performance (see Appendix).

VRS Investment Management	T. Cash	# EEs Matched	Blended Peer Group			Positioning vs 75th Percentile		VRS vs 50th
			25th	50th	75th	% Under	% Over	
Target Total Cash								
Chief Investment Officer	\$798	1	\$619	\$794	\$1,114	0%	100%	0%
Managing Director	1,650	3	1,430	1,917	3,041	100%	0%	-14%
Program Director	3,264	7	2,729	3,610	5,741	100%	0%	-10%
Director	1,713	5	1,813	2,329	3,352	100%	0%	-26%
Senior Portfolio Manager	692	2	645	908	1,387	100%	0%	-24%
Portfolio Manager	3,526	13	2,977	4,003	5,473	77%	23%	-12%
Senior Investment Officer	1,415	7	1,299	1,642	1,952	100%	0%	-14%
Investment Officer	1,238	9	1,311	1,489	1,774	89%	11%	-17%
Senior Investment Analyst	327	3	291	334	415	67%	33%	-2%
Total	\$14,623	50	\$13,114	\$17,027	\$24,247	88%	12%	-14%

Pay Level Analysis

VRS Midpoints

- While the previous pages focused on actual salaries and incentive opportunities, the below analysis focuses on VRS' target midpoints.
- Most targeted salary midpoints fell slightly below the public fund 75th percentile while most targeted total compensation midpoints fell below the median of the targeted 75/25 blend.

Position	Salary Grade	Base Salary			Sal + Target Incentive			
		Current Mid	Pub Fund 75th	Variance %	% Sal	Current Mid	75/25 Median	Variance %
Chief Investment Officer	12	408	546	-25%	70%	694	794	-13%
Deputy Chief Investment Officer	11	336	--	--	65%	554	--	--
Managing Director	10	326	328	-1%	65%	538	639	-16%
Program Director	9	265	285	-7%	60%	424	516	-18%
Director - Strategy, Research, or Risk	8	242	250	-3%	50%	363	466	-22%
Senior Portfolio Manager	7	242	249	-3%	50%	363	454	-20%
Portfolio Manager	6	210	215	-2%	40%	294	308	-5%
Risk Manager, Research Manager	5	188	--	--	30%	244	--	--
Senior Investment Officer	4	155	181	-15%	30%	202	235	-14%
Investment Officer	3	116	145	-20%	30%	151	165	-9%
Senior Investment Analyst	2	94	101	-6%	25%	118	111	6%
Investment Analyst	1	77	--	--	5%	81	--	--

Pay Level Analysis

VRS' Current and Proposed Salary Ranges

The survey data used in this exhibit differs from the prior pages. The data used on slides 10 & 11 has been aged to reflect the most recent performance year.

- To remain competitive with other leading public funds, McLagan proposes the below changes to VRS' salary range structure:
 - Proposed changes to the current salary range using VRS target midpoints (75th percentile of public fund peers).
 - Compress the below levels:
 - Deputy CIO and Managing Director
 - Portfolio Manager and Manager

Grade	Position	Current Salary Range			PF 75th %ile	Proposed Salary Range		
		Min	Mid	Max		Min	Mid	Max
12	Chief Investment Officer	\$327	\$408	\$489	\$579	325	\$430	540
11	Deputy Chief Investment Officer	269	336	403	364	275	365	455
10	Managing Director	260	326	391	348			
9	Program Director	212	265	317	303	235	315	395
8	Director	193	242	290	265	205	275	345
7	Senior Portfolio Manager	193	242	290	265	205	275	345
6	Portfolio Manager	168	210	251	228	160	215	270
5	Manager	150	188	225	--			
4	Senior Investment Officer	124	155	185	192	135	180	225
3	Investment Officer	92	116	139	154	105	140	175
2	Senior Investment Analyst	75	94	113	107	80	105	130
1	Investment Analyst	61	77	91	88	65	85	105

Note: The Public Fund survey data has been aged 3% per year from 2020 to 2022 for base salaries.

VRS' Proposed Salaries & Target Total Comp

The survey data used in this exhibit differs from the prior pages. The data used on slides 10 & 11 has been aged to reflect the most recent performance year.

- Incorporating VRS' current target incentives (as a percent of salary) and proposed salary ranges, the variance to market median total cash is approximately +/- 10% in all instances except for the Director and Senior Portfolio Manager levels.

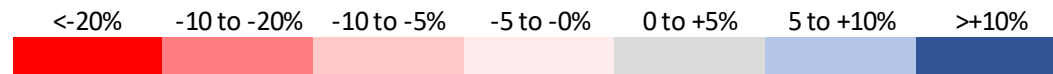
Position	Salary Grade	VRS - Proposed Salary Range			Sal + Target Incentive						
		Minimum	Midpoint	Maximum	Target T.Comp Range				75/25 Median	Variance \$	Variance %
					IC % Sal	Minimum	Midpoint	Maximum			
Chief Investment Officer	10	\$325	\$430	\$540	70%	\$553	\$731	\$918	\$832	-\$101	-12%
Dep CIO / Managing Director	9	275	365	455	65%	454	602	751	670	-67	-10%
Program Director	8	235	315	395	60%	376	504	632	540	-36	-7%
Director	7	205	275	345	50%	308	413	518	484	-72	-15%
Senior Portfolio Manager	6	205	275	345	50%	308	413	518	484	-72	-15%
Portfolio Manager / Manager	5	160	215	270	40%	224	301	378	323	-22	-7%
Senior Investment Officer	4	135	180	225	30%	176	234	293	246	-12	-5%
Investment Officer	3	105	140	175	30%	137	182	228	173	9	5%
Senior Investment Analyst	2	80	105	130	20%	96	126	156	117	9	8%
Investment Analyst	1	65	85	105	10%	72	94	116	--	--	--

Note: The Public Fund survey data has been aged 3% per year from 2019 to 2021 for total cash compensation. The private sector data has been aged 7% per year from 2019 to 2021 for total cash compensation.

Investment Professional Total Compensation 2017 - 2020

- Overall, total compensation for all employees within US public funds tends to increase modestly each year (approximately +0% to +4%).
- Investment functions however, have seen larger increases each year. Since 2017, total compensation for investment professionals within public funds has increased low- to mid-single digits at median.
- Important to note, the below covers only constant incumbents (present in all three years) and those within the investment functions (e.g., portfolio management, research, trading, etc.).

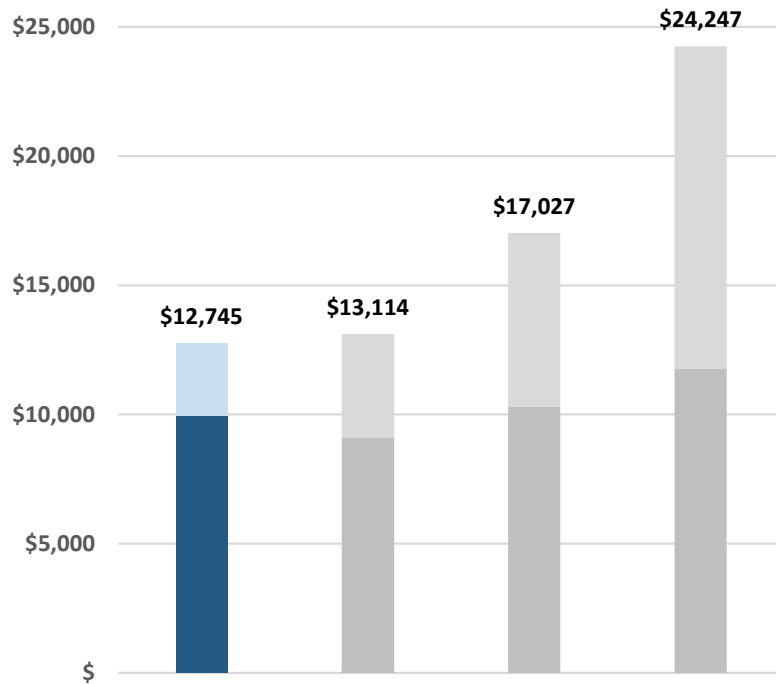
Investment Only	All Constant Incs			Only Bonus Eligible Constant Incs		
	% Δ Total Compensation			% Δ Total Compensation		
	'17 to '18	'18 to '19	'19 to '20	'17 to '18	'18 to '19	'19 to '20
\$0 - \$100K	8%	8%	5%	9%	7%	4%
\$100K - \$200K	6%	5%	3%	7%	5%	3%
\$200K - \$300K	4%	7%	2%	4%	7%	3%
\$300K - \$500K	2%	6%	5%	2%	7%	5%
\$500K+	3%	0%	4%	3%	0%	4%
# of Constant Incs	1,565			958		



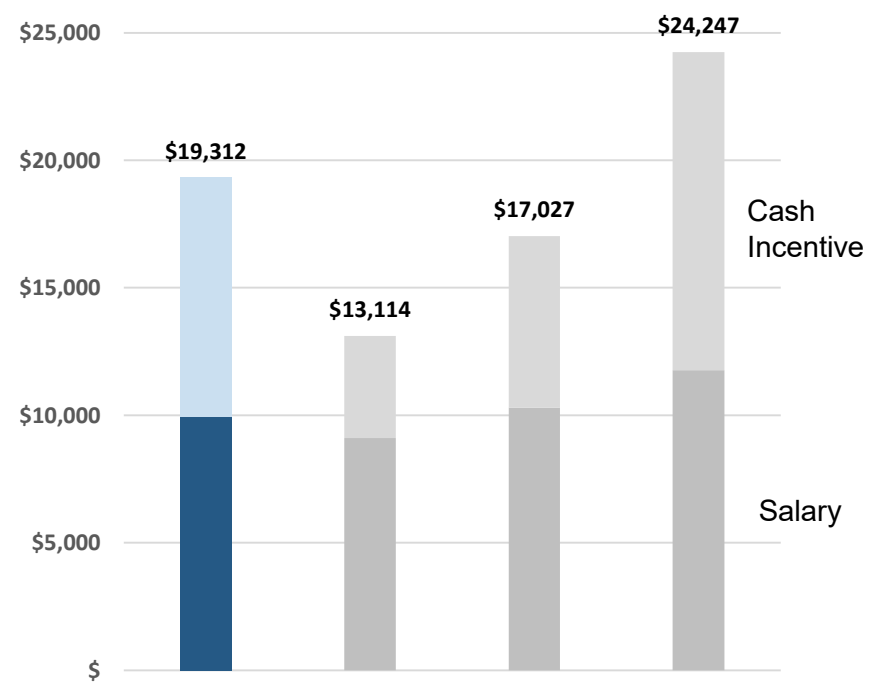
Appendix I

Overview – Maximum and Actual Total Cash

VRS' Actual Total Cash vs. 75/25 Blend



VRS' Maximum Total Cash vs. 75/25 Blend



Base Salaries + Maximum Incentives

- Consistent with its pay philosophy, all VRS positions have the opportunity to earn above-median pay for superior performance (e.g., all incentive components at maximum). As with previous years, VRS' \$19.3M maximum total cash falls between the \$17.0M median and \$24.2M 75th percentile.

VRS Investment Management	T. Cash	# EEs Matched	Blended Peer Group T. Cash			Positioning vs 75th Percentile		VRS vs 50th
			25th	50th	75th	% Under	% Over	
Maximum Total Cash								
Chief Investment Officer	\$1,127	1	\$619	\$794	\$1,114	0%	100%	42%
Managing Director	2,301	3	1,430	1,917	3,041	33%	67%	20%
Program Director	4,488	7	2,729	3,610	5,741	0%	100%	24%
Director	2,284	5	1,813	2,329	3,352	60%	40%	-2%
Senior Portfolio Manager	923	2	645	908	1,387	50%	50%	2%
Portfolio Manager	4,533	13	2,977	4,003	5,473	15%	85%	13%
Senior Investment Officer	1,741	7	1,299	1,642	1,952	29%	71%	6%
Investment Officer	1,524	9	1,311	1,489	1,774	56%	44%	2%
Senior Investment Analyst	393	3	291	334	415	0%	100%	18%
Total	\$19,312	50	\$13,114	\$17,027	\$24,247	28%	72%	13%

Base Salaries + Actual Earned Incentives

- Based on actual earned incentives, VRS' \$12.7M total cash spend fell 25% below the \$17.0M median reflecting that for these 50 incumbents, actual payouts were below both target and maximum.

VRS Investment Management	T. Cash	# EEs Matched	Blended Peer Group			Positioning vs 75th Percentile		VRS vs 50th
			T. Cash	25th	50th	75th	% Under	
Actual Total Cash								
Chief Investment Officer	\$602	1	\$619	\$794	\$1,114	100%	0%	-24%
Managing Director	1,402	3	1,430	1,917	3,041	100%	0%	-27%
Program Director	2,742	7	2,729	3,610	5,741	86%	14%	-24%
Director	1,645	5	1,813	2,329	3,352	100%	0%	-29%
Senior Portfolio Manager	512	2	645	908	1,387	100%	0%	-44%
Portfolio Manager	3,114	13	2,977	4,003	5,473	92%	8%	-22%
Senior Investment Officer	1,310	7	1,299	1,642	1,952	100%	0%	-20%
Investment Officer	1,119	9	1,311	1,489	1,774	100%	0%	-25%
Senior Investment Analyst	299	3	291	334	415	100%	0%	-10%
Total	\$12,745	50	\$13,114	\$17,027	\$24,247	96%	4%	-25%

Leading Public Funds Peer Group

Leading Public Funds Peer Group		
	AUM	% Internally Managed
California Public Employees' Retirement System	\$394.7	
California State Teachers' Retirement System	254.1	
New York State & Local Retirement System	225.9	
Florida State Board Administration	169.7	
Teacher Retirement System of Texas	160.0	
New York State Teachers' Retirement System	125.6	
Washington State Investment Board	107.5	
State of Wisconsin Investment Board	116.5	
Ohio Public Employees' Retirement System	104.2	
State Teachers Retirement System of Ohio	71.5	
Michigan State Retirement Systems	77.7	
Colorado Public Employees Retirement Association	52.0	
Hig Quartile	\$183.8	61%
Median	121.0	51%
Low Quartile	97.6	43%
Virginia Retirement System	\$92.1	29%

*Amounts for VRS were provided by VRS to McLagan.

Private Sector Firm Summary

All Private Sector				
	# Firms	12/31/19 AUM (\$Billions)		
		LowQ	Median	HighQ
Investment Mangement Firms	162	\$14.9	\$53.1	\$218.6
Banks (Investment Management Department)	24	15.8	38.6	88.6
Insurance Companies (Investment Management Departments)	39	26.1	63.1	97.3
Endowments & Foundations	54	1.9	3.3	7.2
Corporate Plan Sponsors	11	1.7	6.0	17.6
Total	290	\$7.0	\$28.4	\$101.2



Reappoint IAC members and appoint new IAC member.

Requested Action

The Board reappoints Theodore Economou, Thomas Gayner and Lawrence Kochard to the Investment Advisory Committee, each for a two-year term ending September 13, 2024, February 19, 2025, and February 16, 2025, respectively, and appoints Palmer P. Garson for a two-year term ending October 16, 2024.

Rationale for Requested Action

Theodore Economou, Thomas Gayner and Lawrence Kochard currently serve on the Investment Advisory Committee (IAC) and are willing to be reappointed for another two-year term. Mr. Economou most recently served as CIO for Lombard Odier Investment Managers. Mr. Gayner is Co-Chief Executive Officer of Markel Corporation. Mr. Kochard is the Chief Investment Officer at Makena Capital Management.

Palmer P. Garson has been a Managing Director of Silvercrest Asset Management Group since 2013, and she has 30 years of service in the financial services industry, beginning in investment banking and private equity and progressing to wealth management. Earlier in her career, she co-founded Jefferson Capital Partners, a private equity firm, and developed extensive finance experience while working for Morgan Stanley & Co., A.G. Edwards and Mellon Bank. Ms. Garson also served one term as a member of the VRS Board of Trustees from 2005 to 2010. Ms. Garson has a Bachelor of Arts degree from Duke University and a Master of Business Administration from the Darden Graduate School of Business at the University of Virginia. A copy of her biography is attached.

Authority for Requested Action

Code of Virginia § 51.1-124.26 requires the Board to appoint an Investment Advisory Committee to provide the Board with sophisticated, objective, and prudent investment advice, which will further assist the Board in fulfilling its fiduciary duty as trustee of the funds of the Retirement System.

The above action is approved.

A. Scott Andrews, Chair
VRS Board of Trustees

Date

THEODORE ECONOMOU, CFA

Board Member and Advisor

- Board positions in Europe, USA and Asia
 - 30-year executive career spanning public corporations and governmental organizations
 - Advising financial & investment organizations representing more than \$100bn in assets
 - Asset management experience covering private assets, public assets and real assets.
-

BOARD AND ADVISORY MANDATES

EUROBANK PRIVATE BANK LUXEMBOURG SA (Luxembourg) 2022 – Present

Member of the Board of Directors

Member of the Audit & Remuneration Committee, and of the Risk Committee.

METHAK INVESTMENT HOLDING (Jeddah, Saudi Arabia) 2022 – Present

Member of the Board of Directors

Methak IH is the investment arm of the Methak Educational Endowment

VIRGINIA RETIREMENT SYSTEM (Virginia, USA) 2013 – Present

Member, Investment Advisory Committee

Attend 3 investment committee and board meetings per year to advise on the management of US\$100 billion in assets owned by the retirement system for the government employees of the commonwealth of Virginia, USA.

CLAREMONT GRADUATE UNIVERSITY (California, USA) 2014 – Present

**Member of the Board, Financial Engineering Advisory Board ,
The Peter Drucker and Masatoshi Ito Graduate School of Management**

Provide guidance and expertise on the use of quantitative strategies by institutional investors

PRIVATE FAMILY TRUST (Geneva, Switzerland) 2013–Present

Advisor & proxy holder

Manage a portfolio of 100 apartments in the city of Geneva.

LOMBARD ODIER PENSION FUND (Geneva, Switzerland) 2014 – 2020

Chair, Investment Committee

Led restructuring of 1.5Bn CHF investment portfolio to target higher performance.

- Restructured Base portfolio around time horizons in order to reconcile return, risk, and liquidity goals and constraints with the Foundation Board requirements • Designed and implemented 1(e) excess pension program launched in January 2018.
- Increased private assets allocation to 30% of total.
- Lombard Odier Pension Fund won « high commendation » at the 2019 Pension Fund Awards sponsored by Investment & Pensions Europe (IPE).

Getting to know Tom Gayner



Thomas "Tom" Gayner is Co-Chief Executive Officer of Markel Corporation, a diverse financial holding company including insurance, reinsurance, and investment operations around the world. Markel is listed on the Fortune 500 and is headquartered in Richmond, Virginia, with 61 offices in 16 countries.

Tom joined Markel in 1990 and oversees all investing activities. He is also responsible for Markel Ventures, a wholly owned subsidiary which acquires controlling interests in manufacturing, technology, and service companies.

Prior to Markel, Tom served as Vice President of Davenport & Company LLC of Virginia and as a certified public accountant with PricewaterhouseCoopers LLP.

Tom serves as the Chairman of the Board of the Davis Series Mutual Funds and on the boards of the Graham Holdings, Cable One, and Markel. He is a member of the Investment Advisory Committee of the Virginia Retirement System.

Tom is a graduate of the University of Virginia and The Lawrenceville School.



Contact

lkochard@gmail.com

www.linkedin.com/in/larry-kochard-4a21b6b (LinkedIn)

Top Skills

Alternative Investments

Hedge Funds

Asset Management

Honors-Awards

Rodney H. Adams Award for
Endowment Management

Publications

Using a Z-score Approach to
Combine Value and Momentum in
Tactical Asset Allocation

Low-Volatility Cycles: The Influence
of Valuation and Momentum on Low-
Volatility Portfolios

Larry Kochard

Chief Investment Officer at Makena Capital Management, LLC
Charlottesville, Virginia, United States

Summary

Larry Kochard is the Chief Investment Officer (CIO) at Makena Capital Management. He is also a Managing Director and a member of the firm's Executive Committee. Larry was previously the Chief Executive Officer and Chief Investment Officer of the University of Virginia Investment Management Company (UVIMCO).

In addition to being CIO of Makena, Larry serves on the board of Janus Henderson Group (where he chairs the compensation committee), is Chair of the Investment Advisory Committee of the Virginia Retirement System, and is on the board of the Virginia Museum of Fine Arts (VMFA). Larry has also served on the boards of the Virginia Environmental Endowment (VEE), VCU Investment Management Co., and The College of William and Mary Foundation (W&M). He chaired the investment committees at VEE and W&M, and is currently a member of the investment committee of the VMFA. He also guest lectures and teaches investment classes at the University of Virginia. Larry is the co-author with Cathleen Rittereiser of *Foundation and Endowment Investing: Philosophies and Strategies of Top Investors and Institutions*. Featuring profiles of successful chief investment officers, the book was published by John Wiley and Sons in December 2007.

Larry holds a BA in Economics from the College of William & Mary, an MBA in Finance and Accounting from the University of Rochester, an MA and PhD in Economics from the University of Virginia, and is a CFA charter holder. He is married and has four children.

Experience

Makena Capital Management, LLC

Chief Investment Officer

January 2018 - Present (4 years 10 months)

Menlo Park, CA

Janus Henderson Group
Board member
2008 - Present (14 years)

UVIMCO
CEO/CIO
January 2011 - December 2017 (7 years)
Charlottesville, VA

Georgetown University
Chief Investment Officer
July 2004 - December 2010 (6 years 6 months)
Manage \$1 billion endowment and seven full-time staff members.

Virginia Retirement System
6 years

Managing Director of Equity and Hedge Fund Investments
2001 - 2004 (3 years)

- Managed \$30 billion of the \$40 billion pension fund for public employees and teachers.
- Managed 16 investment professionals.
- Managed \$27 billion public equity program.
- Public equity portfolio included money managed internally (\$6 billion), in addition to hiring, managing and firing external money managers.
- Portfolio included US and non-US investments.
- Managed \$1.2 billion hedge fund program.
- Managed \$2 billion private equity program.
- Actively involved in asset allocation decisions.
- Managed \$500 million defined contribution program.
- Restructured public equity program.
- Lead staff person on the corporate governance task force (2002).

Member, Investment Advisory Committee
1998 - 2001 (3 years)

The Investment Advisory Committee (IAC) advises the Board of Trustees regarding investments of the pension fund for public employees and teachers in Virginia. The IAC is responsible for advising the Board on recommendations made by the staff regarding the merits of active and passive investment strategies, as well as internal and external investment programs. The IAC recommends long-term asset allocation ranges and new asset classes for

approval by the Board of Trustees, and approves target asset allocations within the long-term ranges.

1990 to 1993

This period was spent in Sacramento, California, recuperating from an illness. During this time I volunteered to manage Muriel Johnson's campaign for Sacramento County Supervisor (she won and is completing her eleventh year in office), and started preparations for my doctoral studies in Economics.

Goldman Sachs

Vice President

1986 - 1989 (3 years)

Capital Markets

- Capital markets Coverage Officer for Savings & Loans, Mortgage Banks and Government Agencies.
- Helped clients manage the liability side of their balance sheets.
- Coordinated the execution of new debt and preferred issues in the public and private markets.
- Assisted clients with hedging interest rate and currency risks.
- Helped clients manage their capital structure through innovative financing approaches.

Education

University of Virginia

Ph.D., Economics · (1994 - 1999)

University of Virginia

MA, Economics · (1996)

University of Rochester - William E. Simon Graduate School of Business Administration

MBA, Finance and Accounting · (1978 - 1980)

William & Mary

VA, Economics · (1974 - 1978)

Palmer P. Garson**Managing Director – Silvercrest Asset Management Group**

Palmer P. Garson joined Silvercrest Asset Management as a Managing Director in 2013. Palmer's more than 30-year career in financial services began in investment banking and private equity and progressed to wealth management. Earlier in her career, she co-founded Jefferson Capital Partners, a private equity firm, and developed extensive finance experience while working for Morgan Stanley & Co., A.G. Edwards and Mellon Bank. Palmer currently serves as a trustee for the Mary Morton Parsons Foundation, the Virginia Foundation of Independent Colleges and Saint Mary's School. She has served on numerous investment committees and is currently active with VCIMCO (VCU's Endowment), Randolph College, Virginia Foundation of Independent Colleges, Saint Mary's School (chair) and The Order of St. John. Palmer has also been active with Collegiate School where she was board chair on two separate occasions. She is also a former trustee for the Duke Alumni Association and the Darden School Foundation. Palmer has a Bachelor of Arts degree from Duke University and a Master of Business Administration from the Darden Graduate School of Business at the University of Virginia.



Amend Board governance documents to reflect the renaming of the Administration and Personnel Committee to the Administration, Finance and Talent Management Committee.

Requested Action

The Virginia Retirement System Board of Trustees approves amendments to its Governance Policy; the Administration and Personnel Committee charter; the Audit and Compliance Committee charter; and, the Code of Ethics and Conduct to accommodate the change in the name of the Administration and Personnel Committee to the Administration, Finance and Talent Management Committee.

Description/Background

At its September 14, 2022, meeting, the Administration and Personnel Committee agreed to recommend to the Board that its name be changed to the **Administration, Finance and Talent Management Committee**. There are several governance-related documents that require amendments.

The affected documents are:

- Board Governance Policy;
- Administration and Personnel Committee charter;
- Audit and Compliance Committee charter; and
- Code of Ethics and Conduct.

In accordance with its duties under the Administration and Personnel Committee charter, the Administration and Personnel Committee reviewed the Board’s Governance Policy, the two affected committee charters, the Code of Ethics and Conduct and the proposed amendments. The Administration and Personnel Committee concurs with and recommends the proposed amendments.

In accordance with the Board’s Governance Policy, the Administration and Personnel Committee presented the proposed Governance Policy and committee charter amendments at a prior Board meeting to allow the changes to be voted on for final approval at today’s meeting.

Authority for Requested Action

Code of Virginia § 51.1-124.22(A)(8) authorizes the Board to make determinations necessary to carry out the provisions of Title 51.1 of the Code of Virginia.

The above action is approved.

A. Scott Andrews, Chair
VRS Board of Trustees

Date

BOARD OF TRUSTEES GOVERNANCE POLICY

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BOARD OF TRUSTEES GOVERNANCE POLICY

I. PURPOSE

This Governance Policy is established to:

- A. Set forth the policies and procedures pursuant to which the Board of Trustees will fulfill its statutory and fiduciary responsibilities;
- B. Ensure that the Board will perform its functions in a manner that is consistent with and in furtherance of the principles set forth below; and
- C. Facilitate the organized, efficient, and cohesive functioning of the Board.

II. AUTHORITY

Title 51.1 of the *Code of Virginia* establishes the Virginia Retirement System (“VRS”) as an independent agency of the Commonwealth, and sets forth the purpose, powers, and duties of the Board of Trustees (the “Board”) relative to its responsibilities as administrator and trustee of the retirement systems and plans provided for therein and in Article X, Section 11 of the Constitution of Virginia.

Pursuant to Title 51.1, the Board administers and is trustee of the funds of the Virginia Retirement System Trust, including Plan 1, Plan 2, the defined benefit component of the Hybrid Retirement Plan, and Plan 1 and Plan 2 hazardous duty benefits for political subdivision employees; the State Police Officers’ Retirement System Trust, including Plan 1 and Plan 2; the Virginia Law Officers’ Retirement System Trust, including Plan 1 and Plan 2; the Judicial Retirement System Trust, including Plan 1 and Plan 2, and the defined benefit component of the Hybrid Retirement Plan for judges; the Virginia Sickness and Disability Program (VSDP) Trust for state employees, including VSDP long-term care; the Virginia Local Disability Program (VLDP) Trust for eligible school division and political subdivision employees, including VLDP long-term care; a disability retirement option for certain members not covered under VSDP or VLDP; the Hybrid 457 Deferred Compensation Plan; the Hybrid 401(a) Cash Match Plan; the Optional Retirement Plan for Political Appointees, the Optional Retirement Plan for School Superintendents, the Optional Retirement Plan for Employees of Higher Education (ORPHE); the Commonwealth of Virginia 457 Deferred Compensation Plan; the Virginia Cash Match Plan; the Virginia Supplemental Retirement Plan; the Group Life Insurance Program; the Retiree Health Insurance Credit Program; and the Line of Duty Death and Health Benefits Trust Fund.

In addition, pursuant to Title 51.1, the Board administers or has substantial oversight responsibilities for the Benefit Restoration Plan, the Commonwealth of Virginia Voluntary Group Long Term Care Insurance Program, and the Volunteer Firefighters' and Rescue Squad Workers' Service Award Fund Program, as well as benefit eligibility determinations under the Line of Duty Act in Title 9.1.

III. PRINCIPLES

A. COMMITMENT:

The Board is dedicated to seeing that VRS accomplishes its mission and fulfills its vision. These are:

Mission: "VRS delivers retirement and other benefits to Virginia public employees through sound financial stewardship and superior customer service."

Vision: "To be the trusted leader in the delivery of benefits and services to those we serve."

B. GOVERNING STYLE:

1. To achieve its commitment, the Board will govern with an emphasis on:
 - a) Outward vision and strategic leadership rather than administrative focus;
 - b) Encouraging diversity of viewpoints;
 - c) Maintaining a clear distinction between the roles of the Board and those of the Director, the Chief Investment Officer, and the Audit Director;
 - d) Collective determination rather than individual decision-making; and
 - e) Being proactive rather than reactive.

2. Accordingly, in all of its deliberations, actions, and decisions, the Board will be guided by the following principles:
 - a) The Board's focus will be to set long-term objectives and goals for members, retirees and beneficiaries, not on day-to-day administrative operations;
 - b) The Board will set broad organizational values and perspectives to guide VRS staff;
 - c) The Board will exercise whatever self-discipline is needed to govern with excellence. Discipline will apply to matters such as preparation for meetings, attendance, policy-making principles, respect of clarified roles, and speaking with one voice;

- d) The Board will be accountable to the members, retirees and beneficiaries for competent, conscientious and effective accomplishment of its obligations; and no officer, individual, or committee of the Board will usurp this role or hinder this commitment.
- e) The Board will monitor its own processes and performance, and it will ensure the continuity and advancement of its governance capability by orientation of new Board members and ongoing training and development of all Board members.

IV. STRUCTURE AND FUNCTION OF THE BOARD

A. COMPOSITION

1. The members of the Board are appointed, serve, and can be removed pursuant to *Code of Virginia* § [51.1.124.20](#), as it may be amended from time to time:
 - a) The VRS Board is composed of nine members, each appointed for a term of five years. No member may serve for more than two consecutive five-year terms and, should a member be appointed to complete the remainder of a former member's term, he or she may serve only one complete five-year term thereafter.
 - b) The Governor appoints five Board members and the Joint Rules Committee of the General Assembly appoints four members of the Board. All appointments must be confirmed by the General Assembly.
 - c) Of the five members appointed by the Governor, two shall have a minimum of five years of experience in the direct management, analysis, supervision or investment of assets; one shall have at least five years of direct experience in the management and administration of employee benefit plans; one shall be a local employee; and, one shall be a faculty member or employee of a state-supported institution of higher education.
 - d) Of the four members appointed by the General Assembly, two shall have a minimum of five years of experience in the direct management, analysis, supervision or investment of assets; one shall be a state employee; and one shall be a teacher.
 - e) Board members are subject to removal from office only as set forth in sections 24.2-230 through 24.2-238 of the Code of Virginia.
2. All new Board members shall complete an orientation program as soon as practicable after the date of their appointment to the Board.
3. All Board members shall sign an affirmation pledging to uphold both the letter and the spirit of the attached Board of Trustees Code of Ethics and Conduct as

soon as practicable after the date of their appointment to the Board, and at least annually thereafter.

B. STANDARD OF CARE

As provided in Article X, Section 11 of the Constitution of Virginia:

“The General Assembly shall maintain a retirement system for state employees and employees of participating political subdivisions and school divisions. The funds of the retirement system shall be deemed separate and independent trust funds, shall be segregated from all other funds of the Commonwealth, and shall be invested and administered solely in the interests of the members and beneficiaries thereof. Neither the General Assembly nor any public officer, employee, or agency shall use or authorize the use of such trust funds for any purpose other than as provided in law for benefits, refunds, and administrative expenses, including but not limited to legislative oversight of the retirement system. Such trust funds shall be invested as authorized by law. Retirement system benefits shall be funded using methods which are consistent with generally accepted actuarial principles. The retirement system shall be subject to restrictions, terms, and conditions as may be prescribed by the General Assembly.”

The Board standard of care is further described in § 51.1-124.30 of the *Code of Virginia*:

“The Board shall discharge its duties with respect to the Retirement System solely in the interest of the beneficiaries thereof and shall invest the assets of the Retirement System with care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims. The Board shall also diversify such investments so as to minimize the risk of large losses unless under the circumstances it is clearly prudent not to do so.” *Code of Virginia* § 51.1-124.30.C.

“No officer, director or member of the Board or of any advisory committee of the Retirement System or any of its tax exempt subsidiary corporations whose actions are within the standard of care in subsection C above shall be held personally liable for losses suffered by the Retirement System on investments made under the authority of this chapter.” *Code of Virginia* § 51.1-124.30.D.

C. CHAIRPERSON

The Governor designates which of the nine members of the Board shall serve as chairperson, subject to confirmation by the General Assembly. In accordance with § 51.1-124.20(D) of the *Code of Virginia*, the chairperson may serve no more than two two-year terms.

The chairperson is charged with:

1. Facilitating the operation of Board meetings;
2. Reviewing proposed agendas for Board meetings;
3. Presiding over meetings of the Board;
4. When required, certifying any actions taken by the Board;
5. Communicating on behalf of the Board to outside entities interested in VRS; and
6. Performing such additional duties as provided herein or as may be set by resolution of the Board.

D. VICE-CHAIRPERSON

The vice-chairperson is a member of the Board, elected by a majority vote of the Board. The election of the vice-chairperson shall take place at the first regular meeting following the installation of a new chairperson or at the first regular meeting following the reappointment of the chairperson. The vice-chairperson is elected for a two-year term, and may be re-elected for two additional terms.

In the event of the absence or incapacity of the chairperson, the vice-chairperson shall preside over Board meetings, and shall fulfill such other duties and responsibilities of the chairperson as may be necessary.

E. SECRETARY

The Director shall act as secretary to the Board. The Director shall continue to serve as secretary until such time as he or she is unable or unwilling to continue to do so, or until such time as the Board appoints another secretary.

The Secretary to the Board has the following duties and responsibilities:

1. To maintain a current list of the membership of the Board and of each committee;
2. To notify Board members of meetings;
3. To coordinate and disseminate information to the members of the Board;
4. To maintain official minutes and records of all proceedings of the Board;
5. To respond to requests received by VRS under the Freedom of Information Act (FOIA);
6. To accept service of process on behalf of the Board;
7. To notify Board members of training and filing requirements related to the State and Local Government Conflict of Interests Act (COIA);
8. To prepare, prior to each meeting, an agenda for use by the presiding chairperson; and
9. To coordinate presentations for the Board.

F. MEETINGS/ATTENDANCE

The Board determines and approves a regular meeting schedule on an annual basis. Changes in the schedule may be made in coordination with the Board members. The Board is authorized to schedule additional meetings, if deemed necessary, after giving appropriate notice to all members of the Board and to the public.

Attendance at Board meetings is considered to be an essential element of a Board member's fiduciary responsibility. Therefore, members are expected to attend all meetings unless there are extenuating circumstances that prevent such attendance.

G. PROCEDURAL STANDARDS

1. The rules contained in the current edition of *Robert's Rules of Order Newly Revised* shall govern all proceedings of the Board and VRS committee meetings insofar as they are applicable and not inconsistent with any of the policies adopted by the Board. Special note is to be made of the rules provided for procedure in small boards which are deemed to be appropriate for use in all meetings contemplated in these policies, including meetings of all advisory, standing, and special committees.
2. Unless otherwise specified by the Board, voting by proxy is not allowed.
3. A majority of members of the Board shall constitute a quorum at Board meetings.
4. Except as otherwise specified herein, approval of an action or decision shall be by a majority of those voting.

H. RESPONSIBILITIES AND DUTIES OF THE BOARD

To fulfill its fiduciary and administrative responsibilities, the Board may, as necessary, review, monitor, and oversee the following items, among others:

1. Agency mission and vision
2. Budget vs. Actual expenditures
3. Internal controls
4. Strategic plan and objectives
5. Design of Defined Benefit plans and programs
6. Design of Group Life and other Insurance programs
7. Design of Defined Contribution programs
8. Performance of Director, Audit Director, and Chief Investment Officer
9. Investment performance
10. Funded status
11. Actuarial valuations and demographic and economic assumptions
12. Financial health of VRS through review of financial statements

To fulfill its fiduciary and administrative responsibilities, the Board shall approve the following items, among others, as needed:

1. Governance documents
2. Agency Performance Objectives
3. Agency compensation plans
4. Funding policy and contribution rates
5. Asset allocation targets (policy risk/reward parameters)
6. Allowable ranges around the policy targets
7. Total fund and program level benchmarks
8. Active risk limits relative to policy
9. Defined Benefit Plan Investment Policy Statement
10. Defined Contribution Plans Investment Policy Statements
11. Investment Belief Statements for defined benefit and defined contribution plans
12. Appointments to Standing, Special, and Advisory Committees
13. Appointment and termination of Custodian Bank
14. Appointment and termination of Plan Actuary
15. Appointment of Director, Audit Director, and Chief Investment Officer
16. Investment and administrative budgets
17. Legislation to be introduced at VRS request
18. Cost of living increases where approval is required by statute
19. Internal Audit long-term and annual work plans.

V. CONNECTION OF THE BOARD TO VRS OPERATIONS

The Board is connected to the operations, conduct, and achievements of VRS through the Director, the Chief Investment Officer, and the Audit Director.

The individuals in these three positions are appointed, employed, monitored, and evaluated directly by the Board. They constitute the Board's only link to each area of VRS. Therefore, as specified below, all authority and accountability of the VRS staff, as far as the Board is concerned, is considered the authority and accountability of one of these three people.

The Director and the Chief Investment Officer are responsible for direct operational decision making and administration of the policies and guidelines established by the Board. The power to delegate authority, to execute contracts, or sign official documents on behalf of the Board rests solely with the Board, and this authority is exercised by signature resolutions passed by the Board from time to time.

A. DIRECTOR

Pursuant to *Code of Virginia* § 51.1-124.22(A), the Board shall appoint a Director, who shall not be a member of the Board, to serve as the chief administrative officer of the VRS at the pleasure of the Board.

The Board herewith delegates to the Director full responsibility to administer the provisions of Title 51.1 of the *Code of Virginia* under the general direction of the Board and in compliance with the statutes and such policies, rules, guidelines, and procedures as the Board may adopt.

This delegation includes, but is not limited to, the following duties and authority:

1. Determining the accuracy and timeliness of all payments due to VRS;
2. Accounting for and depositing payments made to VRS;
3. Making payment and distributing funds consistent with Title 51.1 of the *Code of Virginia* and other applicable state and federal laws and regulations;
4. Responding to all correspondence regarding rights and benefits of members and employers;
5. Assisting committees of the Board in the discharge of their functions, including providing an orientation program to Board members as soon as practicable after the date of their appointment, in coordination with the CIO and Audit Director;
6. Maintaining VRS records, files, and documents;
7. Developing and maintaining communications and relationships with other state agencies, public retirement systems, and organizations involved with or having an impact on public retirement issues;
8. Representing VRS before the General Assembly and/or any of its committees and agencies on matters relating to the administration of VRS;
9. Serving as liaison with legal, medical, and actuarial professionals and third party administrators;
10. Monitoring the activities and performance of consultants and outside service providers hired by VRS;
11. Developing, approving, and monitoring progress towards completion of divisional business plans and projects;
12. Overseeing the day-to-day administrative operations of VRS;
13. Assigning duties to administrative staff;
14. Determining the appropriate organizational structure and staffing for all functions of VRS other than those performed by the investment and internal audit departments;
15. Determining administrative staff compensation within the parameters of the current compensation plan;
16. Developing, implementing, and supervising plans, policies, standards, programs, and services for applicable personnel;
17. Hiring, retaining, and terminating administrative staff;
18. Providing the Board and the Board chairperson with timely information necessary to discharge their fiduciary duties;
19. Developing, amending, and refining policies for Board approval, including, but not limited to, the following:
 - a) Strategic plan and objectives;
 - b) Service quality standards;

- c) Agency performance evaluation; and
- d) Other administrative policies;
- 20. Issuing final case decisions regarding applications for disability retirement and other matters that have been appealed pursuant to the Administrative Process Act;
- 21. Evaluating and establishing service credits;
- 22. Verifying eligibility for, computing, and paying service retirement allowances;
- 23. Determining whether to discontinue recovery of and waive overpayments, and reporting such determinations to the Benefits and Actuarial Committee when it is outside of normal business operations;
- 24. Making determinations regarding new and/or amended employer coverage;
- 25. Approving and authorizing payment of refund requests;
- 26. Adjudicating questions regarding interpretation and application of relevant law and policy;
- 27. Referring questions to the Board when the determination would be precedent-setting;
- 28. Developing and maintaining the administrative portion of the VRS budget ;
- 29. Monitoring Agency-wide expenditures versus budget;
- 30. Developing and implementing internal controls;
- 31. Coordinating with the Chief Investment Officer in such a manner as to ensure operational efficiency at both the Board and agency levels;
- 32. Absent express Board action otherwise, performing the duties of Secretary to the Board; and
- 33. Performing such additional duties when directed to do so by the Board.

The power to delegate authority to disburse or transfer public funds or assets, execute contracts, or sign official documents on behalf of the Board rests solely with the Board. Therefore, only the Director and any other staff member so authorized by any signature resolutions approved by the Board, and consistent with such signature resolutions, may execute contracts and official documents on behalf of VRS and authorize the disbursement or transfer of public funds or assets of VRS. This authority may not be further delegated by the Director to any other person or persons.

The Director may, however, as he or she deems reasonable, delegate any other of the Director's responsibilities, duties, and authority to members of the administrative staff in order to facilitate the efficient functioning of VRS.

B. CHIEF INVESTMENT OFFICER

Pursuant to *Code of Virginia* § 51.1-124.24(A), the Board shall appoint a Chief Investment Officer ("CIO"), who shall not be a member of the Board, to direct, manage and administer the investment department at the pleasure of the Board.

The Board herewith delegates to the CIO full responsibility to devise and approve investment strategies that are intended to move the defined benefit and defined

contribution plans investment programs towards their broad objectives and goals. As such, the CIO should be free to devise any strategy that is within the policies and guidelines as the Board may adopt.

This delegation includes, but is not limited to, the following duties and authority:

1. Planning, organizing and directing the investment work of VRS;
2. Implementing investment policies and strategies established by the Board;
3. Determining asset allocation within the guidelines established by the Board;
4. Supervising, evaluating, and monitoring the investment portfolio and associated investment activities;
5. Hiring and/or terminating consultants;
6. Hiring and/or terminating investment managers;
7. Developing and maintaining the investment department portion of the VRS budget;
8. Developing and implementing internal controls;
9. Implementing investment-related regulatory requirements;
10. Providing the Board and the Board Chairperson with timely information necessary to discharge their fiduciary duties;
11. Representing VRS before the General Assembly and/or any of its committees and agencies on investment matters;
12. Determining the appropriate organizational structure and staffing for the investment functions of VRS;
13. Determining investment staff compensation within the parameters of the current compensation plan;
14. Developing, implementing, and supervising plans, policies, standards, programs, and services for investment personnel;
15. Hiring, retaining, and terminating investment staff;
16. Overseeing the day-to-day investment operations;
17. Responding to applicable correspondence regarding investment matters;
18. Assisting committees of the Board in the discharge of their functions, including providing an orientation program to Board members as soon as practicable after the date of their appointment, in coordination with the Director and Audit Director;
19. Monitoring activities and performance of internal and external investment managers;
20. Recommending to the Board the appointment, replacement, and termination of the custodian bank;
21. Maintaining necessary systems and technology for investment management and support of all investment functions, in compliance with applicable Virginia Information Technologies Agency (VITA) security standards;
22. Developing, amending, and refining policies for Board approval, including, but not limited to, the following:
 - a) VRS Defined Benefit Plan Investment Policy Statement;

- b) VRS Defined Benefit Plan Investment Belief Statements
 - c) VRS Investment Policy Statement For An Unbundled Defined Contribution Plan Structure;
 - d) VRS Investment Policy Statement For A Bundled Defined Contribution Plan Structure;
 - e) VRS Defined Contribution Plans Investment Belief Statements; and
 - f) Other applicable investment policies;
23. Monitoring compliance with and continued appropriateness of the defined benefit and the defined contribution plans fund policies and guidelines;
24. Coordinating with the Director in such a manner as to ensure operational efficiency at both the Board and agency levels; and
25. Performing such additional duties when directed to do so by the Board.

The power to delegate authority to disburse or transfer public funds or assets, execute contracts, or sign official documents on behalf of the Board rests solely with the Board. Therefore, only the CIO and any other staff member so authorized by any signature resolutions approved by the Board, and consistent with such signature resolutions, may execute contracts and official documents on behalf of VRS. This authority may not be further delegated by the CIO to any other person or persons. The CIO may, however, as he or she deems reasonable, delegate any other of the CIO's responsibilities, duties, and authority to members of the investment staff in order to facilitate the efficient functioning of the investment department of VRS. Notwithstanding the foregoing, an authorized entity may execute necessary documents on behalf of VRS as may be required by contract or agreement.

C. AUDIT DIRECTOR

The Board shall appoint an Audit Director, who reports directly to the Board through the Audit and Compliance Committee, to serve at the pleasure of the Board.

The Board herewith delegates to the Audit Director full responsibility to provide objective analyses, appraisals, recommendations, and pertinent comments concerning the implementation of and adherence to established policies and procedures throughout VRS.

This delegation includes, but is not limited to, the following duties and authority:

1. Reviewing and appraising the soundness, adequacy and applications of accounting, financial, and other operating controls, and promoting effective control at a reasonable cost;
2. Ascertaining the extent of compliance with established policies, plans, and procedures;
3. Ascertaining the extent to which assets are accounted for and safeguarded from losses of all kinds;
4. Ascertaining the reliability of financial data developed within the organization;

5. Recommending operating improvements;
6. Developing a comprehensive long-range audit plan and implementing the plan after review and approval by the Audit and Compliance Committee and approval by the Board;
7. Approving audit scopes and objectives; audit procedures; sampling plans; and, the extent of Information System audit coverage;
8. Supervising examinations of VRS operations and other special projects;
9. Ensuring all audit procedures are performed and are documented in accordance with departmental policies and procedures;
10. Revising the long-range and annual audit plans, as necessary, to accommodate changing needs and unexpected events;
11. Reporting to the Audit and Compliance Committee on a regular basis and, when necessary, reporting directly to the Board;
12. Assisting committees of the Board in the discharge of their functions, including providing an orientation program to Board members as soon as practicable after the date of their appointment, in coordination with the Director and CIO;
13. Monitoring implementation of audit recommendations;
14. Determining the appropriate organizational structure and staffing for the internal audit department;
15. Hiring, retaining, and terminating a professional and proficient audit staff;
16. Determining Internal Audit staff compensation within the parameters of the current compensation plan.
17. Establishing an Internal Audit Department Charter; and
18. Performing such additional duties when directed to do so by the Board.

The Audit Director has sole authority to determine the scope of internal audit activities, and shall not be restricted by the Director or the CIO.

The Audit Director shall have unrestricted access to all VRS activities, records, properties, and personnel pertinent to each area under review. Special arrangements shall be made for the examination of records that are confidential in nature.

The Audit Director shall have direct access to the Director and to the CIO in any instance where the Audit Director believes such access is needed to fulfill the stated objectives of the Department.

The Audit Director may, as he or she deems reasonable, delegate any of the Audit Director's responsibilities, duties, and authority to members of the internal audit staff in order to facilitate the efficient functioning of the internal audit department.

VI. COMMITTEES

A. ADVISORY COMMITTEES

Pursuant to *Code of Virginia* § 51.1-124.26, the Board shall appoint an Investment Advisory Committee to provide the Board with sophisticated, objective, and prudent investment advice to serve at the pleasure of the Board.

In addition, the Board may appoint such advisory committees as it deems necessary to further assist it in fulfilling its fiduciary duty as trustee of the VRS funds.

The Board shall also set forth the purpose and authority of the advisory committee.

The recommendations of an advisory committee are not binding upon the Board.

Each advisory committee may include no more than two (2) Board members. No individual Board member may serve on more than one advisory committee. Other than such Board members, no elected or appointed official may serve on any such advisory committees.

Appointment to an advisory committee shall require a two-thirds vote of the Board. Advisory committee members serve at the pleasure of the Board and may be removed by a majority vote of the Board.

The Board of Trustees Code of Ethics and Conduct shall also apply to all advisory committee members, who shall sign an affirmation pledging to uphold both the letter and the spirit of that Code as soon as practicable after the date of their appointment to the advisory committee, and at least annually thereafter.

Once appointed by the Board, an advisory committee shall develop a committee charter subject to approval and adoption by the Board. Each advisory committee charter shall include a statement of the purpose and authority for which the committee was appointed, a description of the committee's duties and responsibilities, and an overview of the composition and operating procedures of the committee.

The Board has established the following advisory committees:

1. INVESTMENT ADVISORY COMMITTEE (REQUIRED BY LAW)

The purpose of the Investment Advisory Committee is to provide the Board with sophisticated, objective, and prudent investment advice. It shall consist of seven to nine members.

The Investment Advisory Committee shall, except for the defined contribution plans investments:

- a) Review, evaluate, and monitor investments and investment opportunities;

- b) Make appropriate recommendations to the Board about such investments and investment opportunities; and
- c) Make recommendations to the Board about overall asset allocation.

2. DEFINED CONTRIBUTION PLANS ADVISORY COMMITTEE

The purpose of the Defined Contribution Plans Advisory Committee (DCPAC) is to review matters relating to or affecting plan administration, plan design and investments of the various defined contribution plans established pursuant to the *Code of Virginia* and to make recommendations to the Board regarding those matters.

In addition to the duties and responsibilities outlined in its charter, the DCPAC shall assist the Board with its statutory responsibilities to review and oversee the policies and procedures constituting the process by which the Board reviews and determines whether to approve requests by institutions of higher education that seek to withdraw from participation in the Optional Retirement Plan for Employees of Institutions of Higher Education.

B. STANDING COMMITTEES

The Board may establish such standing committees as it determines would be necessary or helpful in fulfilling its responsibilities.

The purpose and authority of a standing committee must be carefully set forth to avoid conflict with authority delegated to the Director, the CIO, and/or the Audit Director.

Once created, a standing committee shall remain in existence until such time as the Board takes the necessary action to dissolve it.

Unless otherwise specified, all standing committees established by the Board are subject to the following principles and guidelines:

1. Standing committees are to focus their efforts on matters of material significance to the VRS Board, and refrain from any involvement in operational details or decision-making that are the responsibility of the Director, the CIO, and/or the Audit Director.
2. Standing committees may assist the Board by suggesting policy alternatives for Board consideration.
3. A standing committee does not speak or act for the Board, unless the Board specifically delegates such authority to it for a specific and time-limited purpose.
4. Each standing committee shall notify all Board members of the time and place of all committee meetings. Board members may choose to attend any committee meeting, regardless of whether or not they are members of the committee. Any

member of the VRS Board who is not a member of the standing committee but is present at a meeting of that committee may serve as an alternate to an absent member of the committee for purposes of constituting a quorum, and any such participation shall not be considered voting by proxy. Moreover, any VRS Board member who is not a member of the standing committee but is present at a meeting of that committee shall have all the rights and privileges afforded to a member of the committee while present at such meeting, including voting and being counted toward a quorum, and any such participation shall not be considered voting by proxy.

Once established by the Board, a standing committee shall develop a committee charter subject to approval and adoption by the Board. Each committee charter shall include a statement of the purpose and authority for which the committee was established, a description of the committee's duties and responsibilities, and an overview of the composition and operating procedures of the committee.

The Board has established the following standing committees:

1. ADMINISTRATION, ~~FINANCE AND TALENT MANAGEMENT AND PERSONNEL~~ COMMITTEE

The purpose of the Administration, ~~Finance and Talent Management and Personnel~~ Committee is to review matters relating to or affecting administrative functions, personnel plans, the budget, and finance, and to make recommendations to the full Board regarding those matters.

2. AUDIT AND COMPLIANCE COMMITTEE

The purpose of the Audit and Compliance Committee is to review matters relating to or affecting internal and external audit, including, but not limited to, VRS' financial reporting process, systems of internal control, auditing procedures and process, and process for monitoring compliance with laws, regulations and the Code of Conduct; and to submit reports or make recommendations to the full Board regarding those matters.

3. BENEFITS AND ACTUARIAL COMMITTEE

The purpose of the Benefits and Actuarial Committee is to review matters relating to or affecting benefits, benefit administration, and actuarial soundness of all plans administered by VRS except for the defined contribution plans, and to make recommendations to the full Board regarding those matters.

4. INVESTMENT POLICY COMMITTEE

The purpose of the Investment Policy Committee is to facilitate the determination of appropriate defined benefit plan investment policies, setting guidelines under which those policies will be carried out, and to make appropriate recommendations to the full Board regarding those policies and guidelines. It is the intent of the Board that all substantive concerns, discussions, and recommendations regarding VRS investment policy be directed to the Investment Policy Committee for vetting and reporting back to the Board for action, if any.

C. SPECIAL COMMITTEES

The Board may establish a special committee, as needed, to carry out a specified task. Upon completion of the task for which it was established, and presentation of its final report to the Board, a special committee shall cease to exist. A special committee may not be appointed to perform a task that falls within the assigned function of any existing standing or advisory committee.

VII. RELATIONSHIP WITH THE PUBLIC

Because it is a public body responsible for the management of public funds, the VRS Board has the responsibility to conduct its business in an environment that is open to public scrutiny. In doing so, the VRS Board shall operate in full compliance with both the letter and the spirit of the Virginia Freedom of Information Act (FOIA) and the State and Local Government Conflict of Interests Act (COIA).

A. PRINCIPLES

1. VRS shall maintain open communication with the public, the employers, and members it serves, and the news media.
2. VRS shall make public information available in as efficient a manner as possible, while protecting the confidentiality of the members, retirees, beneficiaries, and employers it serves.
3. The public shall be granted access to all meetings and to all records of meetings of the Board and Board committees except for such meetings as are closed pursuant to and in accordance with FOIA.

B. COMMUNICATION WITH THE MEDIA

1. The Chairperson of the Board is authorized to act as spokesperson for the Board and for VRS.
2. The Chairperson may delegate all or a part of this authority as he or she deems appropriate, subject to approval by the Board. The Board herewith approves the following delegation:

- a) The Director or his or her designee is authorized to act as spokesperson regarding administrative and operational matters.
- b) The CIO or his or her designee is authorized to act as spokesperson regarding investment matters.
3. The Chairperson shall, to the extent possible, review all official press releases regarding Board policy, activities, or other matters prior to publication.

VIII. OPINIONS OF THE ATTORNEY GENERAL

Pursuant to *Code of Virginia* § 2.2-505(A), requests from VRS for written advice in the form of official advisory opinions from the Attorney General must be made in writing by the Board Chairperson or by the Director. Before requesting an official advisory opinion of the Attorney General, the Director shall review the request with and obtain the prior approval of the Board Chairperson and, where feasible, the Board of Trustees.

IX. AMENDMENT OF GOVERNANCE POLICY

The VRS Board of Trustees Governance Policy and committee charters, in whole or in part, may be altered, amended, modified, and/or rescinded, and new policies or provisions may be adopted in lieu thereof, by a two-thirds vote of the Board, provided that a copy of the proposed amendment is submitted in writing at the preceding regular meeting,

In the case of urgent and/or extraordinary circumstances requiring the immediate action of the Board, the Board may amend a policy or provision at the same meeting at which the proposed amendment is introduced, provided that such action is by unanimous consent. Furthermore, any such amendment must be submitted for reconsideration at the next Board meeting and, only if it then is reaffirmed by a two-thirds vote, shall such amendment permanently become a part of the Governance Policy or committee charter.

Notwithstanding the foregoing, the Administration, Finance and Talent Management and Personnel Committee shall periodically review the Governance Policy and committee charters. The Committee shall report its findings and recommended changes to the Board.

X. VALIDITY OF GOVERNANCE POLICY

In the event any of the provisions set forth in the Governance Policy shall be deemed to be invalid as a result of any conflict with a provision of the *Code of Virginia* or the Appropriation Act, such conflict shall not invalidate the entirety of the Governance

Policy, but the remaining provisions of the Governance Policy shall continue in full force and effect.

In the event any of the provisions set forth in the Governance Policy are found to be in conflict with any provision(s) of the committee charters adopted hereunder, the Governance Policy shall supersede and take precedence over any conflicting provisions of a committee charter.

COMMITTEE CHARTER FOR THE
ADMINISTRATION ~~AND PERSONNEL~~, FINANCE AND TALENT MANAGEMENT
COMMITTEE

PURPOSE

The purpose of the Administration ~~and Personnel~~, Finance and Talent Management Committee (Committee) is to review matters relating to or affecting administrative functions, personnel plans, the budget, and finance, and to make recommendations to the full Board regarding those matters.

AUTHORITY

The Committee is authorized to request, gather, and consider whatever information it deems relevant to the matters brought before it, and to report its findings or recommendations on those matters to the Board. The Committee is not empowered to take any further or independent action unless such action is specifically authorized or directed by the Board.

DUTIES AND RESPONSIBILITIES

To fulfill the purpose for which it was established, the Committee shall perform the following:

1. Review administrative issues identified by the Board, the Director, or the Chief Investment Officer and make recommendations to the Board regarding such issues.
2. Review VRS budget proposals and make related recommendations to the Board.
3. Regularly review the status of the budget in relation to actual expenditures and identify for the Board any areas in need of attention.
4. Review and make recommendations to the Board regarding VRS's mission and strategic plan and objectives as needed.
5. Review and make recommendations to the Board regarding requests for carry-forward funds, additional revenue appropriations, transfers of appropriations from the second year to the first year of a biennium, and transfers between programs in timely fashion so as to enable the Board to act on these issues before they are forwarded to the Department of Planning and Budget.

6. Review and make recommendations to the Board regarding non-budgeted purchasing requests that exceed the Director's authority as set forth in the VRS purchasing guidelines.
7. Review and make recommendations to the Board regarding the establishment of or changes to personnel and compensation policies and plans.
8. Review and make recommendations to the Board regarding the annual Agency Performance Outcomes and related Agency Operating Standards.
9. Review and make recommendations to the Board regarding the performance of the Director and the Chief Investment Officer.
10. Work with the Chief Investment Officer and the chairperson of the Investment Advisory Committee to identify potential new members for the Investment Advisory Committee and to determine which candidate(s) will be recommended to the Board for appointment to the Investment Advisory Committee.
11. Review each member of the Investment Advisory Committee who is eligible for reappointment and determine whether to recommend that the member be reappointed by the Board.
12. Investigate any allegations or complaints regarding violation(s) of the Board's Code of Ethics and Standards of Conduct and report findings to the Board, together with recommendations regarding action to be taken.
13. Periodically, as needed, review the Board's Governance Policy and committee charters, and recommend such changes as are deemed appropriate.
14. Perform such other duties when directed to do so by the Board.

COMPOSITION

The Committee is composed of at least three (3) and no more than five (5) Board members: The chairperson of the Board, the vice-chairperson of the Board, and additional Board members appointed by the chairperson of the Board, subject to approval by the Board.

The terms of the chairperson and vice-chairperson of the Committee run concurrently with their terms as chairperson and vice-chairperson of the Board. The other Committee members are appointed for a two-year term, and may be reappointed for additional two-year terms.

OFFICERS

Chairperson

The VRS Board chairperson shall serve as the chairperson of the Committee.

The chairperson is charged with:

1. Facilitating the operation of the Committee meetings;
2. Reviewing proposed agendas for Committee meetings;
3. Presiding over meetings of the Committee;
4. Reporting to the Board on the matters considered by the Committee, and the recommendations of the Committee; and
5. Performing such additional duties as are required to facilitate the Committee's fulfillment of its responsibilities.

Vice-Chairperson

The VRS Board vice-chairperson shall serve as the vice-chairperson of the Committee.

In the event of the absence or incapacity of the Committee chairperson, the vice-chairperson shall preside at meetings of the Committee and shall fulfill such other duties and responsibilities of the chairperson as may be necessary.

Secretary

The Director, or the Director's designee, shall act as secretary to the Committee. The Director shall continue to serve as secretary until such time as he or she is unable or unwilling to continue to do so, or until such time as the Committee appoints another secretary.

The secretary has the following duties:

1. Help the chairperson develop the agenda for Committee meetings;
2. Notify Committee members of meetings;
3. Coordinate and distribute information to Committee members;
4. Act as liaison between the Committee and VRS staff;
5. Coordinate matters on the agenda and presentations for the Committee; and
6. Maintain the minutes and records of all Committee meetings.

CONDUCT OF BUSINESS

1. The rules contained in the current edition of *Robert's Rules of Order Newly Revised* shall govern all Committee meetings insofar as they are applicable and not inconsistent with any of the policies adopted by the Board, including this

- charter, with particular attention to the rules provided for conduct of business in committees.
2. Unless otherwise specified by the Board, voting by proxy is not allowed.
 3. A majority of the appointed members of the Committee shall constitute a quorum at meetings of the Committee. For the purposes of determining the presence of a quorum, an abstention or disqualification shall be considered an absence. However, any member of the Board who is not a member of the Committee but is present at a Committee meeting may serve as an alternate to an absent member of the Committee for purposes of constituting a quorum, and any such participation shall not be considered voting by proxy. Moreover, any Board member who is not a member of the Committee but is present at a Committee meeting shall have all the rights and privileges afforded to a Committee member while present at such meeting, including voting and being counted toward a quorum, and any such participation shall not be considered voting by proxy. The presence of any alternate at a Committee meeting and the participation by any Board member who is not a member of the Committee shall be recorded in the minutes of the Committee meeting.
 4. Except as otherwise specified herein, approval of an action or decision shall be by a majority of those Committee members present and voting at a Committee meeting.
 5. The Committee chairperson will seek at all times to develop a consensus of opinion among Committee members in order to be able to present clear and concise recommendations to the Board. In the event that a consensus is not obtainable, the Committee chairperson will present the range of opinions and their rationale to the Board.
 6. The Committee chairperson will report to the Board on the content and results of each Committee meeting. The chairperson or vice-chairperson will sign all meeting minutes, as applicable.
 7. The Committee will generally meet at least twice per year and more often if necessary to meet the objectives listed in this charter.

CHANGES IN THE CHARTER

The Committee may, from time to time, deem it necessary to alter, amend, modify, or rescind all or a part of this charter. Such revisions, once approved by a majority vote of the Committee, shall be submitted to the Board for final approval. If approved by a two-thirds vote of the Board, such revisions shall be incorporated into and made a part of this charter.

COMMITTEE CHARTER

AUDIT AND COMPLIANCE COMMITTEE

PURPOSE

The purpose of the Audit and Compliance Committee (Committee) is to review matters relating to or affecting internal and external audit, including, but not limited to, VRS' financial reporting process, systems of internal control, auditing procedures and process, and process for monitoring compliance with laws, regulations, and the Code of Conduct, and to submit reports or make recommendations to the full Board regarding those matters.

AUTHORITY

The Committee is authorized to request, gather, and consider whatever information it deems relevant to the matters brought before it, and to report its findings or recommendations on those matters to the Board. The Committee is not empowered to take any further or independent action unless such action is specifically authorized or directed by the Board.

DUTIES AND RESPONSIBILITIES

To fulfill the purpose for which it was established, the Committee shall perform the following:

1. Monitor internal and external audit functions and report to the Board following each Committee meeting on the reports and matters presented to or considered by the Committee.
2. Review the effectiveness of internal and external auditing methods including coordination of efforts. (Note: While members of the Committee are expected to become sufficiently familiar with the accounting practices of VRS so that they are able to do this, they are not expected to become accounting experts. They may, as necessary and in good faith, rely upon the professional accounting expertise of the Audit Director and of the external auditors.)

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3. Review and make recommendations to the Board regarding both the annual and long-range audit plans developed by the Audit Director and provide feedback in response thereto.
4. Monitor progress of work on the annual work plan through review of the Audit Director's semi-annual progress reports, and reports of any revisions made to the work plan.
5. Receive and review reports of the Audit Director and report on same to the Board with recommendations, if any, for necessary action.
6. Make appropriate inquiries of management and the Audit Director to determine whether there are inappropriate scope or resource limitations.
7. Consider the effectiveness of the VRS' internal control system, including information technology security and control.
8. Receive and review reports from the Audit Director regarding the effectiveness and sufficiency of the internal audit department including the appropriateness of the department's funding and organizational structure. Determine whether requests by the Audit Director for changes in the staffing of that department should be submitted to the Administration ~~and Personnel~~, Finance and Talent Management Committee.
9. Review annual report of the Audit Recommendation Follow-Up System and monitor status of management's progress in response to audit recommendations.
10. Review and approve changes to the Internal Audit Department Charter.
11. Ensure that an independent, full-scope quality assurance review of the internal audit department is performed at least once every five years, review the report of such review, recommend to the Board what, if any, corrective actions are necessary, and monitor the implementation of such corrective actions as are mandated by the Board.
12. Ensure the internal audit department has unrestricted access to all VRS activities, records, properties, and personnel applicable to the area under review. The Board has endorsed this right and has resolved that the scope of internal audit activities not be restricted by actions of management.
13. Provide the opportunity for meetings between the Committee and the Audit Director whenever the Committee or Audit Director finds such to be necessary.
14. Review and make recommendations to the Board regarding the performance of the Audit Director.
15. In cases where the Director or the Chief Investment Officer disagrees with an audit recommendation, the matter shall be presented to the Committee, which shall make an initial determination as to whether the audit recommendation requires management action or should be deleted and will present that determination to the Board for a final decision.
16. Receive and review reports from management regarding the process for communicating the VRS Code of Conduct to agency personnel, and for monitoring compliance therewith. This includes the processes and compliance

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- mechanisms in place for both administrative and investment department personnel.
17. Conduct entrance and exit conferences with the Auditor of Public Accounts, and report to the Board on the scope and substance of those meetings.
 18. As necessary, request permission from the full Board to retain independent counsel (through the Office of the Attorney General), accountants, or others to advise the Committee.
 19. Receive and review reports of the Auditor of Public Accounts and any other external auditors, and report on same to the Board with recommendations, if any, for necessary action. Review the annual financial statements and other sections of the annual report, and consider whether they are complete and consistent with information known to Committee members, and to the best of their knowledge reflect appropriate accounting principles. Have management and the external auditors review all matters required to be communicated to the Committee under generally accepted government auditing standards. Allow for meetings with the external auditors to discuss any matters that the Committee or auditors believe should be discussed.
 20. Periodically consider the desirability of an audit by an independent accounting firm and, if such audit is deemed necessary, present such a recommendation to the Board together with a list of candidate firms.
 21. Perform such other duties when directed to do so by the Board.

COMPOSITION

The Committee is composed of at least three (3) Board members appointed by the chairperson of the Board, subject to approval by the Board.

Each member is appointed for a two-year term, and may be reappointed for additional two-year terms.

OFFICERS

Chairperson

The VRS Board chairperson shall appoint the chairperson of the Committee, subject to approval by the Board.

The Committee chairperson is appointed for a two-year term, and may be reappointed for additional two-year terms.

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The chairperson is charged with:

1. Facilitating the operation of the Committee meetings;
2. Reviewing proposed agendas for Committee meetings;
3. Presiding over meetings of the Committee;
4. Reporting to the Board on the matters considered by the Committee, and the recommendations of the Committee; and
5. Performing such additional duties as are required to facilitate the Committee's fulfillment of its responsibilities.

Vice-Chairperson

The Committee shall elect its vice-chairperson at the first meeting following the appointment or reappointment of a chairperson, or at the first meeting following such time as a sitting vice-chairperson becomes unable or unwilling to complete his or her term.

The term of the vice-chairperson shall commence upon election and shall terminate at the first meeting of the Committee following the appointment or reappointment of a Committee chairperson.

In the event of the absence or incapacity of the Committee chairperson, the vice-chairperson shall preside at meetings of the Committee and shall fulfill such other duties and responsibilities of the chairperson as may be necessary.

Secretary

The Audit Director, or the Audit Director's designee, shall act as secretary to the Committee. The Audit Director shall continue to serve as secretary until such time as he or she is unable or unwilling to continue to do so, or until such time as the Committee appoints another secretary.

The secretary has the following duties:

1. Help the chairperson develop the agenda for Committee meetings;
2. Notify Committee members of meetings;
3. Coordinate and distribute information to Committee members;
4. Act as liaison between the Committee and VRS staff;
5. Coordinate matters on the agenda and presentations for the Committee; and
6. Maintain the minutes and records of all Committee meetings.

CONDUCT OF BUSINESS

1. The rules contained in the current edition of *Robert's Rules of Order Newly Revised* shall govern all Committee meetings insofar as they are applicable and not inconsistent with any of the policies adopted by the Board, including this charter, with particular attention to the rules provided for conduct of business in committees.
2. Unless otherwise specified by the Board, voting by proxy is not allowed.
3. A majority of the members of the Committee shall constitute a quorum at meetings of the Committee. For the purposes of determining the presence of a quorum, an abstention or disqualification shall be considered an absence. However, any member of the Board who is not a member of the Committee but is present at a Committee meeting may serve as an alternate to an absent member of the Committee for purposes of constituting a quorum, and any such participation shall not be considered voting by proxy. Moreover, any Board member who is not a member of the Committee but is present at a Committee meeting shall have all the rights and privileges afforded to a Committee member while present at such meeting, including voting and being counted toward a quorum, and any such participation shall not be considered voting by proxy. The presence of any alternate at a Committee meeting and the participation by any Board member who is not a member of the Committee shall be recorded in the minutes of the Committee meeting.
4. Except as otherwise specified herein, approval of an action or decision shall be by a majority of those Committee members present and voting at a Committee meeting.
5. The Committee chairperson will seek at all times to develop a consensus of opinion among Committee members in order to be able to present clear and concise recommendations to the Board. In the event that a consensus is not obtainable, the Committee chairperson will present the range of opinions and their rationale to the Board.
6. The Committee chairperson will report to the Board on the content and results of each Committee meeting. The chairperson or vice-chairperson will sign all meeting minutes, as applicable.
7. The Committee shall meet at least four times per year.

CHANGES IN THE CHARTER

The Committee may, from time to time, deem it necessary to alter, amend, modify, or rescind all or a part of this charter. Such revisions, once approved by a majority vote of the Committee, shall be submitted to the Board for final approval. If

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approved by a two-thirds vote of the Board, such revisions shall be incorporated into and made a part of this charter.

BOARD OF TRUSTEES CODE OF ETHICS AND CONDUCT

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I. PURPOSE

The VRS Board is the trustee of the funds of the plans that it administers and, as such, is obligated to discharge all of its duties solely in the interest of the VRS members, beneficiaries, and participants of all said plans.

In addition, the Board is charged with oversight responsibility for several other plans and, as to these, the Board has fiduciary obligations.

In furtherance of these duties and obligations, the Board of Trustees hereby adopts this Code of Ethics and Conduct, which is established to define the ethical and behavioral guidelines within which all Board of Trustees members and non-Board members of committees of the Board (hereafter referred to as Board members) are expected to conduct themselves while serving as Board members.

Adherence to this Code will allow the Trustees to pursue the mandates of their Governance Policy, foster harmonious relations between Board members, and facilitate mutual respect and public confidence.

II. FIDUCIARY DUTIES

By virtue of the authority given to the VRS Board to exercise control over the disposition of the assets and funds described in Section II of the Board of Trustees Governance Policy, each Board member is a fiduciary and, as such, owes a special duty to VRS and to VRS members, beneficiaries, and participants.¹

As a fiduciary, each Board member shall adhere to the duties of loyalty, prudence and following plan documents. In doing so, each Board member shall:

- A. Discharge his or her duties solely in the interest of the members, beneficiaries and participants of the VRS systems and plans for the exclusive purpose of providing benefits to VRS members, beneficiaries and participants.

¹ Members of the Investment Advisory Committee (IAC) and Defined Contribution Plans Advisory Committee (DCPAC) are not members of the Board of Trustees and therefore are not considered fiduciaries of the Virginia Retirement System. Unless otherwise stated, references to fiduciary duties do not apply to IAC and DCPAC members.

- B. Be loyal to VRS members, beneficiaries and participants, and not to the source of his or her appointment.
- C. Treat all VRS members, beneficiaries and participants equally and fairly. A Board member's loyalty is to VRS members, beneficiaries and participants as a group, and not to individuals or groups of individuals.
- D. Discharge his or her duties with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims.
- E. Be informed so as to be familiar with applicable state and federal laws and other matters relating to his or her duties as a Board member.
- F. Strive to understand and work towards VRS objectives.
- G. Prepare for and attend all Board and assigned committee meetings, and shall strive to maintain a continuing awareness of the actions and activities of the Board and its committees.
- H. Take advantage of educational opportunities so as to be properly informed.
- I. Seek out expert assistance in matters where he or she lacks familiarity.
- J. In conjunction with all Board members, engage in performing ongoing oversight of those employed directly by the Board (i.e., the Director, the Chief Investment Officer and the Audit Director).
- K. Review and follow all plan documents and related laws.

III. CODE OF ETHICS

In adhering to the Board's commitment to upholding the highest standards of integrity, ethical principles and professional conduct, each Board member shall:

- A. Conduct himself or herself with integrity, competence and dignity, including when dealing with fellow Board members, the Director, the Chief Investment Officer, the Audit

Director, all VRS advisory committee members, VRS members, business partners, VRS employees, other stakeholders and the public.

- B. Maintain high ethical and moral character, both professionally and personally, such that his or her conduct shall not reflect negatively upon the Board of Trustees or VRS.
- C. Use proper care and exercise independent professional judgment.
- D. Maintain the confidentiality of information owned, obtained or developed by VRS, including information provided in closed meetings.
- E. Adhere to the Commonwealth of Virginia's State and Local Government Conflict of Interests Act ([Code of Virginia § 2.2-3100 et seq.](#)).
- F. Take affirmative steps to avoid breaches of duty (through negligence or intentional action or omission), unauthorized communication with individuals seeking to influence the Board and unauthorized communications with individuals who may receive personal gains as a result of Board actions.
- G. Recognize that all VRS business transactions must be based on integrity, competence and financial merit and benefit to VRS members, beneficiaries and participants, and not on personal relationships.
- H. Disclose in writing to the Board chair and secretary any outside business or financial interest that could influence the impartial discharge of his or her official responsibilities and duties.

IV. STANDARDS OF CONDUCT

In furtherance of the Board's commitment to seeing that VRS accomplishes its mission and fulfills its vision, each Board member shall:

- A. Refrain from engaging in conduct that would discredit or compromise the integrity of the Board of Trustees and VRS.
- B. Avoid any conflict of interest with respect to his or her fiduciary responsibilities, including:

1. Not using his or her position to obtain employment at VRS for themselves, family members or close associates.
 2. Not seeking, accepting or being offered a position of employment at VRS until five years after the termination of his or her service on the Board or any advisory committee.
 3. Abstaining from a vote on any issue in which he or she has an unavoidable conflict of interest, as referenced in Section III (H). He or she may participate in the discussion concerning the issue unless a majority of the Board votes otherwise.
- C. In conjunction with all Board members, provide oversight of the Director, Chief Investment Officer and Audit Director, who are delegated responsibility to administer the day-to-day operations of the organization as outlined in the Board's Governance Policy. While providing oversight, each Board member shall not:
1. Give orders or directions to any employee of VRS, except to the Director, Chief Investment Officer and Audit Director.
 2. Become involved in operational management.
- D. Discuss in open Board meetings all substantive matters. Board members who contact VRS staff on substantive matters are encouraged to communicate the same to all other Board members.
- E. Refer all proposals or other communications regarding potential or existing investments or other contracts or services directly to the Chief Investment Officer or the Director, as appropriate.
- F. Take proactive steps to avoid communication or contact with prospective or actual applicants or bidders upon the release of any procurement vehicle for the selection of advisors, managers, consultants, contractors or any other vendor.
- G. File, as a condition to becoming a Board member and as required thereafter, a disclosure statement of personal interests and such other information required in accordance with [§ 2.2-3100 et seq. of the Code of Virginia](#).
- H. Adhere to the responsibilities of a co-fiduciary by not enabling, knowingly participating in or concealing a breach by another Board member. If a Board member is aware of a

breach he or she shall take all reasonable steps to prevent or halt such breach and report it to the Board chair and secretary.

V. GIFTS

In accordance with Commonwealth of Virginia’s State and Local Government Conflict of Interests Act ([Code of Virginia § 2.2-3100 et seq.](#)), each Board member shall avoid the appearance of impropriety regarding the acceptance of gifts. The *Code of Virginia* defines “gifts” as any gratuity, favor, discount, entertainment, hospitality, loan, forbearance or other item having monetary value. It includes services as well as gifts of transportation, local travel, lodging and meals, whether provided in-kind, by purchase of a ticket, payment in advance or reimbursement after the expense has been incurred.

In furtherance of this objective, each Board member shall not:

- A. Accept gifts from any person or entity engaged in business with VRS.
- B. Receive, accept, seek or solicit, directly or indirectly, anything of economic value as a gift, gratuity or favor from a person if it reasonably could be expected that the gift, gratuity or favor would:
 - 1. Influence the vote, action or judgment of the Board member.
 - 2. Be considered as part of a reward for action or inaction.
- C. Accept or receive any gift through an intermediary, if he or she knows, or has reason to know, that the gift originated from a source that would make the gift prohibited under this policy.
- D. Accept a gift if the source of the gift is not identified. If the source of any gift cannot be ascertained, the gift shall be donated to a suitable charitable organization or otherwise discarded.
- E. Accept any complimentary work, analysis or other “favor” offered or performed by a current, prospective or potential vendor of VRS that is intended to benefit personally the involved Board member if such work, analysis or other “favor” is offered to or performed for such Board member because of his or her capacity as a Trustee of the Virginia Retirement System.

- F. Solicit, encourage, or accept entertainment, including but not limited to meals, refreshments or entry fees from a current, prospective or potential vendor of VRS.
- G. Accept cash, cash equivalents or securities of any value.

Board members should direct questions regarding gifts to the Board secretary, who may request or direct the Board member to request clarification from the Virginia Conflict of Interest and Ethics Advisory Council.

VI. SPONSORED TRAVEL

For the purposes of this policy:

“Sponsored travel” shall mean payment of travel and related expenses by a source other than VRS or the person(s) traveling on behalf of VRS.

“Source of funds” shall be the person or entity directly providing the reimbursement to VRS and not others who may pay dues or otherwise provide funding to that person or entity.

A Board member, acting in his or her capacity as such, may accept sponsored travel to give a speech, participate in a panel or seminar, or provide a similar service at a professional or educational conference, convention or seminar when his or her participation is requested due to the experience, expertise or opinions related to the performance of his or her duties for VRS provided that:

- A. The source of the funds is not a person or entity that is in a business relationship with VRS, has ever been in a business relationship with VRS or potentially may enter into a business relationship with VRS.
- B. The speech, seminar, or other forum for which the sponsored travel has been offered will not be publicized, promoted, or represented in any way as being sponsored by a person or entity that is in a business relationship with VRS, has ever been in a business relationship with VRS or potentially may enter into a business relationship with VRS.
- C. The sponsored travel is specifically approved as herein provided.
- D. The Board maintains a public record of all such sponsored travel, as set forth herein.

- E. Approval of sponsored travel shall be sought, obtained and recorded as follows:
1. A written request to accept sponsored travel shall include:
 - a) A description of the event to be attended.
 - b) Identification of the person or entity that has offered to pay the expenses.
 - c) A description of the expenses that will be covered or reimbursed.
 - d) The names of the persons to whom the request has been submitted.
 2. All requests for sponsored travel by Board members, its committee members, the Director, the Chief Investment Officer and the Audit Director shall be approved by the Audit and Compliance Committee. Requests for such approval shall be submitted to the Director who will forward the requests to the Audit and Compliance Committee for approval.
 3. The Audit and Compliance Committee will, to the extent practical, approve or disapprove the request within three (3) business days of having received it.
- F. Records of all sponsored travel shall be maintained as follows:
1. A report of all sponsored travel, including a copy of the original request and an itemization of all expenses paid for, shall be submitted along with all other reports of travel for review by the Audit and Compliance Committee.
 2. The Audit and Compliance Committee shall report to the Board on all sponsored travel, which report shall be maintained in the minutes of the Board.
- G. The Director, Chief Investment Officer and Audit Director may, in his or her discretion and pursuant to the duties and responsibilities delegated to them, adopt this policy for application to travel by VRS staff or otherwise amend the policies and procedures for travel and reimbursement as they pertain to VRS staff.

VII. ALL VRS RELATED TRAVEL

No spouse, family member or other invitee of a Board member traveling on behalf of VRS may accompany the Board member unless the spouse, family member, invitee or Board

member pays for all additional or incremental costs and expenses associated with such attendance.

VIII. GENERAL PROVISIONS

- A. This Code of Ethics and Conduct shall not be construed as excusing any Board member from any other restrictions of state or federal law concerning conflicts of interest and fiduciary duties, nor shall it be construed as superseding such state or federal law.
- B. Any breach of this Code of Ethics and Conduct shall be referred to the Administration ~~and Personnel~~, Finance and Talent Management Committee, which shall investigate, as necessary, and report its findings to the Board together with a recommended course of action.
- C. All Board members will sign an affirmation, annually, pledging to uphold this Code of Ethics and Conduct.

IX. AFFIRMATION

VIRGINIA RETIREMENT SYSTEM BOARD OF TRUSTEES
CODE OF ETHICS AND CONDUCT

I hereby pledge to uphold the Virginia Retirement System Board of Trustees Code of Ethics and Conduct.

Member Name

Board or Advisory Committee

Signature

Date

MEMORANDUM

DATE: 10/18/2022

TO: VRS Board of Trustees
Ronald D. Schmitz, Chief Investment Officer
Andrew H. Junkin, Chief Managing Director

FROM: VRS Governance Team

SUBJECT: Fiscal Year 2022 Corporate Governance Report

This memorandum will serve as the Corporate Governance Report for Fiscal Year 2022. In September 2018, The Board of Trustees adopted a revised Proxy Voting and Securities Litigation Policy (see Exhibit 1). The policy's guiding principle for proxy voting and securities litigation activity is an emphasis on fiduciary responsibility, only taking actions that are in the best interest of the plan's participants and beneficiaries. The policy mandates that a proxy voting provider vote all proxies with allowable exceptions including comingled or mutual funds and certain separate accounts where proxy voting is part of the firm's investment strategy.

Proxy Voting

Institutional Shareholder Services, Inc. (ISS) continues to be the proxy research and implementation provider for VRS. ISS is currently owned by Deutsche Börse AG, a German financial marketplace exchange that offers listing and trading services. In November 2020, Deutsche Börse acquired a majority stake in ISS from private equity firm Genstar Capital. During FY2022, staff reviewed and evaluated the services provided by ISS and determined that these services continue to meet the needs of VRS (see Exhibit 2 for ISS U.S. proxy voting guidelines).

As of June 30, 2022, eight out of fourteen of Public Equity's external traditional mandates used ISS for proxy voting. Including internal mandates, ISS handled the proxies for 60% of Public Equity's market value. Managers who do not use VRS's ISS proxy voting platform are noted in Exhibit 3.

Securities Litigation

Under independent authority granted to VRS in the Appropriation Act to enter into agreements to seek legal advice related to its investments outside the OAG appointment process, VRS appointed the law firms of Bernstein Litowitz Berger & Grossman LLP (Bernstein Litowitz), Cohen Milstein Sellers & Toll PLLC (CohenMilstein), Kessler Topaz Meltzer & Check LLP (Kessler Topaz), and Labaton Sucharow LLP (Labaton) effective December 1, 2017. Each of the agreements have a term of two years, with automatic renewals for up to four additional one-year terms unless terminated by written

notice by either VRS or the law firm. All four firms have been renewed for a one-year term ending November 30, 2022.

The Office of the Attorney General (OAG) recently appointed eight firms to provide domestic securities litigation services to VRS for a period beginning December 1, 2020 and running through November 30, 2022. Bernstein Litowitz, CohenMilstein, Kessler Topaz and Labaton are included in the list of firms appointed by OAG.

The firms work closely with VRS' custodians – Bank of New York Mellon, Goldman Sachs, and State Street Bank & Trust to monitor the VRS investment portfolio to:

- Inform VRS about newly filed securities class actions and whether and to what extent VRS has sustained a loss with respect to the affected securities;
- Inform VRS about settled or adjudicated securities class actions; and
- Provide legal advice and representation about prosecution of securities claims.

VRS has not been the lead plaintiff in any U.S. securities litigation matters other than Escala in 2006 and MF Global in 2012, but VRS continues to participate monetarily in the settlement of U.S. class action litigation by filing proofs of claim, monitoring payments, etc.

Bank of New York Mellon reported that VRS received class action proceeds totaling \$5,830,967 during FY2022 on behalf of the defined benefit plan. These proceeds were related to separate accounts where Bank of New York Mellon serves as the custodian. Investments in traditional equity accounts with other custodial or prime broker relationships received class action proceeds totaling \$55,259 on behalf of the defined benefit program. BlackRock reported as a unit holder of various BlackRock collective trust funds, the VRS defined contribution accounts pro-rata share of class action proceeds totaled \$102,648 during FY2022. In addition, State Street Bank & Trust reported \$105 of recoveries from previously closed VRS defined contribution investment management accounts.

Since the Supreme Court case of *Morrison v. National Australia Bank Ltd.*, 561 U.S. 247 (2010), investors such as VRS have not had the protection of the U.S. securities laws if the securities were purchased on a foreign exchange. Given the new realities of global securities litigation after Morrison, VRS has adapted and continues to adapt to the new and varying challenges of monitoring its portfolio to ensure that non-U.S. opportunities to recover assets based on securities fraud are not lost. For example, with the assistance of outside counsel, VRS takes a conservative approach by participating in cases in select foreign jurisdictions where such participation is similar to the claims filing process in domestic actions. Also, VRS only participates in foreign securities litigation in those jurisdictions that either do not involve a risk that VRS would be liable for expenses if the litigation is unsuccessful (i.e., no “loser pays” rule) or where the litigation funder fully indemnifies VRS for any potential “loser pays” costs. In such jurisdictions, VRS assumes a passive role in its participation in the case after an initial filing of transactional data supporting the VRS claim.

VRS joined 5 non-U.S. cases and received no proceeds from non-U.S. cases during FY2022, and we are participating passively in 19 other non-U.S. cases for which the recovery amounts have not yet been determined.

Investor Organizations

VRS continues to be a non-voting member of the Council of Institutional Investors (CII) and staff continues to view the organization as a cost-effective resource for research on corporate governance issues. CII members consist of representatives from public and private pension plans, foundations, endowments, mutual funds, insurance companies, and international institutional investors with member assets over three trillion dollars. The organization is well respected among regulatory bodies and government leaders. The diversity of its membership affords thought provoking debate on corporate governance issues. Because of the depth of its membership, quality of data, and timely dissemination of information, staff still believes that participation in other corporate governance organizations is not necessary at this time.

**BOARD OF TRUSTEES’
PROXY VOTING AND LITIGATION POLICY**

GUIDING PRINCIPLE

The guiding principle for the Virginia Retirement System’s (“VRS”) proxy voting and litigation activity is fiduciary responsibility, only taking actions that are in the best interest of the plan's participants and beneficiaries.

I. POLICY STATEMENT

A. PROXY VOTING

It is the policy of VRS to review all proxy issues carefully and to vote them in the best interest of the participants and beneficiaries of the fund. The Board should review a report on VRS proxy voting from time to time, which includes an evaluation of any outside Proxy Voting Service Provider.

B. VRS AS LONG-TERM INVESTOR

VRS should act like an owner of companies in which it invests by encouraging long-term value creation. However, the costs of becoming an active investor must be considered. VRS should always seek cost-effective means for acting as an owner. VRS can share the costs of any shareholder activism by joining organizations made up of other similar institutional investors who are also concerned about creating and improving economic value for shareholders.

C. LITIGATION

Other than cases brought under the Virginia Administrative Process Act,¹ the most common type of litigation that affects VRS directly is securities litigation class actions for investments in which VRS has incurred a loss. From time to time other types of litigation will arise, including cases where VRS is a defendant and cases brought under the Virginia Fraud Against Taxpayers Act (§ 8.01-216.1, et seq., of the *Code of Virginia*). While VRS acknowledges that there are situations that may give rise to a fiduciary duty to pursue legal action on its own to recover on a claim, VRS also places significant weight on the fact that

¹ Article V, section A (2) of the Board Governance Policy delegates authority to the Director to issue final case decisions regarding applications for disability retirement and other matters that have been appealed pursuant to the Administrative Process Act.

most (if not all) of these domestic claims will be prosecuted by class action attorneys on behalf of a multitude of institutional investors, whether or not VRS undertakes an active role. Consequently, the default position for VRS in connection with domestic securities litigation is to simply file claims in connection with the settlement of securities litigation class action matters based on VRS holdings in the affected securities.

VRS will consider an active role in securities litigation typically in those cases where (i) VRS has experienced a significant loss related to illegal conduct, fraud, or willful wrongdoing, (ii) active involvement could provide added value to VRS (e.g., in the form of a higher recovery than if VRS was not involved), either in the specific case or on a longer-term, portfolio-wide basis, or (iii) in the case of foreign litigation where active involvement is the only avenue for recovery. For the purposes of this policy and as a general guideline, a loss is significant when it exceeds three basis points of the total fund value (“Loss Threshold”). The decision to take an active role in any securities litigation requires a balancing of the costs and benefits involved.

In considering whether to take an active role in securities litigation, VRS should also assess the long-term consequences of litigation as well as the impact of litigation on staff productivity. VRS will appoint outside counsel with expertise in securities litigation to assist in determining whether fraud or willful wrongdoing has occurred in connection with the acquisition or ownership of its investments. Outside counsel will identify significant cases that should be brought to the Board’s attention and, if the Board decides to take an active role in the case, to help evaluate an appropriate litigation strategy.²

The landscape of United States securities laws drastically changed with the Supreme Court decision in *Morrison v. National Australia Bank Ltd.*, 561 U.S. 247 (2010). Under *Morrison*, investors no longer have the protection of the U.S. securities laws if the securities were purchased on a foreign exchange. After the *Morrison* decision, it is no longer possible to pursue a recovery in securities litigation in a foreign jurisdiction as a “free rider” as part of a class action, and an affirmative decision to participate in the class is typically required. Generally, in cases pending in foreign jurisdictions, VRS will only consider recovery methods that do not involve a risk that VRS would be liable for any expenses if the litigation were unsuccessful. For example, in most cases, VRS would not consider pursuing recovery in a foreign jurisdiction where the losing party in litigation pays the prevailing party’s fees and costs. However, VRS might consider such foreign litigation if there was insurance in place to cover the potential “loser pays” liability.

On relatively rare occasions, other types of litigation affect VRS that are not related to securities litigation for investments in which VRS has incurred a loss. For example, VRS may be a defendant in litigation, and the outcome of the litigation could affect the assets in the trust fund. While these types of cases are relatively rare and arise under unique facts

² See “Selection of Counsel” in section II (C) (2).

and circumstances, the same guiding principle applies to the strategic decisions that may be involved in their resolution.

II. GUIDELINES

A. PROXY VOTING

VRS should contract out the development of proxy voting positions to a Proxy Voting Service Provider. The decision by VRS staff to hire an outside Proxy Voting Service Provider should be based on a thorough review of the provider's proxy voting policies. These proxy voting policies must be based on sound economic analysis and research of proxy issues and driven solely by the objective of enhancing and protecting shareholder returns. VRS staff should review and evaluate the Proxy Voting Service Provider used by VRS from time to time.

Generally, VRS policy mandates that the Proxy Voting Service Provider vote all proxies. Exceptions to this policy include commingled or mutual funds where proxy policies are part of the fund documentation and certain separate accounts where proxy voting is part of the firm's investment strategy. VRS staff should review the proxy voting policies of such managers for overall reasonableness and should use the results of this review as a manager evaluation criterion.

VRS staff should provide to the Board from time to time a review and evaluation of the VRS Proxy Voting Service Provider.

B. VRS AS LONG-TERM INVESTOR

It is expected that VRS will align itself with certain oversight organizations with an eye toward creating and improving economic value for shareholders. This will provide VRS with access to multiple, cost-effective tools for promoting good corporate governance at portfolio companies and for monitoring regulatory organizations such as the Securities and Exchange Commission. Moreover, membership will provide information and analysis about corporate governance issues, best practices and solutions going forward.

C. LITIGATION

1. Filing Proofs of Claim

The VRS custodial bank is responsible for filing all proofs of claim, including the necessary supporting documents and information, in every securities class action pending in the U.S. in which VRS has an interest (the "Claims Filing"). To memorialize the custodian's Claims Filing responsibilities, the Chief Investment Officer ("CIO") shall prepare and revise, as appropriate, a statement of work to be included with the custodial

agreement setting out formal Claims Filing procedures for the custodial bank to follow. These procedures shall include:

- i. Identifying and reviewing all class action recoveries (whether by settlement or trial)
- ii. Providing timely notice of each settlement recovery, with sufficient time to allow VRS to opt out
- iii. Filing complete and accurate proof of claim forms in a timely fashion on behalf of VRS
- iv. Providing quarterly reports regarding these efforts
- v. Providing quarterly reports identifying all securities litigation proceeds recovered by VRS directly or on its behalf

Alternatively, the VRS Board may elect to use a third-party vendor to be responsible for the Claims Filing activities.

2. Selection of Counsel

VRS has undertaken an open procurement process to select a number of outside counsel firms to provide legal advice related to investments, and has entered into contractual agreements with each of the firms. Pursuant to this policy, VRS staff is authorized to select which of these firms should assist with a specific action depending on the facts and circumstances of each case. Criteria may include the firm's expertise in a particular area of law, the firm's analysis of a specific case, or the firm's recommended strategy.

3. Class Actions – Securities Listed on a Domestic Exchange

The Board desires to create an evaluation policy that provides guidance regarding when and how VRS will become actively involved in domestic securities litigation, including seeking lead plaintiff status. The VRS Board adopts this policy to place itself, the CIO and the Director, with the advice of counsel, in the best position to identify, protect, and serve the best interests of VRS.

The following is an outline of the procedures to assist in decisions regarding domestic securities litigation issues.

i. Monitoring and Evaluation Procedures

VRS may retain a vendor specializing in identifying and analyzing potential and existing securities cases to perform this function, and to report its findings on a timely basis. VRS also retains law firms as outside counsel to monitor and advise VRS of recently-filed

class actions that appear to have merit and for which VRS has sustained a loss that (i) exceeds its Loss Threshold or (ii) is substantial and involves unique factors justifying the involvement of VRS regardless of the Loss Threshold.

When a case meets the Loss Threshold for active management, VRS staff, in consultation with the office of the Attorney General (“OAG”) and outside counsel, shall evaluate whether the class action is meritorious and deserves closer examination. The evaluation shall include a review of available information regarding the lawsuit before considering whether to seek lead plaintiff status or embark on some other active claim management strategy (e.g., opting out of the class and pursuing a separate claim).

ii. Decision-making Process

Absent a loss exceeding the Loss Threshold or unusual and compelling circumstances, the VRS Board will not consider pursuing any active claim management strategy for any given case without the concurrence of the Office of the Attorney General (“OAG”). VRS staff should work with outside counsel to evaluate securities litigation options available to VRS on a case-by-case basis. VRS may also engage other vendors to monitor and identify potential securities litigation cases. These outside entities should forward material pertaining to such cases to VRS for further review and evaluation under the guidance contained in this policy.

The VRS Board will only consider taking an active role in litigation in accordance with the “Monitoring and Evaluation Procedures” described above.

If these initial criteria are met, VRS staff should coordinate its analysis with outside counsel to ensure that the situation meets the VRS criteria. If so, VRS staff and outside counsel should forward relevant information and a recommended course of legal action to VRS investment staff for review and evaluation consistent with the guidance contained in this policy. Following this review and evaluation, VRS staff should only forward a recommendation to pursue legal action to the VRS Board for those cases that are considered appropriate under this policy.

In most cases, decisions regarding a given case must be submitted, in advance, to the VRS Board at a regular meeting or, where immediate action is necessary, at a special meeting. However, where it is determined that immediate action is required in order to preserve the rights or interests of VRS by such involvement, and the matter cannot be timely presented at a regular or special meeting, or where a quorum cannot be reached at such meeting, the Chair of the VRS Board (or if the Chair is not available, the Vice Chair or the Chair’s designee), after consultation with the Director and CIO, and with the advice of counsel, is authorized to make the decision. The VRS Board shall be notified as soon as practicable upon the exercise of such authority, and the VRS Board shall receive a summary of the action at its next regular meeting. This procedure may also be used for other

time-sensitive decisions related to securities litigation where it is deemed in the best interests of the plan to do so, to the extent such decisions are in conformance with this policy.

If the VRS Board (or its designees under this policy) approves a recommendation to pursue an active role in a given case, VRS will work with outside counsel to pursue an agreed-upon litigation or active claim management strategy.

The VRS Board should receive an annual report on the total asset recoveries from securities litigation received during the year, including a status report on any litigation in which VRS is the lead plaintiff.

iii. Settlement or Other Disposition/Resolution

In most cases, decisions to settle a case or to pursue other disposition or resolution in a given case will be submitted, in advance, to the VRS Board at a regular meeting or, where immediate action is necessary, at a special meeting. However, where it is determined that immediate action is required in order to preserve the rights or interests of VRS by such involvement, and the matter cannot be timely presented at a regular or special meeting, or where a quorum cannot be reached at such meeting, the Chair of the VRS Board (or if the Chair is not available, the Vice Chair or the Chair's designee), after consultation with the Director and CIO, and with the advice of counsel, is authorized to make the decision. The VRS Board shall be notified as soon as practicable upon the exercise of such authority, and the VRS Board shall receive a summary of the action at its next regular meeting.

3. Class Actions – Securities Listed on a Foreign Exchange

Given the new realities of global securities litigation after *Morrison*, VRS must adapt to the new challenges of monitoring its portfolio to ensure that opportunities to recover assets based on securities fraud are not lost. This includes the analysis of whether to participate in an action in a foreign jurisdiction or to bring a state law action.

i. Participation in a Foreign Action

Unlike the class action process in the United States where investors can remain absent, receive notice of a settlement, and then decide to file a proof of claim or opt-out of the class case, foreign actions generally require investors to join as named plaintiffs or “opt-in” at the commencement of the case. This “opt-in” process will require affirmative decisions by VRS early in the process to join the case (and sometimes prior to the case being filed) to recover anything on its losses.

There are select foreign jurisdictions such as Australia, Japan and possibly other emerging jurisdictions where participation is very similar to the claims filing process in

domestic actions. For example, participation does not involve a risk that VRS would be liable for expenses if the litigation is unsuccessful (i.e., no “loser pays” rule or the risk is assumed by a third party), and VRS could assume a passive role in its participation in the case after an initial filing of transactional data supporting the VRS claim. Under those circumstances, the Loss Threshold does not come into play as the only way for VRS to participate in a foreign case to maximize its potential recovery on actionable losses is to take affirmative action.

In the case of jurisdictions (such as Australia and Japan) where participation in a foreign action does not involve a risk that VRS would be liable for expenses if the litigation is unsuccessful, VRS staff should obtain assurances and recommendations from its outside counsel and the OAG in the review and evaluation of foreign actions in those jurisdictions. In cases where there is no risk that VRS will be liable for expenses in the event of a loss, the Chair of the VRS Board (or if the Chair is not available, the Vice Chair or the Chair’s designee), after consultation with the Director and CIO, and with the advice of counsel, is authorized to make the decision to participate in a foreign action. The VRS Board shall be notified as soon as practicable upon the exercise of such authority, and the VRS Board shall receive a summary of the action at its next regular meeting. Consistent with the *Code of Virginia*, VRS staff will coordinate its efforts with OAG or the Governor’s Office as appropriate under the circumstances.

ii. Participation in State Law Action

Another option that is sometimes available with a foreign loss is to bring an action under state law in the United States. Because there are numerous issues that must be considered beforehand, the VRS Board should consider an action under state law only under very rare circumstances and after extensive consultation with staff, OAG, and outside counsel. In most cases, decisions regarding bringing a state law action related to a given foreign case will be submitted, in advance, to the VRS Board at a regular meeting or, where immediate action is necessary, at a special meeting. However, where it is determined that immediate action is required in order to preserve the rights or interests of VRS by such involvement, and the matter cannot be timely presented at a regular or special meeting, or where a quorum cannot be reached at such meeting, the Chair of the VRS Board (or if the Chair is not available, the Vice Chair or the Chair’s designee), after consultation with the Director and CIO, and with the advice of counsel, is authorized to make the decision. The VRS Board shall be notified as soon as practicable upon the exercise of such authority, and the VRS Board shall receive a summary of the action at its next regular meeting.

iii. Settlement or Other Disposition/Resolution

In most cases, decisions to settle a case or to pursue other disposition or resolution in a given case will be submitted, in advance, to the VRS Board at a regular meeting or, where immediate action is necessary, at a special meeting. However, where it is determined

that immediate action is required in order to preserve the rights or interests of VRS by such settlement or other disposition, and the matter cannot be timely presented at a regular or special meeting, or where a quorum cannot be reached at such meeting, the Chair of the VRS Board (or if the Chair is not available, the Vice Chair or the Chair's designee), after consultation with the Director and CIO, and with the advice of counsel, is authorized to make the decision. The VRS Board shall be notified as soon as practicable upon the exercise of such authority, and the VRS Board shall receive a summary of the action at its next regular meeting.

iv. Monitoring Procedures

VRS recognizes the importance of developing a protocol to stay informed and make prudent decisions relating to its involvement in foreign actions. VRS will use outside counsel and other entities to assist in monitoring foreign actions. This will ensure that VRS has the greatest possible visibility into applicable deadlines so VRS can make a timely and informed decision on whether to participate in a given foreign action and in what manner such participation will occur.

The VRS Board should receive an annual report on the total asset recoveries from foreign securities litigation received during the year.

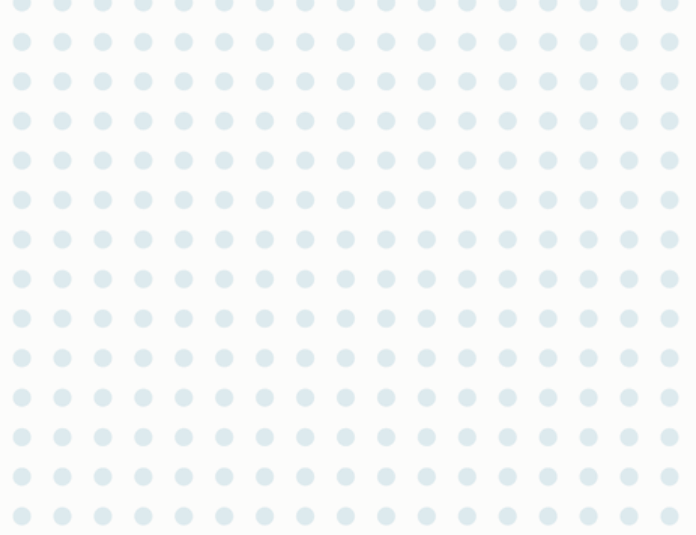
4. Other Litigation

In all other types of litigation, with the exception of cases under the Administrative Process Act, such as those cases where VRS is a defendant and settlement negotiations may be ongoing, VRS staff will submit recommendations for actions (e.g., approval of a settlement), in advance, to the VRS Board at a regular meeting or, where immediate action is necessary, at a special meeting. However, where it is determined that immediate action is required in order to preserve the rights or interests of VRS, and the matter cannot be timely presented at a regular or special meeting, or where a quorum cannot be reached at such meeting, the Chair of the VRS Board (or if the Chair is not available, the Vice Chair or the Chair's designee), after consultation with the Director and CIO, and with the advice of counsel, is authorized to make the decision. The VRS Board shall be notified as soon as practicable upon the exercise of such authority, and the VRS Board shall receive a summary of the action at its next regular meeting. Consistent with the *Code of Virginia*, VRS staff will coordinate its efforts with OAG or the Governor's Office as appropriate under the circumstances.

5. Interpretation

The Board of Trustees intends that this Policy should be construed broadly to provide the flexibility necessary for VRS to take immediate action where it is required to protect the best interests of the Fund's members, retirees and beneficiaries. In all cases, any

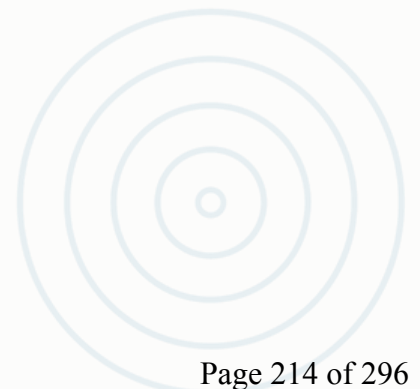
such action must be reported to the Board at the earliest practicable opportunity and summarized at the next regular meeting of the Board.



UNITED STATES

Proxy Voting Guidelines Benchmark Policy Recommendations

Effective for Meetings on or after February 1, 2022
Published December 13, 2021



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Coverage

The U.S. research team provides proxy analyses and voting recommendations for the common shareholder meetings of U.S. - incorporated companies that are publicly-traded on U.S. exchanges, as well as certain OTC companies, if they are held in our institutional investor clients' portfolios. Coverage generally includes corporate actions for common equity holders, such as written consents and bankruptcies. ISS' U.S. coverage includes investment companies (including open-end funds, closed-end funds, exchange-traded funds, and unit investment trusts), limited partnerships ("LPs"), master limited partnerships ("MLPs"), limited liability companies ("LLCs"), and business development companies. ISS reviews its universe of coverage on an annual basis, and the coverage is subject to change based on client need and industry trends.

Foreign-incorporated companies

In addition to U.S.- incorporated, U.S.- listed companies, ISS' U.S. policies are applied to certain foreign-incorporated company analyses. Like the SEC, ISS distinguishes two types of companies that list but are not incorporated in the U.S.:

- U.S. Domestic Issuers – which have a majority of outstanding shares held in the U.S. and meet other criteria, as determined by the SEC, and are subject to the same disclosure and listing standards as U.S. incorporated companies (e.g. they are required to file DEF14A proxy statements) – are generally covered under standard U.S. policy guidelines.
- [Foreign Private Issuers](#) (FPIs) – which are allowed to take exemptions from most disclosure requirements (e.g., they are allowed to file 6-K for their proxy materials) and U.S. listing standards – are generally covered under a combination of policy guidelines:
 - FPI Guidelines (see the [Americas Regional Proxy Voting Guidelines](#)), may apply to companies incorporated in governance havens, and apply certain minimum independence and disclosure standards in the evaluation of key proxy ballot items, such as the election of directors; and/or
 - Guidelines for the market that is responsible for, or most relevant to, the item on the ballot.

U.S. incorporated companies listed only on non-U.S. exchanges are generally covered under the ISS guidelines for the market on which they are traded.

An FPI is generally covered under ISS' approach to FPIs outlined above, even if such FPI voluntarily files a proxy statement and/or other filing normally required of a U.S. Domestic Issuer, so long as the company retains its FPI status.

In all cases – including with respect to other companies with cross-market features that may lead to ballot items related to multiple markets – items that are on the ballot solely due to the requirements of another market (listing, incorporation, or national code) may be evaluated under the policy of the relevant market, regardless of the "assigned" primary market coverage.

1. Board of Directors

Voting on Director Nominees in Uncontested Elections


Four fundamental principles apply when determining votes on director nominees:

Independence: Boards should be sufficiently independent from management (and significant shareholders) to ensure that they are able and motivated to effectively supervise management's performance for the benefit of all shareholders, including in setting and monitoring the execution of corporate strategy, with appropriate use of shareholder capital, and in setting and monitoring executive compensation programs that support that strategy. The chair of the board should ideally be an independent director, and all boards should have an independent leadership position or a similar role in order to help provide appropriate counterbalance to executive management, as well as having sufficiently independent committees that focus on key governance concerns such as audit, compensation, and nomination of directors.

Composition: Companies should ensure that directors add value to the board through their specific skills and expertise and by having sufficient time and commitment to serve effectively. Boards should be of a size appropriate to accommodate diversity, expertise, and independence, while ensuring active and collaborative participation by all members. Boards should be sufficiently diverse to ensure consideration of a wide range of perspectives.

Responsiveness: Directors should respond to investor input, such as that expressed through significant opposition to management proposals, significant support for shareholder proposals (whether binding or non-binding), and tender offers where a majority of shares are tendered.

Accountability: Boards should be sufficiently accountable to shareholders, including through transparency of the company's governance practices and regular board elections, by the provision of sufficient information for shareholders to be able to assess directors and board composition, and through the ability of shareholders to remove directors.

 **General Recommendation:** Generally vote for director nominees, except under the following circumstances (with new nominees¹ considered on case-by-case basis):

Independence

Vote against² or withhold from non-independent directors (Executive Directors and Non-Independent Non-Executive Directors per [ISS' Classification of Directors](#)) when:

- Independent directors comprise 50 percent or less of the board;
- The non-independent director serves on the audit, compensation, or nominating committee;
- The company lacks an audit, compensation, or nominating committee so that the full board functions as that committee; or
- The company lacks a formal nominating committee, even if the board attests that the independent directors fulfill the functions of such a committee.

¹ A "new nominee" is a director who is being presented for election by shareholders for the first time. Recommendations on new nominees who have served for less than one year are made on a case-by-case basis depending on the timing of their appointment and the problematic governance issue in question.

² In general, companies with a plurality vote standard use "Withhold" as the contrary vote option in director elections; companies with a majority vote standard use "Against". However, it will vary by company and the proxy must be checked to determine the valid contrary vote option for the particular company.

ISS Classification of Directors – U.S.

1. **Executive Director**
 - 1.1. Current officer¹ of the company or one of its affiliates².
2. **Non-Independent Non-Executive Director**
 - Board Identification
 - 2.1. Director identified as not independent by the board.
 - Controlling/Significant Shareholder
 - 2.2. Beneficial owner of more than 50 percent of the company's voting power (this may be aggregated if voting power is distributed among more than one member of a group).
 - Current Employment at Company or Related Company
 - 2.3. Non-officer employee of the firm (including employee representatives).
 - 2.4. Officer¹, former officer, or general or limited partner of a joint venture or partnership with the company.
 - Former Employment
 - 2.5. Former CEO of the company.^{3,4}
 - 2.6. Former non-CEO officer¹ of the company or an affiliate² within the past five years.
 - 2.7. Former officer¹ of an acquired company within the past five years.⁴
 - 2.8. Officer¹ of a former parent or predecessor firm at the time the company was sold or split off within the past five years.
 - 2.9. Former interim officer if the service was longer than 18 months. If the service was between 12 and 18 months an assessment of the interim officer's employment agreement will be made.⁵
 - Family Members
 - 2.10. Immediate family member⁶ of a current or former officer¹ of the company or its affiliates² within the last five years.
 - 2.11. Immediate family member⁶ of a current employee of company or its affiliates² where additional factors raise concern (which may include, but are not limited to, the following: a director related to numerous employees; the company or its affiliates employ relatives of numerous board members; or a non-Section 16 officer in a key strategic role).
 - Professional, Transactional, and Charitable Relationships
 - 2.12. Director who (or whose immediate family member⁶) currently provides professional services⁷ in excess of \$10,000 per year to: the company, an affiliate², or an individual officer of the company or an affiliate; or who is (or whose immediate family member⁶ is) a partner, employee, or controlling shareholder of an organization which provides the services.
 - 2.13. Director who (or whose immediate family member⁶) currently has any material transactional relationship⁸ with the company or its affiliates²; or who is (or whose immediate family member⁶ is) a partner in, or a controlling shareholder or an executive officer of, an organization which has the material transactional relationship⁸ (excluding investments in the company through a private placement).
 - 2.14. Director who (or whose immediate family member⁶) is a trustee, director, or employee of a charitable or non-profit organization that receives material grants or endowments⁸ from the company or its affiliates².
 - Other Relationships
 - 2.15. Party to a voting agreement⁹ to vote in line with management on proposals being brought to shareholder vote.
 - 2.16. Has (or an immediate family member⁶ has) an interlocking relationship as defined by the SEC involving members of the board of directors or its Compensation Committee.¹⁰
 - 2.17. Founder¹¹ of the company but not currently an employee.
 - 2.18. Director with pay comparable to Named Executive Officers.
 - 2.19. Any material¹² relationship with the company.
3. **Independent Director**
 - 3.1. No material¹² connection to the company other than a board seat.

Footnotes:

1. The definition of officer will generally follow that of a “Section 16 officer” (officers subject to Section 16 of the Securities and Exchange Act of 1934) and includes the chief executive, operating, financial, legal, technology, and accounting officers of a company (including the president, treasurer, secretary, controller, or any vice president in charge of a principal business unit, division, or policy function). Current interim officers are included in this category. For private companies, the equivalent positions are applicable. A non-employee director serving as an officer due to statutory requirements (e.g. corporate secretary) will generally be classified as a Non-Independent Non-Executive Director under “Any material relationship with the company.” However, if the company provides explicit disclosure that the director is not receiving additional compensation exceeding \$10,000 per year for serving in that capacity, then the director will be classified as an Independent Director.
2. “Affiliate” includes a subsidiary, sibling company, or parent company. ISS uses 50 percent control ownership by the parent company as the standard for applying its affiliate designation. The manager/advisor of an externally managed issuer (EMI) is considered an affiliate.
3. Includes any former CEO of the company prior to the company’s initial public offering (IPO).
4. When there is a former CEO of a special purpose acquisition company (SPAC) serving on the board of an acquired company, ISS will generally classify such directors as independent unless determined otherwise taking into account the following factors: the applicable listing standards determination of such director’s independence; any operating ties to the firm; and the existence of any other conflicting relationships or related party transactions.
5. ISS will look at the terms of the interim officer’s employment contract to determine if it contains severance pay, long-term health and pension benefits, or other such standard provisions typically contained in contracts of permanent, non-temporary CEOs. ISS will also consider if a formal search process was under way for a full-time officer at the time.
6. “Immediate family member” follows the SEC’s definition of such and covers spouses, parents, children, step-parents, step-children, siblings, in-laws, and any person (other than a tenant or employee) sharing the household of any director, nominee for director, executive officer, or significant shareholder of the company.
7. Professional services can be characterized as advisory in nature, generally involve access to sensitive company information or to strategic decision-making, and typically have a commission- or fee-based payment structure. Professional services generally include but are not limited to the following: investment banking/financial advisory services, commercial banking (beyond deposit services), investment services, insurance services, accounting/audit services, consulting services, marketing services, legal services, property management services, realtor services, lobbying services, executive search services, and IT consulting services. The following would generally be considered transactional relationships and not professional services: deposit services, IT tech support services, educational services, and construction services. The case of participation in a banking syndicate by a non-lead bank should be considered a transactional (and hence subject to the associated materiality test) rather than a professional relationship. “Of Counsel” relationships are only considered immaterial if the individual does not receive any form of compensation (in excess of \$10,000 per year) from, or is a retired partner of, the firm providing the professional service. The case of a company providing a professional service to one of its directors or to an entity with which one of its directors is affiliated, will be considered a transactional rather than a professional relationship. Insurance services and marketing services are assumed to be professional services unless the company explains why such services are not advisory.
8. A material transactional relationship, including grants to non-profit organizations, exists if the company makes annual payments to, or receives annual payments from, another entity, exceeding the greater of: \$200,000 or 5 percent of the recipient’s gross revenues, for a company that follows NASDAQ listing standards; or the greater of \$1,000,000 or 2 percent of the recipient’s gross revenues, for a company that follows NYSE listing standards. For a company that follows neither of the preceding standards, ISS will apply the NASDAQ-based materiality test. (The recipient is the party receiving the financial proceeds from the transaction).
9. Dissident directors who are parties to a voting agreement pursuant to a settlement or similar arrangement may be classified as Independent Directors if an analysis of the following factors indicates that the voting agreement does not compromise their alignment with all shareholders’ interests: the terms of the agreement; the duration of the standstill provision in the agreement; the limitations and requirements of actions that are agreed upon; if the dissident director nominee(s) is subject to the standstill; and if there any conflicting relationships or related party transactions.
10. Interlocks include: executive officers serving as directors on each other’s compensation or similar committees (or, in the absence of such a committee, on the board); or executive officers sitting on each other’s boards and at least one serves on the other’s compensation or similar committees (or, in the absence of such a committee, on the board).

11. The operating involvement of the founder with the company will be considered; if the founder was never employed by the company, ISS may deem him or her an Independent Director.

12. For purposes of ISS's director independence classification, "material" will be defined as a standard of relationship (financial, personal, or otherwise) that a reasonable person might conclude could potentially influence one's objectivity in the boardroom in a manner that would have a meaningful impact on an individual's ability to satisfy requisite fiduciary standards on behalf of shareholders.

Composition

Attendance at Board and Committee Meetings: Generally vote against or withhold from directors (except nominees who served only part of the fiscal year³) who attend less than 75 percent of the aggregate of their board and committee meetings for the period for which they served, unless an acceptable reason for absences is disclosed in the proxy or another SEC filing. Acceptable reasons for director absences are generally limited to the following:

- Medical issues/illness;
- Family emergencies; and
- Missing only one meeting (when the total of all meetings is three or fewer).

In cases of chronic poor attendance without reasonable justification, in addition to voting against the director(s) with poor attendance, generally vote against or withhold from appropriate members of the nominating/governance committees or the full board.

If the proxy disclosure is unclear and insufficient to determine whether a director attended at least 75 percent of the aggregate of his/her board and committee meetings during his/her period of service, vote against or withhold from the director(s) in question.

Overboarded Directors: Generally vote against or withhold from individual directors who:

- Sit on more than five public company boards; or
- Are CEOs of public companies who sit on the boards of more than two public companies besides their own— withhold only at their outside boards⁴.

Gender Diversity: For companies in the Russell 3000 or S&P 1500 indices, generally vote against or withhold from the chair of the nominating committee (or other directors on a case-by-case basis) at companies where there are no women on the company's board. An exception will be made if there was a woman on the board at the preceding annual meeting and the board makes a firm commitment to return to a gender-diverse status within a year.

³ Nominees who served for only part of the fiscal year are generally exempted from the attendance policy.

⁴ Although all of a CEO's subsidiary boards with publicly-traded common stock will be counted as separate boards, ISS will not recommend a withhold vote for the CEO of a parent company board or any of the controlled (>50 percent ownership) subsidiaries of that parent but may do so at subsidiaries that are less than 50 percent controlled and boards outside the parent/subsidiary relationships.

This policy will also apply for companies not in the Russell 3000 and S&P1500 indices, effective for meetings on or after **Feb. 1, 2023**.

Racial and/or Ethnic Diversity: For companies in the Russell 3000 or S&P 1500 indices, generally vote against or withhold from the chair of the nominating committee (or other directors on a case-by-case basis) where the board has no apparent racially or ethnically diverse members⁵. An exception will be made if there was racial and/or ethnic diversity on the board at the preceding annual meeting and the board makes a firm commitment to appoint at least one racial and/or ethnic diverse member within a year.

Responsiveness

Vote case-by-case on individual directors, committee members, or the entire board of directors as appropriate if:

- The board failed to act on a shareholder proposal that received the support of a majority of the shares cast in the previous year or failed to act on a management proposal seeking to ratify an existing charter/bylaw provision that received opposition of a majority of the shares cast in the previous year. Factors that will be considered are:
 - Disclosed outreach efforts by the board to shareholders in the wake of the vote;
 - Rationale provided in the proxy statement for the level of implementation;
 - The subject matter of the proposal;
 - The level of support for and opposition to the resolution in past meetings;
 - Actions taken by the board in response to the majority vote and its engagement with shareholders;
 - The continuation of the underlying issue as a voting item on the ballot (as either shareholder or management proposals); and
 - Other factors as appropriate.
- The board failed to act on takeover offers where the majority of shares are tendered;
- At the previous board election, any director received more than 50 percent withhold/against votes of the shares cast and the company has failed to address the issue(s) that caused the high withhold/against vote.

Vote case-by-case on Compensation Committee members (or, in exceptional cases, the full board) and the Say on Pay proposal if:

- The company's previous say-on-pay received the support of less than 70 percent of votes cast. Factors that will be considered are:
 - The company's response, including:
 - Disclosure of engagement efforts with major institutional investors, including the frequency and timing of engagements and the company participants (including whether independent directors participated);
 - Disclosure of the specific concerns voiced by dissenting shareholders that led to the say-on-pay opposition;
 - Disclosure of specific and meaningful actions taken to address shareholders' concerns;
 - Other recent compensation actions taken by the company;
 - Whether the issues raised are recurring or isolated;
 - The company's ownership structure; and
 - Whether the support level was less than 50 percent, which would warrant the highest degree of responsiveness.

⁵ Aggregate diversity statistics provided by the board will only be considered if specific to racial and/or ethnic diversity.

- The board implements an advisory vote on executive compensation on a less frequent basis than the frequency that received the plurality of votes cast.

Accountability

Problematic Takeover Defenses/Governance Structure

Poison Pills: Vote against or withhold from all nominees (except new nominees¹, who should be considered case-by-case) if:

- The company has a poison pill that was not approved by shareholders⁶. However, vote case-by-case on nominees if the board adopts an initial pill with a term of one year or less, depending on the disclosed rationale for the adoption, and other factors as relevant (such as a commitment to put any renewal to a shareholder vote);
- The board makes a material adverse modification to an existing pill, including, but not limited to, extension, renewal, or lowering the trigger, without shareholder approval; or
- The pill, whether short-term⁷ or long-term, has a deadhand or slowhand feature.

Classified Board Structure: The board is classified, and a continuing director responsible for a problematic governance issue at the board/committee level that would warrant a withhold/against vote recommendation is not up for election. All appropriate nominees (except new) may be held accountable.

Removal of Shareholder Discretion on Classified Boards: The company has opted into, or failed to opt out of, state laws requiring a classified board structure.

Director Performance Evaluation: The board lacks mechanisms to promote accountability and oversight, coupled with sustained poor performance relative to peers. Sustained poor performance is measured by one-, three-, and five-year total shareholder returns in the bottom half of a company's four-digit GICS industry group (Russell 3000 companies only). Take into consideration the company's operational metrics and other factors as warranted. Problematic provisions include but are not limited to:

- A classified board structure;
- A supermajority vote requirement;
- Either a plurality vote standard in uncontested director elections, or a majority vote standard in contested elections;
- The inability of shareholders to call special meetings;
- The inability of shareholders to act by written consent;
- A multi-class capital structure; and/or
- A non-shareholder-approved poison pill.

Unilateral Bylaw/Charter Amendments and Problematic Capital Structures: Generally vote against or withhold from directors individually, committee members, or the entire board (except new nominees¹, who should be considered case-by-case) if the board amends the company's bylaws or charter without shareholder approval in a manner that materially diminishes shareholders' rights or that could adversely impact shareholders, considering the following factors:

- The board's rationale for adopting the bylaw/charter amendment without shareholder ratification;
- Disclosure by the company of any significant engagement with shareholders regarding the amendment;

⁶ Public shareholders only, approval prior to a company's becoming public is insufficient.

⁷ If the short-term pill with a deadhand or slowhand feature is enacted but expires before the next shareholder vote, ISS will generally still recommend withhold/against nominees at the next shareholder meeting following its adoption.

- The level of impairment of shareholders' rights caused by the board's unilateral amendment to the bylaws/charter;
- The board's track record with regard to unilateral board action on bylaw/charter amendments or other entrenchment provisions;
- The company's ownership structure;
- The company's existing governance provisions;
- The timing of the board's amendment to the bylaws/charter in connection with a significant business development; and
- Other factors, as deemed appropriate, that may be relevant to determine the impact of the amendment on shareholders.

Unless the adverse amendment is reversed or submitted to a binding shareholder vote, in subsequent years vote case-by-case on director nominees. Generally vote against (except new nominees¹, who should be considered case-by-case) if the directors:

- Classified the board;
- Adopted supermajority vote requirements to amend the bylaws or charter; or
- Eliminated shareholders' ability to amend bylaws.

Unequal Voting Rights

Problematic Capital Structure - Newly Public Companies: For **2022**, for newly public companies⁸, generally vote against or withhold from the entire board (except new nominees¹, who should be considered case-by-case) if, prior to or in connection with the company's public offering, the company or its board implemented a multi-class capital structure in which the classes have unequal voting rights without subjecting the multi-class capital structure to a reasonable time-based sunset. In assessing the reasonableness of a time-based sunset provision, consideration will be given to the company's lifespan, its post-IPO ownership structure and the board's disclosed rationale for the sunset period selected. No sunset period of more than seven years from the date of the IPO will be considered to be reasonable.

Continue to vote against or withhold from incumbent directors in subsequent years, unless the problematic capital structure is reversed, removed, or subject to a newly added reasonable sunset.

Common Stock Capital Structure with Unequal Voting Rights: Starting **Feb 1, 2023**, generally vote withhold or against directors individually, committee members, or the entire board (except new nominees¹, who should be considered case-by-case), if the company employs a common stock structure with unequal voting rights⁹.

Exceptions to this policy will generally be limited to:

- Newly-public companies⁸ with a sunset provision of no more than seven years from the date of going public;
- Limited Partnerships and the Operating Partnership (OP) unit structure of REITs;
- Situations where the unequal voting rights are considered *de minimis*; or
- The company provides sufficient protections for minority shareholders, such as allowing minority shareholders a regular binding vote on whether the capital structure should be maintained.

⁸ Newly-public companies generally include companies that emerge from bankruptcy, SPAC transactions, spin-offs, direct listings, and those who complete a traditional initial public offering.

⁹ This generally includes classes of common stock that have additional votes per share than other shares; classes of shares that are not entitled to vote on all the same ballot items or nominees; or stock with time-phased voting rights ("loyalty shares").

Problematic Governance Structure - Newly Public Companies: For newly public companies⁸, generally vote against or withhold from directors individually, committee members, or the entire board (except new nominees¹, who should be considered case-by-case) if, prior to or in connection with the company's public offering, the company or its board adopted the following bylaw or charter provisions that are considered to be materially adverse to shareholder rights:

- Supermajority vote requirements to amend the bylaws or charter;
- A classified board structure; or
- Other egregious provisions.

A reasonable sunset provision will be considered a mitigating factor.

Unless the adverse provision is reversed or removed, vote case-by-case on director nominees in subsequent years.

Management Proposals to Ratify Existing Charter or Bylaw Provisions: Vote against/withhold from individual directors, members of the governance committee, or the full board, where boards ask shareholders to ratify existing charter or bylaw provisions considering the following factors:

- The presence of a shareholder proposal addressing the same issue on the same ballot;
- The board's rationale for seeking ratification;
- Disclosure of actions to be taken by the board should the ratification proposal fail;
- Disclosure of shareholder engagement regarding the board's ratification request;
- The level of impairment to shareholders' rights caused by the existing provision;
- The history of management and shareholder proposals on the provision at the company's past meetings;
- Whether the current provision was adopted in response to the shareholder proposal;
- The company's ownership structure; and
- Previous use of ratification proposals to exclude shareholder proposals.

Restrictions on Shareholders' Rights

Restricting Binding Shareholder Proposals: Generally vote against or withhold from the members of the governance committee if:

- The company's governing documents impose undue restrictions on shareholders' ability to amend the bylaws. Such restrictions include but are not limited to: outright prohibition on the submission of binding shareholder proposals or share ownership requirements, subject matter restrictions, or time holding requirements in excess of SEC Rule 14a-8. Vote against or withhold on an ongoing basis.

Submission of management proposals to approve or ratify requirements in excess of SEC Rule 14a-8 for the submission of binding bylaw amendments will generally be viewed as an insufficient restoration of shareholders' rights. Generally continue to vote against or withhold on an ongoing basis until shareholders are provided with an unfettered ability to amend the bylaws or a proposal providing for such unfettered right is submitted for shareholder approval.

Problematic Audit-Related Practices

Generally vote against or withhold from the members of the Audit Committee if:

- The non-audit fees paid to the auditor are [excessive](#);
- The company receives an adverse opinion on the company's financial statements from its auditor; or
- There is persuasive evidence that the Audit Committee entered into an inappropriate indemnification agreement with its auditor that limits the ability of the company, or its shareholders, to pursue legitimate legal recourse against the audit firm.

Vote case-by-case on members of the Audit Committee and potentially the full board if:

- Poor accounting practices are identified that rise to a level of serious concern, such as: fraud; misapplication of GAAP; and material weaknesses identified in Section 404 disclosures. Examine the severity, breadth, chronological sequence, and duration, as well as the company's efforts at remediation or corrective actions, in determining whether withhold/against votes are warranted.

Problematic Compensation Practices

In the absence of an Advisory Vote on Executive Compensation (Say on Pay) ballot item or in egregious situations, vote against or withhold from the members of the Compensation Committee and potentially the full board if:

- There is an unmitigated misalignment between CEO pay and company performance ([pay for performance](#));
- The company maintains significant [problematic pay practices](#); or
- The board exhibits a significant level of [poor communication and responsiveness](#) to shareholders.

Generally vote against or withhold from the Compensation Committee chair, other committee members, or potentially the full board if:

- The company fails to include a Say on Pay ballot item when required under SEC provisions, or under the company's declared frequency of say on pay; or
- The company fails to include a Frequency of Say on Pay ballot item when required under SEC provisions.

Generally vote against members of the board committee responsible for approving/setting non-employee director compensation if there is a pattern (i.e. two or more years) of awarding excessive non-employee director compensation without disclosing a compelling rationale or other mitigating factors.

Problematic Pledging of Company Stock:

Vote against the members of the committee that oversees risks related to pledging, or the full board, where a significant level of pledged company stock by executives or directors raises concerns. The following factors will be considered:

- The presence of an anti-pledging policy, disclosed in the proxy statement, that prohibits future pledging activity;
- The magnitude of aggregate pledged shares in terms of total common shares outstanding, market value, and trading volume;
- Disclosure of progress or lack thereof in reducing the magnitude of aggregate pledged shares over time;
- Disclosure in the proxy statement that shares subject to stock ownership and holding requirements do not include pledged company stock; and
- Any other relevant factors.

Climate Accountability

For companies that are significant greenhouse gas (GHG) emitters, through their operations or value chain¹⁰, generally vote against or withhold from the incumbent chair of the responsible committee (or other directors on a case-by-case basis) in cases where ISS determines that the company is not taking the minimum steps needed to understand, assess, and mitigate risks related to climate change to the company and the larger economy.

¹⁰ For 2022, companies defined as "significant GHG emitters" will be those on the current Climate Action 100+ Focus Group list.

For **2022**, minimum steps to understand and mitigate those risks are considered to be the following. Both minimum criteria will be required to be in compliance:

- Detailed disclosure of climate-related risks, such as according to the framework established by the Task Force on Climate-related Financial Disclosures (TCFD), including:
 - Board governance measures;
 - Corporate strategy;
 - Risk management analyses; and
 - Metrics and targets.
- Appropriate GHG emissions reduction targets.

For **2022**, “appropriate GHG emissions reductions targets” will be any well-defined GHG reduction targets. Targets for Scope 3 emissions will not be required for 2022 but the targets should cover at least a significant portion of the company’s direct emissions. Expectations about what constitutes “minimum steps to mitigate risks related to climate change” will increase over time.

Governance Failures

Under extraordinary circumstances, vote against or withhold from directors individually, committee members, or the entire board, due to:

- Material failures of governance, stewardship, risk oversight¹¹, or fiduciary responsibilities at the company;
- Failure to replace management as appropriate; or
- Egregious actions related to a director’s service on other boards that raise substantial doubt about his or her ability to effectively oversee management and serve the best interests of shareholders at any company.

Voting on Director Nominees in Contested Elections

Vote-No Campaigns

- ▷ **General Recommendation:** In cases where companies are targeted in connection with public “vote-no” campaigns, evaluate director nominees under the existing governance policies for voting on director nominees in uncontested elections. Take into consideration the arguments submitted by shareholders and other publicly available information.

Proxy Contests/Proxy Access

- ▷ **General Recommendation:** Vote case-by-case on the election of directors in contested elections, considering the following factors:
- Long-term financial performance of the company relative to its industry;
 - Management’s track record;
 - Background to the contested election;
 - Nominee qualifications and any compensatory arrangements;
 - Strategic plan of dissident slate and quality of the critique against management;
 - Likelihood that the proposed goals and objectives can be achieved (both slates); and

¹¹ Examples of failure of risk oversight include but are not limited to: bribery; large or serial fines or sanctions from regulatory bodies; demonstrably poor risk oversight of environmental and social issues, including climate change; significant adverse legal judgments or settlement; or hedging of company stock.

- Stock ownership positions.

In the case of candidates nominated pursuant to proxy access, vote case-by-case considering any applicable factors listed above or additional factors which may be relevant, including those that are specific to the company, to the nominee(s) and/or to the nature of the election (such as whether there are more candidates than board seats).

Other Board-Related Proposals

Adopt Anti-Hedging/Pledging/Speculative Investments Policy

- ▷ **General Recommendation:** Generally vote for proposals seeking a policy that prohibits named executive officers from engaging in derivative or speculative transactions involving company stock, including hedging, holding stock in a margin account, or pledging stock as collateral for a loan. However, the company's existing policies regarding responsible use of company stock will be considered.

Board Refreshment

Board refreshment is best implemented through an ongoing program of individual director evaluations, conducted annually, to ensure the evolving needs of the board are met and to bring in fresh perspectives, skills, and diversity as needed.

Term/Tenure Limits

- ▷ **General Recommendation:** Vote case-by-case on management proposals regarding director term/tenure limits, considering:
- The rationale provided for adoption of the term/tenure limit;
 - The robustness of the company's board evaluation process;
 - Whether the limit is of sufficient length to allow for a broad range of director tenures;
 - Whether the limit would disadvantage independent directors compared to non-independent directors; and
 - Whether the board will impose the limit evenly, and not have the ability to waive it in a discriminatory manner.

Vote case-by-case on shareholder proposals asking for the company to adopt director term/tenure limits, considering:

- The scope of the shareholder proposal; and
- Evidence of problematic issues at the company combined with, or exacerbated by, a lack of board refreshment.

Age Limits

- ▷ **General Recommendation:** Generally vote against management and shareholder proposals to limit the tenure of independent directors through mandatory retirement ages. Vote for proposals to remove mandatory age limits.

Board Size

- ▷ **General Recommendation:** Vote for proposals seeking to fix the board size or designate a range for the board size.

Vote against proposals that give management the ability to alter the size of the board outside of a specified range without shareholder approval.

Classification/Declassification of the Board

- ▷ **General Recommendation:** Vote against proposals to classify (stagger) the board.

Vote for proposals to repeal classified boards and to elect all directors annually.

CEO Succession Planning

- ▷ **General Recommendation:** Generally vote for proposals seeking disclosure on a CEO succession planning policy, considering, at a minimum, the following factors:
- The reasonableness/scope of the request; and
 - The company's existing disclosure on its current CEO succession planning process.

Cumulative Voting

- ▷ **General Recommendation:** Generally vote against management proposals to eliminate cumulate voting, and for shareholder proposals to restore or provide for cumulative voting, unless:
- The company has proxy access¹², thereby allowing shareholders to nominate directors to the company's ballot; and
 - The company has adopted a majority vote standard, with a carve-out for plurality voting in situations where there are more nominees than seats, and a director resignation policy to address failed elections.

Vote for proposals for cumulative voting at controlled companies (insider voting power > 50%).

Director and Officer Indemnification and Liability Protection

- ▷ **General Recommendation:** Vote case-by-case on proposals on director and officer indemnification and liability protection.

Vote against proposals that would:

- Eliminate entirely directors' and officers' liability for monetary damages for violating the duty of care.
- Expand coverage beyond just legal expenses to liability for acts that are more serious violations of fiduciary obligation than mere carelessness.
- Expand the scope of indemnification to provide for mandatory indemnification of company officials in connection with acts that previously the company was permitted to provide indemnification for, at the discretion of the company's board (*i.e.*, "permissive indemnification"), but that previously the company was not required to indemnify.

Vote for only those proposals providing such expanded coverage in cases when a director's or officer's legal defense was unsuccessful if both of the following apply:

- If the director was found to have acted in good faith and in a manner that s/he reasonably believed was in the best interests of the company; and
- If only the director's legal expenses would be covered.

Establish/Amend Nominee Qualifications

- ▷ **General Recommendation:** Vote case-by-case on proposals that establish or amend director qualifications. Votes should be based on the reasonableness of the criteria and the degree to which they may preclude dissident nominees from joining the board.

Vote case-by-case on shareholder resolutions seeking a director nominee who possesses a particular subject matter expertise, considering:

¹² A proxy access right that meets the [recommended guidelines](#).

- The company's board committee structure, existing subject matter expertise, and board nomination provisions relative to that of its peers;
- The company's existing board and management oversight mechanisms regarding the issue for which board oversight is sought;
- The company's disclosure and performance relating to the issue for which board oversight is sought and any significant related controversies; and
- The scope and structure of the proposal.

Establish Other Board Committee Proposals

▷ **General Recommendation:** Generally vote against shareholder proposals to establish a new board committee, as such proposals seek a specific oversight mechanism/structure that potentially limits a company's flexibility to determine an appropriate oversight mechanism for itself. However, the following factors will be considered:

- Existing oversight mechanisms (including current committee structure) regarding the issue for which board oversight is sought;
- Level of disclosure regarding the issue for which board oversight is sought;
- Company performance related to the issue for which board oversight is sought;
- Board committee structure compared to that of other companies in its industry sector; and
- The scope and structure of the proposal.

Filling Vacancies/Removal of Directors

▷ **General Recommendation:** Vote against proposals that provide that directors may be removed only for cause. Vote for proposals to restore shareholders' ability to remove directors with or without cause. Vote against proposals that provide that only continuing directors may elect replacements to fill board vacancies. Vote for proposals that permit shareholders to elect directors to fill board vacancies.

Independent Board Chair

▷ **General Recommendation:** Generally vote for shareholder proposals requiring that the board chair position be filled by an independent director, taking into consideration the following:

- The scope and rationale of the proposal;
- The company's current board leadership structure;
- The company's governance structure and practices;
- Company performance; and
- Any other relevant factors that may be applicable.

The following factors will increase the likelihood of a "for" recommendation:

- A majority non-independent board and/or the presence of non-independent directors on key board committees;
- A weak or poorly-defined lead independent director role that fails to serve as an appropriate counterbalance to a combined CEO/chair role;
- The presence of an executive or non-independent chair in addition to the CEO, a recent recombination of the role of CEO and chair, and/or departure from a structure with an independent chair;
- Evidence that the board has failed to oversee and address material risks facing the company;
- A material governance failure, particularly if the board has failed to adequately respond to shareholder concerns or if the board has materially diminished shareholder rights; or
- Evidence that the board has failed to intervene when management's interests are contrary to shareholders' interests.

Majority of Independent Directors/Establishment of Independent Committees

- ▷ **General Recommendation:** Vote for shareholder proposals asking that a majority or more of directors be independent unless the board composition already meets the proposed threshold by ISS' definition of Independent Director (See [ISS' Classification of Directors](#).)

Vote for shareholder proposals asking that board audit, compensation, and/or nominating committees be composed exclusively of independent directors unless they currently meet that standard.

Majority Vote Standard for the Election of Directors

- ▷ **General Recommendation:** Generally vote for management proposals to adopt a majority of votes cast standard for directors in uncontested elections. Vote against if no carve-out for a plurality vote standard in contested elections is included.

Generally vote for precatory and binding shareholder resolutions requesting that the board change the company's bylaws to stipulate that directors need to be elected with an affirmative majority of votes cast, provided it does not conflict with the state law where the company is incorporated. Binding resolutions need to allow for a carve-out for a plurality vote standard when there are more nominees than board seats.

Companies are strongly encouraged to also adopt a post-election policy (also known as a director resignation policy) that will provide guidelines so that the company will promptly address the situation of a holdover director.

Proxy Access

- ▷ **General Recommendation:** Generally vote for management and shareholder proposals for proxy access with the following provisions:
- **Ownership threshold:** maximum requirement not more than three percent (3%) of the voting power;
 - **Ownership duration:** maximum requirement not longer than three (3) years of continuous ownership for each member of the nominating group;
 - **Aggregation:** minimal or no limits on the number of shareholders permitted to form a nominating group;
 - **Cap:** cap on nominees of generally twenty-five percent (25%) of the board.

Review for reasonableness any other restrictions on the right of proxy access.
Generally vote against proposals that are more restrictive than these guidelines.

Require More Nominees than Open Seats

- ▷ **General Recommendation:** Vote against shareholder proposals that would require a company to nominate more candidates than the number of open board seats.

Shareholder Engagement Policy (Shareholder Advisory Committee)

- ▷ **General Recommendation:** Generally vote for shareholder proposals requesting that the board establish an internal mechanism/process, which may include a committee, in order to improve communications between directors and shareholders, unless the company has the following features, as appropriate:
- Established a communication structure that goes beyond the exchange requirements to facilitate the exchange of information between shareholders and members of the board;
 - Effectively disclosed information with respect to this structure to its shareholders;
 - Company has not ignored majority-supported shareholder proposals, or a majority withhold vote on a director nominee; and

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- The company has an independent chair or a lead director, according to [ISS' definition](#). This individual must be made available for periodic consultation and direct communication with major shareholders.

2. Audit-Related

Auditor Indemnification and Limitation of Liability

➤ **General Recommendation:** Vote case-by-case on the issue of auditor indemnification and limitation of liability. Factors to be assessed include, but are not limited to:

- The terms of the auditor agreement—the degree to which these agreements impact shareholders' rights;
- The motivation and rationale for establishing the agreements;
- The quality of the company's disclosure; and
- The company's historical practices in the audit area.

Vote against or withhold from members of an audit committee in situations where there is persuasive evidence that the audit committee entered into an inappropriate indemnification agreement with its auditor that limits the ability of the company, or its shareholders, to pursue legitimate legal recourse against the audit firm.

Auditor Ratification

➤ **General Recommendation:** Vote for proposals to ratify auditors unless any of the following apply:

- An auditor has a financial interest in or association with the company, and is therefore not independent;
- There is reason to believe that the independent auditor has rendered an opinion that is neither accurate nor indicative of the company's financial position;
- Poor accounting practices are identified that rise to a serious level of concern, such as fraud or misapplication of GAAP; or
- Fees for non-audit services ("Other" fees) are excessive.

Non-audit fees are excessive if:

- Non-audit ("other") fees > audit fees + audit-related fees + tax compliance/preparation fees

Tax compliance and preparation include the preparation of original and amended tax returns and refund claims, and tax payment planning. All other services in the tax category, such as tax advice, planning, or consulting, should be added to "Other" fees. If the breakout of tax fees cannot be determined, add all tax fees to "Other" fees.

In circumstances where "Other" fees include fees related to significant one-time capital structure events (such as initial public offerings, bankruptcy emergence, and spin-offs) and the company makes public disclosure of the amount and nature of those fees that are an exception to the standard "non-audit fee" category, then such fees may be excluded from the non-audit fees considered in determining the ratio of non-audit to audit/audit-related fees/tax compliance and preparation for purposes of determining whether non-audit fees are excessive.

Shareholder Proposals Limiting Non-Audit Services

➤ **General Recommendation:** Vote case-by-case on shareholder proposals asking companies to prohibit or limit their auditors from engaging in non-audit services.

Shareholder Proposals on Audit Firm Rotation

➤ **General Recommendation:** Vote case-by-case on shareholder proposals asking for audit firm rotation, taking into account:

- The tenure of the audit firm;

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- The length of rotation specified in the proposal;
 - Any significant audit-related issues at the company;
 - The number of Audit Committee meetings held each year;
 - The number of financial experts serving on the committee; and
 - Whether the company has a periodic renewal process where the auditor is evaluated for both audit quality and competitive price.

3. Shareholder Rights & Defenses

Advance Notice Requirements for Shareholder Proposals/Nominations

- **General Recommendation:** Vote case-by-case on advance notice proposals, giving support to those proposals which allow shareholders to submit proposals/nominations as close to the meeting date as reasonably possible and within the broadest window possible, recognizing the need to allow sufficient notice for company, regulatory, and shareholder review.

To be reasonable, the company's deadline for shareholder notice of a proposal/nominations must be no earlier than 120 days prior to the anniversary of the previous year's meeting and have a submittal window of no shorter than 30 days from the beginning of the notice period (also known as a 90-120-day window). The submittal window is the period under which shareholders must file their proposals/nominations prior to the deadline.

In general, support additional efforts by companies to ensure full disclosure in regard to a proponent's economic and voting position in the company so long as the informational requirements are reasonable and aimed at providing shareholders with the necessary information to review such proposals.

Amend Bylaws without Shareholder Consent

- **General Recommendation:** Vote against proposals giving the board exclusive authority to amend the bylaws.

Vote case-by-case on proposals giving the board the ability to amend the bylaws in addition to shareholders, taking into account the following:

- Any impediments to shareholders' ability to amend the bylaws (i.e. supermajority voting requirements);
- The company's ownership structure and historical voting turnout;
- Whether the board could amend bylaws adopted by shareholders; and
- Whether shareholders would retain the ability to ratify any board-initiated amendments.

Control Share Acquisition Provisions

- **General Recommendation:** Vote for proposals to opt out of control share acquisition statutes unless doing so would enable the completion of a takeover that would be detrimental to shareholders.

Vote against proposals to amend the charter to include control share acquisition provisions.

Vote for proposals to restore voting rights to the control shares.

Control share acquisition statutes function by denying shares their voting rights when they contribute to ownership in excess of certain thresholds. Voting rights for those shares exceeding ownership limits may only be restored by approval of either a majority or supermajority of disinterested shares. Thus, control share acquisition statutes effectively require a hostile bidder to put its offer to a shareholder vote or risk voting disenfranchisement if the bidder continues buying up a large block of shares.

Control Share Cash-Out Provisions

- **General Recommendation:** Vote for proposals to opt out of control share cash-out statutes.

Control share cash-out statutes give dissident shareholders the right to "cash-out" of their position in a company at the expense of the shareholder who has taken a control position. In other words, when an investor crosses a

preset threshold level, remaining shareholders are given the right to sell their shares to the acquirer, who must buy them at the highest acquiring price.

Disgorgement Provisions

- ▷ **General Recommendation:** Vote for proposals to opt out of state disgorgement provisions.

Disgorgement provisions require an acquirer or potential acquirer of more than a certain percentage of a company's stock to disgorge, or pay back, to the company any profits realized from the sale of that company's stock purchased 24 months before achieving control status. All sales of company stock by the acquirer occurring within a certain period of time (between 18 months and 24 months) prior to the investor's gaining control status are subject to these recapture-of-profits provisions.

Fair Price Provisions

- ▷ **General Recommendation:** Vote case-by-case on proposals to adopt fair price provisions (provisions that stipulate that an acquirer must pay the same price to acquire all shares as it paid to acquire the control shares), evaluating factors such as the vote required to approve the proposed acquisition, the vote required to repeal the fair price provision, and the mechanism for determining the fair price.

Generally vote against fair price provisions with shareholder vote requirements greater than a majority of disinterested shares.

Freeze-Out Provisions

- ▷ **General Recommendation:** Vote for proposals to opt out of state freeze-out provisions. Freeze-out provisions force an investor who surpasses a certain ownership threshold in a company to wait a specified period of time before gaining control of the company.

Greenmail

- ▷ **General Recommendation:** Vote for proposals to adopt anti-greenmail charter or bylaw amendments or otherwise restrict a company's ability to make greenmail payments.

Vote case-by-case on anti-greenmail proposals when they are bundled with other charter or bylaw amendments.

Greenmail payments are targeted share repurchases by management of company stock from individuals or groups seeking control of the company. Since only the hostile party receives payment, usually at a substantial premium over the market value of its shares, the practice discriminates against all other shareholders.

Shareholder Litigation Rights

Federal Forum Selection Provisions

Federal forum selection provisions require that U.S. federal courts be the sole forum for shareholders to litigate claims arising under federal securities law.

- ▷ **General Recommendation:** Generally vote for federal forum selection provisions in the charter or bylaws that specify "the district courts of the United States" as the exclusive forum for federal securities law matters, in the absence of serious concerns about corporate governance or board responsiveness to shareholders.

Vote against provisions that restrict the forum to a particular federal district court; unilateral adoption (without a shareholder vote) of such a provision will generally be considered a one-time failure under the [Unilateral Bylaw/Charter Amendments](#) policy.

Exclusive Forum Provisions for State Law Matters

Exclusive forum provisions in the charter or bylaws restrict shareholders' ability to bring derivative lawsuits against the company, for claims arising out of state corporate law, to the courts of a particular state (generally the state of incorporation).

- **General Recommendation:** Generally vote for charter or bylaw provisions that specify courts located within the state of Delaware as the exclusive forum for corporate law matters for Delaware corporations, in the absence of serious concerns about corporate governance or board responsiveness to shareholders.

For states other than Delaware, vote case-by-case on exclusive forum provisions, taking into consideration:

- The company's stated rationale for adopting such a provision;
- Disclosure of past harm from duplicative shareholder lawsuits in more than one forum;
- The breadth of application of the charter or bylaw provision, including the types of lawsuits to which it would apply and the definition of key terms; and
- Governance features such as shareholders' ability to repeal the provision at a later date (including the vote standard applied when shareholders attempt to amend the charter or bylaws) and their ability to hold directors accountable through annual director elections and a majority vote standard in uncontested elections.

Generally vote against provisions that specify a state other than the state of incorporation as the exclusive forum for corporate law matters, or that specify a particular local court within the state; unilateral adoption of such a provision will generally be considered a one-time failure under the [Unilateral Bylaw/Charter Amendments](#) policy.

Fee shifting

Fee-shifting provisions in the charter or bylaws require that a shareholder who sues a company unsuccessfully pay all litigation expenses of the defendant corporation and its directors and officers.

- **General Recommendation:** Generally vote against provisions that mandate fee-shifting whenever plaintiffs are not completely successful on the merits (i.e., including cases where the plaintiffs are partially successful).

Unilateral adoption of a fee-shifting provision will generally be considered an ongoing failure under the [Unilateral Bylaw/Charter Amendments](#) policy.

Net Operating Loss (NOL) Protective Amendments

- **General Recommendation:** Vote against proposals to adopt a protective amendment for the stated purpose of protecting a company's net operating losses (NOL) if the effective term of the protective amendment would exceed the shorter of three years and the exhaustion of the NOL.

Vote case-by-case, considering the following factors, for management proposals to adopt an NOL protective amendment that would remain in effect for the shorter of three years (or less) and the exhaustion of the NOL:

- The ownership threshold (NOL protective amendments generally prohibit stock ownership transfers that would result in a new 5-percent holder or increase the stock ownership percentage of an existing 5-percent holder);
- The value of the NOLs;

- Shareholder protection mechanisms (sunset provision or commitment to cause expiration of the protective amendment upon exhaustion or expiration of the NOL);
- The company's existing governance structure including: board independence, existing takeover defenses, track record of responsiveness to shareholders, and any other problematic governance concerns; and
- Any other factors that may be applicable.

Poison Pills (Shareholder Rights Plans)

Shareholder Proposals to Put Pill to a Vote and/or Adopt a Pill Policy

➤ **General Recommendation:** Vote for shareholder proposals requesting that the company submit its poison pill to a shareholder vote or redeem it unless the company has: (1) A shareholder-approved poison pill in place; or (2) The company has adopted a policy concerning the adoption of a pill in the future specifying that the board will only adopt a shareholder rights plan if either:

- Shareholders have approved the adoption of the plan; or
- The board, in its exercise of its fiduciary responsibilities, determines that it is in the best interest of shareholders under the circumstances to adopt a pill without the delay in adoption that would result from seeking stockholder approval (i.e., the “fiduciary out” provision). A poison pill adopted under this fiduciary out will be put to a shareholder ratification vote within 12 months of adoption or expire. If the pill is not approved by a majority of the votes cast on this issue, the plan will immediately terminate.

If the shareholder proposal calls for a time period of less than 12 months for shareholder ratification after adoption, vote for the proposal, but add the caveat that a vote within 12 months would be considered sufficient implementation.

Management Proposals to Ratify a Poison Pill

➤ **General Recommendation:** Vote case-by-case on management proposals on poison pill ratification, focusing on the features of the shareholder rights plan. Rights plans should contain the following attributes:

- No lower than a 20 percent trigger, flip-in or flip-over;
- A term of no more than three years;
- No deadhand, slowhand, no-hand, or similar feature that limits the ability of a future board to redeem the pill;
- Shareholder redemption feature (qualifying offer clause); if the board refuses to redeem the pill 90 days after a qualifying offer is announced, 10 percent of the shares may call a special meeting or seek a written consent to vote on rescinding the pill.

In addition, the rationale for adopting the pill should be thoroughly explained by the company. In examining the request for the pill, take into consideration the company's existing governance structure, including: board independence, existing takeover defenses, and any problematic governance concerns.

Management Proposals to Ratify a Pill to Preserve Net Operating Losses (NOLs)

➤ **General Recommendation:** Vote against proposals to adopt a poison pill for the stated purpose of protecting a company's net operating losses (NOL) if the term of the pill would exceed the shorter of three years and the exhaustion of the NOL.

Vote case-by-case on management proposals for poison pill ratification, considering the following factors, if the term of the pill would be the shorter of three years (or less) and the exhaustion of the NOL:

- The ownership threshold to transfer (NOL pills generally have a trigger slightly below 5 percent);
- The value of the NOLs;
- Shareholder protection mechanisms (sunset provision, or commitment to cause expiration of the pill upon exhaustion or expiration of NOLs);

- The company's existing governance structure including: board independence, existing takeover defenses, track record of responsiveness to shareholders, and any other problematic governance concerns; and
- Any other factors that may be applicable.

Proxy Voting Disclosure, Confidentiality, and Tabulation

- **General Recommendation:** Vote case-by-case on proposals regarding proxy voting mechanics, taking into consideration whether implementation of the proposal is likely to enhance or protect shareholder rights. Specific issues covered under the policy include, but are not limited to, confidential voting of individual proxies and ballots, confidentiality of running vote tallies, and the treatment of abstentions and/or broker non-votes in the company's vote-counting methodology.

While a variety of factors may be considered in each analysis, the guiding principles are: transparency, consistency, and fairness in the proxy voting process. The factors considered, as applicable to the proposal, may include:

- The scope and structure of the proposal;
- The company's stated confidential voting policy (or other relevant policies) and whether it ensures a "level playing field" by providing shareholder proponents with equal access to vote information prior to the annual meeting;
- The company's vote standard for management and shareholder proposals and whether it ensures consistency and fairness in the proxy voting process and maintains the integrity of vote results;
- Whether the company's disclosure regarding its vote counting method and other relevant voting policies with respect to management and shareholder proposals are consistent and clear;
- Any recent controversies or concerns related to the company's proxy voting mechanics;
- Any unintended consequences resulting from implementation of the proposal; and
- Any other factors that may be relevant.

Ratification Proposals: Management Proposals to Ratify Existing Charter or Bylaw Provisions

- **General Recommendation:** Generally vote against management proposals to ratify provisions of the company's existing charter or bylaws, unless these governance provisions align with best practice.

In addition, voting against/withhold from individual directors, members of the governance committee, or the full board may be warranted, considering:

- The presence of a shareholder proposal addressing the same issue on the same ballot;
- The board's rationale for seeking ratification;
- Disclosure of actions to be taken by the board should the ratification proposal fail;
- Disclosure of shareholder engagement regarding the board's ratification request;
- The level of impairment to shareholders' rights caused by the existing provision;
- The history of management and shareholder proposals on the provision at the company's past meetings;
- Whether the current provision was adopted in response to the shareholder proposal;
- The company's ownership structure; and
- Previous use of ratification proposals to exclude shareholder proposals.

Reimbursing Proxy Solicitation Expenses

- **General Recommendation:** Vote case-by-case on proposals to reimburse proxy solicitation expenses.

When voting in conjunction with support of a dissident slate, vote for the reimbursement of all appropriate proxy solicitation expenses associated with the election.

Generally vote for shareholder proposals calling for the reimbursement of reasonable costs incurred in connection with nominating one or more candidates in a contested election where the following apply:

- The election of fewer than 50 percent of the directors to be elected is contested in the election;
- One or more of the dissident's candidates is elected;
- Shareholders are not permitted to cumulate their votes for directors; and
- The election occurred, and the expenses were incurred, after the adoption of this bylaw.

Reincorporation Proposals

➤ **General Recommendation:** Management or shareholder proposals to change a company's state of incorporation should be evaluated case-by-case, giving consideration to both financial and corporate governance concerns including the following:

- Reasons for reincorporation;
- Comparison of company's governance practices and provisions prior to and following the reincorporation; and
- Comparison of corporation laws of original state and destination state.

Vote for reincorporation when the economic factors outweigh any neutral or negative governance changes.

Shareholder Ability to Act by Written Consent

➤ **General Recommendation:** Generally vote against management and shareholder proposals to restrict or prohibit shareholders' ability to act by written consent.

Generally vote for management and shareholder proposals that provide shareholders with the ability to act by written consent, taking into account the following factors:

- Shareholders' current right to act by written consent;
- The consent threshold;
- The inclusion of exclusionary or prohibitive language;
- Investor ownership structure; and
- Shareholder support of, and management's response to, previous shareholder proposals.

Vote case-by-case on shareholder proposals if, in addition to the considerations above, the company has the following governance and antitakeover provisions:

- An unfettered¹³ right for shareholders to call special meetings at a 10 percent threshold;
- A majority vote standard in uncontested director elections;
- No non-shareholder-approved pill; and
- An annually elected board.

Shareholder Ability to Call Special Meetings

➤ **General Recommendation:** Vote against management or shareholder proposals to restrict or prohibit shareholders' ability to call special meetings.

Generally vote for management or shareholder proposals that provide shareholders with the ability to call special meetings taking into account the following factors:

- Shareholders' current right to call special meetings;
- Minimum ownership threshold necessary to call special meetings (10 percent preferred);
- The inclusion of exclusionary or prohibitive language;

¹³ "Unfettered" means no restrictions on agenda items, no restrictions on the number of shareholders who can group together to reach the 10 percent threshold, and only reasonable limits on when a meeting can be called: no greater than 30 days after the last annual meeting and no greater than 90 prior to the next annual meeting.

- Investor ownership structure; and
- Shareholder support of, and management's response to, previous shareholder proposals.

Stakeholder Provisions

- ▷ **General Recommendation:** Vote against proposals that ask the board to consider non-shareholder constituencies or other non-financial effects when evaluating a merger or business combination.

State Antitakeover Statutes

- ▷ **General Recommendation:** Vote case-by-case on proposals to opt in or out of state takeover statutes (including fair price provisions, stakeholder laws, poison pill endorsements, severance pay and labor contract provisions, and anti-greenmail provisions).

Supermajority Vote Requirements

- ▷ **General Recommendation:** Vote against proposals to require a supermajority shareholder vote.
- Vote for management or shareholder proposals to reduce supermajority vote requirements. However, for companies with shareholder(s) who have significant ownership levels, vote case-by-case, taking into account:
 - Ownership structure;
 - Quorum requirements; and
 - Vote requirements.

Virtual Shareholder Meetings

- ▷ **General Recommendation:** Generally vote for management proposals allowing for the convening of shareholder meetings by electronic means, so long as they do not preclude in-person meetings. Companies are encouraged to disclose the circumstances under which virtual-only¹⁴ meetings would be held, and to allow for comparable rights and opportunities for shareholders to participate electronically as they would have during an in-person meeting.

Vote case-by-case on shareholder proposals concerning virtual-only meetings, considering:

- Scope and rationale of the proposal; and
- Concerns identified with the company's prior meeting practices.

¹⁴ Virtual-only shareholder meeting" refers to a meeting of shareholders that is held exclusively using technology without a corresponding in-person meeting.

4. Capital/Restructuring

Capital

Adjustments to Par Value of Common Stock

- ▷ **General Recommendation:** Vote for management proposals to reduce the par value of common stock unless the action is being taken to facilitate an anti-takeover device or some other negative corporate governance action.

Vote for management proposals to eliminate par value.

Common Stock Authorization

General Authorization Requests

- ▷ **General Recommendation:** Vote case-by-case on proposals to increase the number of authorized shares of common stock that are to be used for general corporate purposes:
- If share usage (outstanding plus reserved) is less than 50% of the current authorized shares, vote for an increase of up to **50%** of current authorized shares.
 - If share usage is 50% to 100% of the current authorized, vote for an increase of up to **100%** of current authorized shares.
 - If share usage is greater than current authorized shares, vote for an increase of up to the current share usage.
 - In the case of a stock split, the allowable increase is calculated (per above) based on the post-split adjusted authorization.

Generally vote against proposed increases, even if within the above ratios, if the proposal or the company's prior or ongoing use of authorized shares is problematic, including, but not limited to:

- The proposal seeks to increase the number of authorized shares of the class of common stock that has superior voting rights to other share classes;
- On the same ballot is a proposal for a reverse split for which support is warranted despite the fact that it would result in an excessive increase in the share authorization;
- The company has a non-shareholder approved poison pill (including an NOL pill); or
- The company has previous sizeable placements (within the past 3 years) of stock with insiders at prices substantially below market value, or with problematic voting rights, without shareholder approval.

However, generally vote for proposed increases beyond the above ratios or problematic situations when there is disclosure of specific and severe risks to shareholders of not approving the request, such as:

- In, or subsequent to, the company's most recent 10-K filing, the company discloses that there is substantial doubt about its ability to continue as a going concern;
- The company states that there is a risk of imminent bankruptcy or imminent liquidation if shareholders do not approve the increase in authorized capital; or
- A government body has in the past year required the company to increase its capital ratios.

For companies incorporated in states that allow increases in authorized capital without shareholder approval, generally vote withhold or against all nominees if a unilateral capital authorization increase does not conform to the above policies.

Specific Authorization Requests

- **General Recommendation:** Generally vote for proposals to increase the number of authorized common shares where the primary purpose of the increase is to issue shares in connection with transaction(s) (such as acquisitions, SPAC transactions, private placements, or similar transactions) on the same ballot, or disclosed in the proxy statement, that warrant support. For such transactions, the allowable increase will be the greater of:
- twice the amount needed to support the transactions on the ballot, and
 - the allowable increase as calculated for general issuances above.

Dual Class Structure

- **General Recommendation:** Generally vote against proposals to create a new class of common stock unless:
- The company discloses a compelling rationale for the dual-class capital structure, such as:
 - The company's auditor has concluded that there is substantial doubt about the company's ability to continue as a going concern; or
 - The new class of shares will be transitory;
 - The new class is intended for financing purposes with minimal or no dilution to current shareholders in both the short term and long term; and
 - The new class is not designed to preserve or increase the voting power of an insider or significant shareholder.

Issue Stock for Use with Rights Plan

- **General Recommendation:** Vote against proposals that increase authorized common stock for the explicit purpose of implementing a non-shareholder-approved shareholder rights plan (poison pill).

Preemptive Rights

- **General Recommendation:** Vote case-by-case on shareholder proposals that seek preemptive rights, taking into consideration:
- The size of the company;
 - The shareholder base; and
 - The liquidity of the stock.

Preferred Stock Authorization

General Authorization Requests

- **General Recommendation:** Vote case-by-case on proposals to increase the number of authorized shares of preferred stock that are to be used for general corporate purposes:
- If share usage (outstanding plus reserved) is less than 50% of the current authorized shares, vote for an increase of up to **50%** of current authorized shares.
 - If share usage is 50% to 100% of the current authorized, vote for an increase of up to **100%** of current authorized shares.
 - If share usage is greater than current authorized shares, vote for an increase of up to the current share usage.
 - In the case of a stock split, the allowable increase is calculated (per above) based on the post-split adjusted authorization.
 - If no preferred shares are currently issued and outstanding, vote against the request, unless the company discloses a specific use for the shares.

Generally vote against proposed increases, even if within the above ratios, if the proposal or the company's prior or ongoing use of authorized shares is problematic, including, but not limited to:

- If the shares requested are blank check preferred shares that can be used for antitakeover purposes;¹⁵
- The company seeks to increase a class of non-convertible preferred shares entitled to more than one vote per share on matters that do not solely affect the rights of preferred stockholders "supervoting shares");
- The company seeks to increase a class of convertible preferred shares entitled to a number of votes greater than the number of common shares into which they are convertible ("supervoting shares") on matters that do not solely affect the rights of preferred stockholders;
- The stated intent of the increase in the general authorization is to allow the company to increase an existing designated class of supervoting preferred shares;
- On the same ballot is a proposal for a reverse split for which support is warranted despite the fact that it would result in an excessive increase in the share authorization;
- The company has a non-shareholder approved poison pill (including an NOL pill); or
- The company has previous sizeable placements (within the past 3 years) of stock with insiders at prices substantially below market value, or with problematic voting rights, without shareholder approval.

However, generally vote for proposed increases beyond the above ratios or problematic situations when there is disclosure of specific and severe risks to shareholders of not approving the request, such as:

- In, or subsequent to, the company's most recent 10-K filing, the company discloses that there is substantial doubt about its ability to continue as a going concern;
- The company states that there is a risk of imminent bankruptcy or imminent liquidation if shareholders do not approve the increase in authorized capital; or
- A government body has in the past year required the company to increase its capital ratios.

For companies incorporated in states that allow increases in authorized capital without shareholder approval, generally vote withhold or against all nominees if a unilateral capital authorization increase does not conform to the above policies.

Specific Authorization Requests

➤ **General Recommendation:** Generally vote for proposals to increase the number of authorized preferred shares where the primary purpose of the increase is to issue shares in connection with transaction(s) (such as acquisitions, SPAC transactions, private placements, or similar transactions) on the same ballot, or disclosed in the proxy statement, that warrant support. For such transactions, the allowable increase will be the greater of:

- twice the amount needed to support the transactions on the ballot, and
- the allowable increase as calculated for general issuances above.

Recapitalization Plans

➤ **General Recommendation:** Vote case-by-case on recapitalizations (reclassifications of securities), taking into account the following:

- More simplified capital structure;
- Enhanced liquidity;
- Fairness of conversion terms;
- Impact on voting power and dividends;
- Reasons for the reclassification;

¹⁵ To be acceptable, appropriate disclosure would be needed that the shares are "declawed": i.e., representation by the board that it will not, without prior stockholder approval, issue or use the preferred stock for any defensive or anti-takeover purpose or for the purpose of implementing any stockholder rights plan.

- Conflicts of interest; and
- Other alternatives considered.

Reverse Stock Splits

▷ **General Recommendation:** Vote for management proposals to implement a reverse stock split if:

- The number of authorized shares will be proportionately reduced; or
- The effective increase in authorized shares is equal to or less than the allowable increase calculated in accordance with ISS' Common Stock Authorization policy.

Vote case-by-case on proposals that do not meet either of the above conditions, taking into consideration the following factors:

- Stock exchange notification to the company of a potential delisting;
- Disclosure of substantial doubt about the company's ability to continue as a going concern without additional financing;
- The company's rationale; or
- Other factors as applicable.

Share Repurchase Programs

▷ **General Recommendation:** For U.S.-incorporated companies, and foreign-incorporated U.S. Domestic Issuers that are traded solely on U.S. exchanges, vote for management proposals to institute open-market share repurchase plans in which all shareholders may participate on equal terms, or to grant the board authority to conduct open-market repurchases, in the absence of company-specific concerns regarding:

- Greenmail,
- The use of buybacks to inappropriately manipulate incentive compensation metrics,
- Threats to the company's long-term viability, or
- Other company-specific factors as warranted.

Vote case-by-case on proposals to repurchase shares directly from specified shareholders, balancing the stated rationale against the possibility for the repurchase authority to be misused, such as to repurchase shares from insiders at a premium to market price.

Share Repurchase Programs Shareholder Proposals

▷ **General Recommendation:** Generally vote against shareholder proposals prohibiting executives from selling shares of company stock during periods in which the company has announced that it may or will be repurchasing shares of its stock. Vote for the proposal when there is a pattern of abuse by executives exercising options or selling shares during periods of share buybacks.

Stock Distributions: Splits and Dividends

▷ **General Recommendation:** Generally vote for management proposals to increase the common share authorization for stock split or stock dividend, provided that the effective increase in authorized shares is equal to or is less than the allowable increase calculated in accordance with ISS' Common Stock Authorization policy.

Tracking Stock

▷ **General Recommendation:** Vote case-by-case on the creation of tracking stock, weighing the strategic value of the transaction against such factors as:

- Adverse governance changes;
- Excessive increases in authorized capital stock;
- Unfair method of distribution;
- Diminution of voting rights;
- Adverse conversion features;
- Negative impact on stock option plans; and
- Alternatives such as spin-off.

Restructuring

Appraisal Rights

▷ **General Recommendation:** Vote for proposals to restore or provide shareholders with rights of appraisal.

Asset Purchases

▷ **General Recommendation:** Vote case-by-case on asset purchase proposals, considering the following factors:

- Purchase price;
- Fairness opinion;
- Financial and strategic benefits;
- How the deal was negotiated;
- Conflicts of interest;
- Other alternatives for the business;
- Non-completion risk.

Asset Sales

▷ **General Recommendation:** Vote case-by-case on asset sales, considering the following factors:

- Impact on the balance sheet/working capital;
- Potential elimination of diseconomies;
- Anticipated financial and operating benefits;
- Anticipated use of funds;
- Value received for the asset;
- Fairness opinion;
- How the deal was negotiated;
- Conflicts of interest.

Bundled Proposals

▷ **General Recommendation:** Vote case-by-case on bundled or “conditional” proxy proposals. In the case of items that are conditioned upon each other, examine the benefits and costs of the packaged items. In instances when the joint effect of the conditioned items is not in shareholders’ best interests, vote against the proposals. If the combined effect is positive, support such proposals.

Conversion of Securities

▷ **General Recommendation:** Vote case-by-case on proposals regarding conversion of securities. When evaluating these proposals, the investor should review the dilution to existing shareholders, the conversion price relative to market value, financial issues, control issues, termination penalties, and conflicts of interest.

Vote for the conversion if it is expected that the company will be subject to onerous penalties or will be forced to file for bankruptcy if the transaction is not approved.

Corporate Reorganization/Debt Restructuring/Prepackaged Bankruptcy Plans/Reverse Leveraged Buyouts/Wrap Plans

➤ **General Recommendation:** Vote case-by-case on proposals to increase common and/or preferred shares and to issue shares as part of a debt restructuring plan, after evaluating:

- Dilution to existing shareholders' positions;
- Terms of the offer - discount/premium in purchase price to investor, including any fairness opinion; termination penalties; exit strategy;
- Financial issues - company's financial situation; degree of need for capital; use of proceeds; effect of the financing on the company's cost of capital;
- Management's efforts to pursue other alternatives;
- Control issues - change in management; change in control, guaranteed board and committee seats; standstill provisions; voting agreements; veto power over certain corporate actions; and
- Conflict of interest - arm's length transaction, managerial incentives.

Vote for the debt restructuring if it is expected that the company will file for bankruptcy if the transaction is not approved.

Formation of Holding Company

➤ **General Recommendation:** Vote case-by-case on proposals regarding the formation of a holding company, taking into consideration the following:

- The reasons for the change;
- Any financial or tax benefits;
- Regulatory benefits;
- Increases in capital structure; and
- Changes to the articles of incorporation or bylaws of the company.

Absent compelling financial reasons to recommend for the transaction, vote against the formation of a holding company if the transaction would include either of the following:

- Increases in common or preferred stock in excess of the allowable maximum (see discussion under "Capital"); or
- Adverse changes in shareholder rights.

Going Private and Going Dark Transactions (LBOs and Minority Squeeze-outs)

➤ **General Recommendation:** Vote case-by-case on going private transactions, taking into account the following:

- Offer price/premium;
- Fairness opinion;
- How the deal was negotiated;
- Conflicts of interest;
- Other alternatives/offers considered; and
- Non-completion risk.

Vote case-by-case on going dark transactions, determining whether the transaction enhances shareholder value by taking into consideration:

- Whether the company has attained benefits from being publicly-traded (examination of trading volume, liquidity, and market research of the stock);
- Balanced interests of continuing vs. cashed-out shareholders, taking into account the following:
- Are all shareholders able to participate in the transaction?
- Will there be a liquid market for remaining shareholders following the transaction?
- Does the company have strong corporate governance?
- Will insiders reap the gains of control following the proposed transaction?
- Does the state of incorporation have laws requiring continued reporting that may benefit shareholders?

Joint Ventures

➤ **General Recommendation:** Vote case-by-case on proposals to form joint ventures, taking into account the following:

-
- Percentage of assets/business contributed;
- Percentage ownership;
- Financial and strategic benefits;
- Governance structure;
- Conflicts of interest;
- Other alternatives; and
- Non-completion risk.

Liquidations

➤ **General Recommendation:** Vote case-by-case on liquidations, taking into account the following:

- Management's efforts to pursue other alternatives;
- Appraisal value of assets; and
- The compensation plan for executives managing the liquidation.

Vote for the liquidation if the company will file for bankruptcy if the proposal is not approved.

Mergers and Acquisitions

➤ **General Recommendation:** Vote case-by-case on mergers and acquisitions. Review and evaluate the merits and drawbacks of the proposed transaction, balancing various and sometimes countervailing factors including:

- *Valuation* - Is the value to be received by the target shareholders (or paid by the acquirer) reasonable? While the fairness opinion may provide an initial starting point for assessing valuation reasonableness, emphasis is placed on the offer premium, market reaction, and strategic rationale.
- *Market reaction* - How has the market responded to the proposed deal? A negative market reaction should cause closer scrutiny of a deal.
- *Strategic rationale* - Does the deal make sense strategically? From where is the value derived? Cost and revenue synergies should not be overly aggressive or optimistic, but reasonably achievable. Management should also have a favorable track record of successful integration of historical acquisitions.
- *Negotiations and process* - Were the terms of the transaction negotiated at arm's-length? Was the process fair and equitable? A fair process helps to ensure the best price for shareholders. Significant negotiation "wins" can also signify the deal makers' competency. The comprehensiveness of the sales process (e.g., full auction, partial auction, no auction) can also affect shareholder value.
- *Conflicts of interest* - Are insiders benefiting from the transaction disproportionately and inappropriately as compared to non-insider shareholders? As the result of potential conflicts, the directors and officers of the company may be more likely to vote to approve a merger than if they did not hold these interests. Consider whether these interests may have influenced these directors and officers to support or recommend the

merger. The CIC figure presented in the "ISS Transaction Summary" section of this report is an aggregate figure that can in certain cases be a misleading indicator of the true value transfer from shareholders to insiders. Where such figure appears to be excessive, analyze the underlying assumptions to determine whether a potential conflict exists.

- *Governance* - Will the combined company have a better or worse governance profile than the current governance profiles of the respective parties to the transaction? If the governance profile is to change for the worse, the burden is on the company to prove that other issues (such as valuation) outweigh any deterioration in governance.

Private Placements/Warrants/Convertible Debentures




General Recommendation: Vote case-by-case on proposals regarding private placements, warrants, and convertible debentures taking into consideration:

- Dilution to existing shareholders' position: The amount and timing of shareholder ownership dilution should be weighed against the needs and proposed shareholder benefits of the capital infusion. Although newly issued common stock, absent preemptive rights, is typically dilutive to existing shareholders, share price appreciation is often the necessary event to trigger the exercise of "out of the money" warrants and convertible debt. In these instances from a value standpoint, the negative impact of dilution is mitigated by the increase in the company's stock price that must occur to trigger the dilutive event.
- Terms of the offer (discount/premium in purchase price to investor, including any fairness opinion, conversion features, termination penalties, exit strategy):
 - The terms of the offer should be weighed against the alternatives of the company and in light of company's financial condition. Ideally, the conversion price for convertible debt and the exercise price for warrants should be at a premium to the then prevailing stock price at the time of private placement.
 - When evaluating the magnitude of a private placement discount or premium, consider factors that influence the discount or premium, such as, liquidity, due diligence costs, control and monitoring costs, capital scarcity, information asymmetry, and anticipation of future performance.
- Financial issues:
 - The company's financial condition;
 - Degree of need for capital;
 - Use of proceeds;
 - Effect of the financing on the company's cost of capital;
 - Current and proposed cash burn rate;
 - Going concern viability and the state of the capital and credit markets.
- Management's efforts to pursue alternatives and whether the company engaged in a process to evaluate alternatives: A fair, unconstrained process helps to ensure the best price for shareholders. Financing alternatives can include joint ventures, partnership, merger, or sale of part or all of the company.
- Control issues:
 - Change in management;
 - Change in control;
 - Guaranteed board and committee seats;
 - Standstill provisions;
 - Voting agreements;
 - Veto power over certain corporate actions; and
 - Minority versus majority ownership and corresponding minority discount or majority control premium.

- Conflicts of interest:
 - Conflicts of interest should be viewed from the perspective of the company and the investor.
 - Were the terms of the transaction negotiated at arm's length? Are managerial incentives aligned with shareholder interests?
- Market reaction:
 - The market's response to the proposed deal. A negative market reaction is a cause for concern. Market reaction may be addressed by analyzing the one-day impact on the unaffected stock price.


Vote for the private placement, or for the issuance of warrants and/or convertible debentures in a private placement, if it is expected that the company will file for bankruptcy if the transaction is not approved.

Reorganization/Restructuring Plan (Bankruptcy)

 **General Recommendation:** Vote case-by-case on proposals to common shareholders on bankruptcy plans of reorganization, considering the following factors including, but not limited to:

- Estimated value and financial prospects of the reorganized company;
- Percentage ownership of current shareholders in the reorganized company;
- Whether shareholders are adequately represented in the reorganization process (particularly through the existence of an Official Equity Committee);
- The cause(s) of the bankruptcy filing, and the extent to which the plan of reorganization addresses the cause(s);
- Existence of a superior alternative to the plan of reorganization; and
- Governance of the reorganized company.

Special Purpose Acquisition Corporations (SPACs)

 **General Recommendation:** Vote case-by-case on SPAC mergers and acquisitions taking into account the following:

- *Valuation* - Is the value being paid by the SPAC reasonable? SPACs generally lack an independent fairness opinion and the financials on the target may be limited. Compare the conversion price with the intrinsic value of the target company provided in the fairness opinion. Also, evaluate the proportionate value of the combined entity attributable to the SPAC IPO shareholders versus the pre-merger value of SPAC. Additionally, a private company discount may be applied to the target if it is a private entity.
- *Market reaction* - How has the market responded to the proposed deal? A negative market reaction may be a cause for concern. Market reaction may be addressed by analyzing the one-day impact on the unaffected stock price.
- *Deal timing* - A main driver for most transactions is that the SPAC charter typically requires the deal to be complete within 18 to 24 months, or the SPAC is to be liquidated. Evaluate the valuation, market reaction, and potential conflicts of interest for deals that are announced close to the liquidation date.
- *Negotiations and process* - What was the process undertaken to identify potential target companies within specified industry or location specified in charter? Consider the background of the sponsors.
- *Conflicts of interest* - How are sponsors benefiting from the transaction compared to IPO shareholders? Potential conflicts could arise if a fairness opinion is issued by the insiders to qualify the deal rather than a third party or if management is encouraged to pay a higher price for the target because of an 80 percent rule (the charter requires that the fair market value of the target is at least equal to 80 percent of net assets of the SPAC). Also, there may be sense of urgency by the management team of the SPAC to close the deal since its charter typically requires a transaction to be completed within the 18-24-month timeframe.
- *Voting agreements* - Are the sponsors entering into any voting agreements/tender offers with shareholders who are likely to vote against the proposed merger or exercise conversion rights?
- *Governance* - What is the impact of having the SPAC CEO or founder on key committees following the proposed merger?

Special Purpose Acquisition Corporations (SPACs) - Proposals for Extensions

➤ **General Recommendation:** Vote case-by-case on SPAC extension proposals taking into account the length of the requested extension, the status of any pending transaction(s) or progression of the acquisition process, any added incentive for non-redeeming shareholders, and any prior extension requests.

- *Length of request:* Typically, extension requests range from two to six months, depending on the progression of the SPAC's acquisition process.
- *Pending transaction(s) or progression of the acquisition process:* Sometimes an initial business combination was already put to a shareholder vote, but, for varying reasons, the transaction could not be consummated by the termination date and the SPAC is requesting an extension. Other times, the SPAC has entered into a definitive transaction agreement, but needs additional time to consummate or hold the shareholder meeting.
- *Added incentive for non-redeeming shareholders:* Sometimes the SPAC sponsor (or other insiders) will contribute, typically as a loan to the company, additional funds that will be added to the redemption value of each public share as long as such shares are not redeemed in connection with the extension request. The purpose of the "equity kicker" is to incentivize shareholders to hold their shares through the end of the requested extension or until the time the transaction is put to a shareholder vote, rather than electing redemption at the extension proposal meeting.
- *Prior extension requests:* Some SPACs request additional time beyond the extension period sought in prior extension requests.

Spin-offs

➤ **General Recommendation:** Vote case-by-case on spin-offs, considering:

- Tax and regulatory advantages;
- Planned use of the sale proceeds;
- Valuation of spinoff;
- Fairness opinion;
- Benefits to the parent company;
- Conflicts of interest;
- Managerial incentives;
- Corporate governance changes;
- Changes in the capital structure.

Value Maximization Shareholder Proposals

➤ **General Recommendation:** Vote case-by-case on shareholder proposals seeking to maximize shareholder value by:

- Hiring a financial advisor to explore strategic alternatives;
- Selling the company; or
- Liquidating the company and distributing the proceeds to shareholders.

These proposals should be evaluated based on the following factors:

- Prolonged poor performance with no turnaround in sight;
- Signs of entrenched board and management (such as the adoption of takeover defenses);
- Strategic plan in place for improving value;
- Likelihood of receiving reasonable value in a sale or dissolution; and
- The company actively exploring its strategic options, including retaining a financial advisor.


5. Compensation

Executive Pay Evaluation

Underlying all evaluations are five global principles that most investors expect corporations to adhere to in designing and administering executive and director compensation programs:

1. **Maintain appropriate pay-for-performance alignment, with emphasis on long-term shareholder value:** This principle encompasses overall executive pay practices, which must be designed to attract, retain, and appropriately motivate the key employees who drive shareholder value creation over the long term. It will take into consideration, among other factors, the link between pay and performance; the mix between fixed and variable pay; performance goals; and equity-based plan costs;
2. **Avoid arrangements that risk “pay for failure”:** This principle addresses the appropriateness of long or indefinite contracts, excessive severance packages, and guaranteed compensation;
3. **Maintain an independent and effective compensation committee:** This principle promotes oversight of executive pay programs by directors with appropriate skills, knowledge, experience, and a sound process for compensation decision-making (e.g., including access to independent expertise and advice when needed);
4. **Provide shareholders with clear, comprehensive compensation disclosures:** This principle underscores the importance of informative and timely disclosures that enable shareholders to evaluate executive pay practices fully and fairly;
5. **Avoid inappropriate pay to non-executive directors:** This principle recognizes the interests of shareholders in ensuring that compensation to outside directors is reasonable and does not compromise their independence and ability to make appropriate judgments in overseeing managers’ pay and performance. At the market level, it may incorporate a variety of generally accepted best practices.

Advisory Votes on Executive Compensation—Management Proposals (Say-on-Pay)

 **General Recommendation:** Vote case-by-case on ballot items related to executive pay and practices, as well as certain aspects of outside director compensation.

Vote against Advisory Votes on Executive Compensation (Say-on-Pay or “SOP”) if:

- There is an unmitigated misalignment between CEO pay and company performance (pay for performance);
- The company maintains significant problematic pay practices;
- The board exhibits a significant level of [poor communication and responsiveness](#) to shareholders.

Vote against or withhold from the members of the Compensation Committee and potentially the full board if:

- There is no SOP on the ballot, and an against vote on an SOP would otherwise be warranted due to pay-for-performance misalignment, problematic pay practices, or the lack of adequate responsiveness on compensation issues raised previously, or a combination thereof;
- The board fails to respond adequately to a previous SOP proposal that received less than 70 percent support of votes cast;
- The company has recently practiced or approved problematic pay practices, such as option repricing or option backdating; or
- The situation is egregious.

Primary Evaluation Factors for Executive Pay

Pay-for-Performance Evaluation

ISS annually conducts a pay-for-performance analysis to identify strong or satisfactory alignment between pay and performance over a sustained period. With respect to companies in the S&P1500, Russell 3000, or Russell 3000E Indices¹⁶, this analysis considers the following:

1. Peer Group¹⁷ Alignment:
 - The degree of alignment between the company's annualized TSR rank and the CEO's annualized total pay rank within a peer group, each measured over a three-year period.
 - The rankings of CEO total pay and company financial performance within a peer group, each measured over a three-year period.
 - The multiple of the CEO's total pay relative to the peer group median in the most recent fiscal year.
2. Absolute Alignment¹⁸ – the absolute alignment between the trend in CEO pay and company TSR over the prior five fiscal years – i.e., the difference between the trend in annual pay changes and the trend in annualized TSR during the period.

If the above analysis demonstrates significant unsatisfactory long-term pay-for-performance alignment or, in the case of companies outside the Russell indices, a misalignment between pay and performance is otherwise suggested, our analysis may include any of the following qualitative factors, as relevant to an evaluation of how various pay elements may work to encourage or to undermine long-term value creation and alignment with shareholder interests:

- The ratio of performance- to time-based incentive awards;
- The overall ratio of performance-based compensation to fixed or discretionary pay;
- The rigor of performance goals;
- The complexity and risks around pay program design;
- The transparency and clarity of disclosure;
- The company's peer group benchmarking practices;
- Financial/operational results, both absolute and relative to peers;
- Special circumstances related to, for example, a new CEO in the prior FY or anomalous equity grant practices (e.g., bi-annual awards);
- Realizable pay¹⁹ compared to grant pay; and
- Any other factors deemed relevant.

Problematic Pay Practices

The focus is on executive compensation practices that contravene the global pay principles, including:

- Problematic practices related to non-performance-based compensation elements;

¹⁶ The [Russell 3000E](#) Index includes approximately 4,000 of the largest U.S. equity securities.

¹⁷ The revised peer group is generally comprised of 14-24 companies that are selected using market cap, revenue (or assets for certain financial firms), GICS industry group, and company's selected peers' GICS industry group, with size constraints, via a process designed to select peers that are comparable to the subject company in terms of revenue/assets and industry, and also within a market-cap bucket that is reflective of the company's market cap. For Oil, Gas & Consumable Fuels companies, market cap is the only size determinant.

¹⁸ Only Russell 3000 Index companies are subject to the Absolute Alignment analysis.

¹⁹ ISS research reports include realizable pay for S&P1500 companies.

- Incentives that may motivate excessive risk-taking or present a windfall risk; and
- Pay decisions that circumvent pay-for-performance, such as options backdating or waiving performance requirements.

Problematic Pay Practices related to Non-Performance-Based Compensation Elements

Pay elements that are not directly based on performance are generally evaluated case-by-case considering the context of a company's overall pay program and demonstrated pay-for-performance philosophy. Please refer to ISS' [U.S. Compensation Policies FAQ](#) document for detail on specific pay practices that have been identified as potentially problematic and may lead to negative recommendations if they are deemed to be inappropriate or unjustified relative to executive pay best practices. The list below highlights the problematic practices that carry significant weight in this overall consideration and may result in adverse vote recommendations:

- Repricing or replacing of underwater stock options/SARs without prior shareholder approval (including cash buyouts and voluntary surrender of underwater options);
- Extraordinary perquisites or tax gross-ups;
- New or materially amended agreements that provide for:
 - Excessive termination or CIC severance payments (generally exceeding 3 times base salary and average/target/most recent bonus);
 - CIC severance payments without involuntary job loss or substantial diminution of duties ("single" or "modified single" triggers) or in connection with a problematic Good Reason definition;
 - CIC excise tax gross-up entitlements (including "modified" gross-ups);
 - Multi-year guaranteed awards that are not at risk due to rigorous performance conditions;
- Liberal CIC definition combined with any single-trigger CIC benefits;
- Insufficient executive compensation disclosure by externally-managed issuers (EMIs) such that a reasonable assessment of pay programs and practices applicable to the EMI's executives is not possible;
- Any other provision or practice deemed to be egregious and present a significant risk to investors.

Options Backdating

The following factors should be examined case-by-case to allow for distinctions to be made between "sloppy" plan administration versus deliberate action or fraud:

- Reason and motive for the options backdating issue, such as inadvertent vs. deliberate grant date changes;
- Duration of options backdating;
- Size of restatement due to options backdating;
- Corrective actions taken by the board or compensation committee, such as canceling or re-pricing backdated options, the recouping of option gains on backdated grants; and
- Adoption of a grant policy that prohibits backdating and creates a fixed grant schedule or window period for equity grants in the future.

Compensation Committee Communications and Responsiveness

Consider the following factors case-by-case when evaluating ballot items related to executive pay on the board's responsiveness to investor input and engagement on compensation issues:

- Failure to respond to majority-supported shareholder proposals on executive pay topics; or
- Failure to adequately respond to the company's previous say-on-pay proposal that received the support of less than 70 percent of votes cast, taking into account:
 - Disclosure of engagement efforts with major institutional investors, including the frequency and timing of engagements and the company participants (including whether independent directors participated);

- Disclosure of the specific concerns voiced by dissenting shareholders that led to the say-on-pay opposition;
- Disclosure of specific and meaningful actions taken to address shareholders' concerns;
- Other recent compensation actions taken by the company;
- Whether the issues raised are recurring or isolated;
- The company's ownership structure; and
- Whether the support level was less than 50 percent, which would warrant the highest degree of responsiveness.

Frequency of Advisory Vote on Executive Compensation ("Say When on Pay")

- ▶ **General Recommendation:** Vote for annual advisory votes on compensation, which provide the most consistent and clear communication channel for shareholder concerns about companies' executive pay programs.

Voting on Golden Parachutes in an Acquisition, Merger, Consolidation, or Proposed Sale

- ▶ **General Recommendation:** Vote case-by-case on say on Golden Parachute proposals, including consideration of existing change-in-control arrangements maintained with named executive officers but also considering new or extended arrangements.

Features that may result in an "against" recommendation include one or more of the following, depending on the number, magnitude, and/or timing of issue(s):

- Single- or modified-single-trigger cash severance;
- Single-trigger acceleration of unvested equity awards;
- Full acceleration of equity awards granted shortly before the change in control;
- Acceleration of performance awards above the target level of performance without compelling rationale;
- Excessive cash severance (generally >3x base salary and bonus);
- Excise tax gross-ups triggered and payable;
- Excessive golden parachute payments (on an absolute basis or as a percentage of transaction equity value); or
- Recent amendments that incorporate any problematic features (such as those above) or recent actions (such as extraordinary equity grants) that may make packages so attractive as to influence merger agreements that may not be in the best interests of shareholders; or
- The company's assertion that a proposed transaction is conditioned on shareholder approval of the golden parachute advisory vote.

Recent amendment(s) that incorporate problematic features will tend to carry more weight on the overall analysis. However, the presence of multiple legacy problematic features will also be closely scrutinized.

In cases where the golden parachute vote is incorporated into a company's advisory vote on compensation (management say-on-pay), ISS will evaluate the say-on-pay proposal in accordance with these guidelines, which may give higher weight to that component of the overall evaluation.

Equity-Based and Other Incentive Plans

Please refer to ISS' [U.S. Equity Compensation Plans FAQ](#) document for additional details on the Equity Plan Scorecard policy.

▶ **General Recommendation:** Vote case-by-case on certain equity-based compensation plans²⁰ depending on a combination of certain plan features and equity grant practices, where positive factors may counterbalance negative factors, and vice versa, as evaluated using an "Equity Plan Scorecard" (EPSC) approach with three pillars:

- **Plan Cost:** The total estimated cost of the company's equity plans relative to industry/market cap peers, measured by the company's estimated Shareholder Value Transfer (SVT) in relation to peers and considering both:
 - SVT based on new shares requested plus shares remaining for future grants, plus outstanding unvested/unexercised grants; and
 - SVT based only on new shares requested plus shares remaining for future grants.
- **Plan Features:**
 - Quality of disclosure around vesting upon a change in control (CIC);
 - Discretionary vesting authority;
 - Liberal share recycling on various award types;
 - Lack of minimum vesting period for grants made under the plan;
 - Dividends payable prior to award vesting.
- **Grant Practices:**
 - The company's three-year burn rate relative to its industry/market cap peers;
 - Vesting requirements in CEO's recent equity grants (3-year look-back);
 - The estimated duration of the plan (based on the sum of shares remaining available and the new shares requested, divided by the average annual shares granted in the prior three years);
 - The proportion of the CEO's most recent equity grants/awards subject to performance conditions;
 - Whether the company maintains a sufficient claw-back policy;
 - Whether the company maintains sufficient post-exercise/vesting share-holding requirements.

Generally vote against the plan proposal if the combination of above factors indicates that the plan is not, overall, in shareholders' interests, or if any of the following egregious factors ("overriding factors") apply:

- Awards may vest in connection with a liberal change-of-control definition;
- The plan would permit repricing or cash buyout of underwater options without shareholder approval (either by expressly permitting it – for NYSE and Nasdaq listed companies – or by not prohibiting it when the company has a history of repricing – for non-listed companies);
- The plan is a vehicle for problematic pay practices or a significant pay-for-performance disconnect under certain circumstances;
- The plan is excessively dilutive to shareholders' holdings;
- The plan contains an evergreen (automatic share replenishment) feature; or
- Any other plan features are determined to have a significant negative impact on shareholder interests.

Further Information on certain EPSC Factors:

Shareholder Value Transfer (SVT)

The cost of the equity plans is expressed as Shareholder Value Transfer (SVT), which is measured using a binomial option pricing model that assesses the amount of shareholders' equity flowing out of the company to employees and directors. SVT is expressed as both a dollar amount and as a percentage of market value, and includes the new

²⁰ Proposals evaluated under the EPSC policy generally include those to approve or amend (1) stock option plans for employees and/or employees and directors, (2) restricted stock plans for employees and/or employees and directors, and (3) omnibus stock incentive plans for employees and/or employees and directors; amended plans will be further evaluated case-by-case.

shares proposed, shares available under existing plans, and shares granted but unexercised (using two measures, in the case of plans subject to the Equity Plan Scorecard evaluation, as noted above). All award types are valued. For omnibus plans, unless limitations are placed on the most expensive types of awards (for example, full-value awards), the assumption is made that all awards to be granted will be the most expensive types.

For proposals that are not subject to the Equity Plan Scorecard evaluation, Shareholder Value Transfer is reasonable if it falls below a company-specific benchmark. The benchmark is determined as follows: The top quartile performers in each industry group (using the Global Industry Classification Standard: GICS) are identified. Benchmark SVT levels for each industry are established based on these top performers' historic SVT. Regression analyses are run on each industry group to identify the variables most strongly correlated to SVT. The benchmark industry SVT level is then adjusted upwards or downwards for the specific company by plugging the company-specific performance measures, size, and cash compensation into the industry cap equations to arrive at the company's benchmark.²¹

Three-Year Burn Rate

For meetings held prior to February 1, 2023, burn-rate benchmarks (utilized in Equity Plan Scorecard evaluations) are calculated as the greater of: (1) the mean (μ) plus one standard deviation (σ) of the company's GICS group segmented by S&P 500, Russell 3000 index (less the S&P500), and non-Russell 3000 index; and (2) two percent of weighted common shares outstanding. In addition, year-over-year burn-rate benchmark changes will be limited to a maximum of two (2) percentage points plus or minus the prior year's burn-rate benchmark. See the [U.S. Equity Compensation Plans FAQ](#) for the benchmarks.

For meetings held prior to February 1, 2023, a company's adjusted burn rate is calculated as follows:

Burn Rate = (# of appreciation awards granted + # of full value awards granted * Volatility Multiplier) / Weighted average common shares outstanding

The Volatility Multiplier is used to provide more equivalent valuation between stock options and full value shares, based on the company's historical stock price volatility.

Effective for meetings held on or after February 1, 2023, a "Value-Adjusted Burn Rate" will instead be used for stock plan evaluations. Value-Adjusted Burn Rate benchmarks will be calculated as the greater of: (1) an industry-specific threshold based on three-year burn rates within the company's GICS group segmented by S&P 500, Russell 3000 index (less the S&P 500) and non-Russell 3000 index; and (2) a de minimis threshold established separately for each of the S&P 500, the Russell 3000 index less the S&P 500, and the non-Russell 3000 index. Year-over-year burn-rate benchmark changes will be limited to a predetermined range above or below the prior year's burn-rate benchmark.

The Value-Adjusted Burn Rate will be calculated as follows:

Value-Adjusted Burn Rate = ((# of options * option's dollar value using a Black-Scholes model) + (# of full-value awards * stock price)) / (Weighted average common shares * stock price).

²¹ For plans evaluated under the Equity Plan Scorecard policy, the company's SVT benchmark is considered along with other factors.

Egregious Factors

Liberal Change in Control Definition

Generally vote against equity plans if the plan has a liberal definition of change in control and the equity awards could vest upon such liberal definition of change in control, even though an actual change in control may not occur. Examples of such a definition include, but are not limited to, announcement or commencement of a tender offer, provisions for acceleration upon a “potential” takeover, shareholder approval of a merger or other transactions, or similar language.

Repricing Provisions

Vote against plans that expressly permit the repricing or exchange of underwater stock options/stock appreciate rights (SARs) without prior shareholder approval. “Repricing” typically includes the ability to do any of the following:

- Amend the terms of outstanding options or SARs to reduce the exercise price of such outstanding options or SARs;
- Cancel outstanding options or SARs in exchange for options or SARs with an exercise price that is less than the exercise price of the original options or SARs;
- Cancel underwater options in exchange for stock awards; or
- Provide cash buyouts of underwater options.

While the above cover most types of repricing, ISS may view other provisions as akin to repricing depending on the facts and circumstances.

Also, vote against or withhold from members of the Compensation Committee who approved repricing (as defined above or otherwise determined by ISS), without prior shareholder approval, even if such repricings are allowed in their equity plan.

Vote against plans that do not expressly prohibit repricing or cash buyout of underwater options without shareholder approval if the company has a history of repricing/buyouts without shareholder approval, and the applicable listing standards would not preclude them from doing so.

Problematic Pay Practices or Significant Pay-for-Performance Disconnect

If the equity plan on the ballot is a vehicle for [problematic pay practices](#), vote against the plan.

ISS may recommend a vote against the equity plan if the plan is determined to be a vehicle for pay-for-performance misalignment. Considerations in voting against the equity plan may include, but are not limited to:

- Severity of the pay-for-performance misalignment;
- Whether problematic equity grant practices are driving the misalignment; and/or
- Whether equity plan awards have been heavily concentrated to the CEO and/or the other NEOs.

Amending Cash and Equity Plans (including Approval for Tax Deductibility (162(m)))



General Recommendation: Vote case-by-case on amendments to cash and equity incentive plans.

Generally vote for proposals to amend executive cash, stock, or cash and stock incentive plans if the proposal:

- Addresses administrative features only; or

- Seeks approval for Section 162(m) purposes only, and the plan administering committee consists entirely of independent directors, per [ISS' Classification of Directors](#). Note that if the company is presenting the plan to shareholders for the first time for any reason (including after the company's initial public offering), or if the proposal is bundled with other material plan amendments, then the recommendation will be case-by-case (see below).

Vote against proposals to amend executive cash, stock, or cash and stock incentive plans if the proposal:

- Seeks approval for Section 162(m) purposes only, and the plan administering committee does not consist entirely of independent directors, per [ISS' Classification of Directors](#).

Vote case-by-case on all other proposals to amend cash incentive plans. This includes plans presented to shareholders for the first time after the company's IPO and/or proposals that bundle material amendment(s) other than those for Section 162(m) purposes.

Vote case-by-case on all other proposals to amend equity incentive plans, considering the following:

- If the proposal requests additional shares and/or the amendments include a term extension or addition of full value awards as an award type, the recommendation will be based on the Equity Plan Scorecard evaluation as well as an analysis of the overall impact of the amendments.
- If the plan is being presented to shareholders for the first time (including after the company's IPO), whether or not additional shares are being requested, the recommendation will be based on the Equity Plan Scorecard evaluation as well as an analysis of the overall impact of any amendments.
- If there is no request for additional shares and the amendments do not include a term extension or addition of full value awards as an award type, then the recommendation will be based entirely on an analysis of the overall impact of the amendments, and the EPSC evaluation will be shown only for informational purposes.

In the first two case-by-case evaluation scenarios, the EPSC evaluation/score is the more heavily weighted consideration.

Specific Treatment of Certain Award Types in Equity Plan Evaluations

Dividend Equivalent Rights

Options that have Dividend Equivalent Rights (DERs) associated with them will have a higher calculated award value than those without DERs under the binomial model, based on the value of these dividend streams. The higher value will be applied to new shares, shares available under existing plans, and shares awarded but not exercised per the plan specifications. DERS transfer more shareholder equity to employees and non-employee directors and this cost should be captured.

Operating Partnership (OP) Units in Equity Plan Analysis of Real Estate Investment Trusts (REITs)

For Real Estate Investment Trusts (REITs), include the common shares issuable upon conversion of outstanding Operating Partnership (OP) units in the share count for the purposes of determining: (1) market capitalization in the Shareholder Value Transfer (SVT) analysis and (2) shares outstanding in the burn rate analysis.

Other Compensation Plans

401(k) Employee Benefit Plans



General Recommendation: Vote for proposals to implement a 401(k) savings plan for employees.

Employee Stock Ownership Plans (ESOPs)

- ▷ **General Recommendation:** Vote for proposals to implement an ESOP or increase authorized shares for existing ESOPs, unless the number of shares allocated to the ESOP is excessive (more than five percent of outstanding shares).

Employee Stock Purchase Plans—Qualified Plans

- ▷ **General Recommendation:** Vote case-by-case on qualified employee stock purchase plans. Vote for employee stock purchase plans where all of the following apply:

- Purchase price is at least 85 percent of fair market value;
- Offering period is 27 months or less; and
- The number of shares allocated to the plan is 10 percent or less of the outstanding shares.

Vote against qualified employee stock purchase plans where when the plan features do not meet all of the above criteria.

Employee Stock Purchase Plans—Non-Qualified Plans

- ▷ **General Recommendation:** Vote case-by-case on nonqualified employee stock purchase plans. Vote for nonqualified employee stock purchase plans with all the following features:

- Broad-based participation;
- Limits on employee contribution, which may be a fixed dollar amount or expressed as a percent of base salary;
- Company matching contribution up to 25 percent of employee's contribution, which is effectively a discount of 20 percent from market value; and
- No discount on the stock price on the date of purchase when there is a company matching contribution.

Vote against nonqualified employee stock purchase plans when the plan features do not meet all of the above criteria. If the matching contribution or effective discount exceeds the above, ISS may evaluate the SVT cost of the plan as part of the assessment.

Option Exchange Programs/Repricing Options

- ▷ **General Recommendation:** Vote case-by-case on management proposals seeking approval to exchange/reprice options taking into consideration:

- Historic trading patterns--the stock price should not be so volatile that the options are likely to be back "in-the-money" over the near term;
- Rationale for the re-pricing--was the stock price decline beyond management's control?;
- Is this a value-for-value exchange?;
- Are surrendered stock options added back to the plan reserve?;
- Timing--repricing should occur at least one year out from any precipitous drop in company's stock price;
- Option vesting--does the new option vest immediately or is there a black-out period?;
- Term of the option--the term should remain the same as that of the replaced option;
- Exercise price--should be set at fair market or a premium to market;
- Participants--executive officers and directors must be excluded.

If the surrendered options are added back to the equity plans for re-issuance, then also take into consideration the company's total cost of equity plans and its three-year average burn rate.

In addition to the above considerations, evaluate the intent, rationale, and timing of the repricing proposal. The proposal should clearly articulate why the board is choosing to conduct an exchange program at this point in time. Repricing underwater options after a recent precipitous drop in the company's stock price demonstrates poor timing and warrants additional scrutiny. Also, consider the terms of the surrendered options, such as the grant date, exercise price and vesting schedule. Grant dates of surrendered options should be far enough back (two to

three years) so as not to suggest that repricings are being done to take advantage of short-term downward price movements. Similarly, the exercise price of surrendered options should be above the 52-week high for the stock price.

Vote for shareholder proposals to put option repricings to a shareholder vote.

Stock Plans in Lieu of Cash

➤ **General Recommendation:** Vote case-by-case on plans that provide participants with the option of taking all or a portion of their cash compensation in the form of stock.

Vote for non-employee director-only equity plans that provide a dollar-for-dollar cash-for-stock exchange.

Vote case-by-case on plans which do not provide a dollar-for-dollar cash for stock exchange. In cases where the exchange is not dollar-for-dollar, the request for new or additional shares for such equity program will be considered using the binomial option pricing model. In an effort to capture the total cost of total compensation, ISS will not make any adjustments to carve out the in-lieu-of cash compensation.

Transfer Stock Option (TSO) Programs

➤ **General Recommendation:** One-time Transfers: Vote against or withhold from compensation committee members if they fail to submit one-time transfers to shareholders for approval.

Vote case-by-case on one-time transfers. Vote for if:

- Executive officers and non-employee directors are excluded from participating;
- Stock options are purchased by third-party financial institutions at a discount to their fair value using option pricing models such as Black-Scholes or a Binomial Option Valuation or other appropriate financial models; and
- There is a two-year minimum holding period for sale proceeds (cash or stock) for all participants.

Additionally, management should provide a clear explanation of why options are being transferred to a third-party institution and whether the events leading up to a decline in stock price were beyond management's control. A review of the company's historic stock price volatility should indicate if the options are likely to be back "in-the-money" over the near term.

Ongoing TSO program: Vote against equity plan proposals if the details of ongoing TSO programs are not provided to shareholders. Since TSOs will be one of the award types under a stock plan, the ongoing TSO program, structure, and mechanics must be disclosed to shareholders. The specific criteria to be considered in evaluating these proposals include, but not limited to, the following:

- Eligibility;
- Vesting;
- Bid-price;
- Term of options;
- Cost of the program and impact of the TSOs on company's total option expense; and
- Option repricing policy.

Amendments to existing plans that allow for introduction of transferability of stock options should make clear that only options granted post-amendment shall be transferable.

Director Compensation

Shareholder Ratification of Director Pay Programs

▷ **General Recommendation:** Vote case-by-case on management proposals seeking ratification of non-employee director compensation, based on the following factors:

- If the equity plan under which non-employee director grants are made is on the ballot, whether or not it warrants support; and
- An assessment of the following qualitative factors:
 - The relative magnitude of director compensation as compared to companies of a similar profile;
 - The presence of problematic pay practices relating to director compensation;
 - Director stock ownership guidelines and holding requirements;
 - Equity award vesting schedules;
 - The mix of cash and equity-based compensation;
 - Meaningful limits on director compensation;
 - The availability of retirement benefits or perquisites; and
 - The quality of disclosure surrounding director compensation.

Equity Plans for Non-Employee Directors

▷ **General Recommendation:** Vote case-by-case on compensation plans for non-employee directors, based on:

- The total estimated cost of the company's equity plans relative to industry/market cap peers, measured by the company's estimated Shareholder Value Transfer (SVT) based on new shares requested plus shares remaining for future grants, plus outstanding unvested/unexercised grants;
- The company's three-year burn rate relative to its industry/market cap peers (in certain circumstances); and
- The presence of any egregious plan features (such as an option repricing provision or liberal CIC vesting risk).

On occasion, non-employee director stock plans will exceed the plan cost or burn-rate benchmarks when combined with employee or executive stock plans. In such cases, vote case-by-case on the plan taking into consideration the following qualitative factors:

- The relative magnitude of director compensation as compared to companies of a similar profile;
- The presence of problematic pay practices relating to director compensation;
- Director stock ownership guidelines and holding requirements;
- Equity award vesting schedules;
- The mix of cash and equity-based compensation;
- Meaningful limits on director compensation;
- The availability of retirement benefits or perquisites; and
- The quality of disclosure surrounding director compensation.

Non-Employee Director Retirement Plans

▷ **General Recommendation:** Vote against retirement plans for non-employee directors. Vote for shareholder proposals to eliminate retirement plans for non-employee directors.

Shareholder Proposals on Compensation

Bonus Banking/Bonus Banking “Plus”

- ▷ **General Recommendation:** Vote case-by-case on proposals seeking deferral of a portion of annual bonus pay, with ultimate payout linked to sustained results for the performance metrics on which the bonus was earned (whether for the named executive officers or a wider group of employees), taking into account the following factors:
- The company’s past practices regarding equity and cash compensation;
 - Whether the company has a holding period or stock ownership requirements in place, such as a meaningful retention ratio (at least 50 percent for full tenure); and
 - Whether the company has a rigorous claw-back policy in place.

Compensation Consultants—Disclosure of Board or Company’s Utilization

- ▷ **General Recommendation:** Generally vote for shareholder proposals seeking disclosure regarding the company, board, or compensation committee’s use of compensation consultants, such as company name, business relationship(s), and fees paid.

Disclosure/Setting Levels or Types of Compensation for Executives and Directors

- ▷ **General Recommendation:** Generally vote for shareholder proposals seeking additional disclosure of executive and director pay information, provided the information requested is relevant to shareholders' needs, would not put the company at a competitive disadvantage relative to its industry, and is not unduly burdensome to the company.

Generally vote against shareholder proposals seeking to set absolute levels on compensation or otherwise dictate the amount or form of compensation (such as types of compensation elements or specific metrics) to be used for executive or directors.

Generally vote against shareholder proposals that mandate a minimum amount of stock that directors must own in order to qualify as a director or to remain on the board.

Vote case-by-case on all other shareholder proposals regarding executive and director pay, taking into account relevant factors, including but not limited to: company performance, pay level and design versus peers, history of compensation concerns or pay-for-performance disconnect, and/or the scope and prescriptive nature of the proposal.

Golden Coffins/Executive Death Benefits

- ▷ **General Recommendation:** Generally vote for proposals calling for companies to adopt a policy of obtaining shareholder approval for any future agreements and corporate policies that could oblige the company to make payments or awards following the death of a senior executive in the form of unearned salary or bonuses, accelerated vesting or the continuation in force of unvested equity grants, perquisites and other payments or awards made in lieu of compensation. This would not apply to any benefit programs or equity plan proposals for which the broad-based employee population is eligible.

Hold Equity Past Retirement or for a Significant Period of Time

- ▷ **General Recommendation:** Vote case-by-case on shareholder proposals asking companies to adopt policies requiring senior executive officers to retain a portion of net shares acquired through compensation plans. The following factors will be taken into account:
- The percentage/ratio of net shares required to be retained;
 - The time period required to retain the shares;
 - Whether the company has equity retention, holding period, and/or stock ownership requirements in place and the robustness of such requirements;

- Whether the company has any other policies aimed at mitigating risk taking by executives;
- Executives' actual stock ownership and the degree to which it meets or exceeds the proponent's suggested holding period/retention ratio or the company's existing requirements; and
- Problematic pay practices, current and past, which may demonstrate a short-term versus long-term focus.

Pay Disparity

➤ **General Recommendation:** Vote case-by-case on proposals calling for an analysis of the pay disparity between corporate executives and other non-executive employees. The following factors will be considered:

- The company's current level of disclosure of its executive compensation setting process, including how the company considers pay disparity;
- If any problematic pay practices or pay-for-performance concerns have been identified at the company; and
- The level of shareholder support for the company's pay programs.

Generally vote against proposals calling for the company to use the pay disparity analysis or pay ratio in a specific way to set or limit executive pay.

Pay for Performance/Performance-Based Awards

➤ **General Recommendation:** Vote case-by-case on shareholder proposals requesting that a significant amount of future long-term incentive compensation awarded to senior executives shall be performance-based and requesting that the board adopt and disclose challenging performance metrics to shareholders, based on the following analytical steps:

- First, vote for shareholder proposals advocating the use of performance-based equity awards, such as performance contingent options or restricted stock, indexed options, or premium-priced options, unless the proposal is overly restrictive or if the company has demonstrated that it is using a "substantial" portion of performance-based awards for its top executives. Standard stock options and performance-accelerated awards do not meet the criteria to be considered as performance-based awards. Further, premium-priced options should have a meaningful premium to be considered performance-based awards.
- Second, assess the rigor of the company's performance-based equity program. If the bar set for the performance-based program is too low based on the company's historical or peer group comparison, generally vote for the proposal. Furthermore, if target performance results in an above target payout, vote for the shareholder proposal due to program's poor design. If the company does not disclose the performance metric of the performance-based equity program, vote for the shareholder proposal regardless of the outcome of the first step to the test.

In general, vote for the shareholder proposal if the company does not meet both of the above two steps.

Pay for Superior Performance

➤ **General Recommendation:** Vote case-by-case on shareholder proposals that request the board establish a pay-for-superior performance standard in the company's executive compensation plan for senior executives. These proposals generally include the following principles:


- Set compensation targets for the plan's annual and long-term incentive pay components at or below the peer group median;
- Deliver a majority of the plan's target long-term compensation through performance-vested, not simply time-vested, equity awards;
- Provide the strategic rationale and relative weightings of the financial and non-financial performance metrics or criteria used in the annual and performance-vested long-term incentive components of the plan;

- Establish performance targets for each plan financial metric relative to the performance of the company's peer companies;
- Limit payment under the annual and performance-vested long-term incentive components of the plan to when the company's performance on its selected financial performance metrics exceeds peer group median performance.

Consider the following factors in evaluating this proposal:


- What aspects of the company's annual and long-term equity incentive programs are performance driven?
- If the annual and long-term equity incentive programs are performance driven, are the performance criteria and hurdle rates disclosed to shareholders or are they benchmarked against a disclosed peer group?
- Can shareholders assess the correlation between pay and performance based on the current disclosure?
- What type of industry and stage of business cycle does the company belong to?

Pre-Arranged Trading Plans (10b5-1 Plans)


 **General Recommendation:** Generally vote for shareholder proposals calling for the addition of certain safeguards in prearranged trading plans (10b5-1 plans) for executives. Safeguards may include:

- Adoption, amendment, or termination of a 10b5-1 Plan must be disclosed in a Form 8-K;
- Amendment or early termination of a 10b5-1 Plan allowed only under extraordinary circumstances, as determined by the board;
- Request that a certain number of days that must elapse between adoption or amendment of a 10b5-1 Plan and initial trading under the plan;
- Reports on Form 4 must identify transactions made pursuant to a 10b5-1 Plan;
- An executive may not trade in company stock outside the 10b5-1 Plan;
- Trades under a 10b5-1 Plan must be handled by a broker who does not handle other securities transactions for the executive.

Prohibit Outside CEOs from Serving on Compensation Committees

 **General Recommendation:** Generally vote against proposals seeking a policy to prohibit any outside CEO from serving on a company's compensation committee, unless the company has demonstrated problematic pay practices that raise concerns about the performance and composition of the committee.

Recoupment of Incentive or Stock Compensation in Specified Circumstances

 **General Recommendation:** Vote case-by-case on proposals to recoup incentive cash or stock compensation made to senior executives if it is later determined that the figures upon which incentive compensation is earned turn out to have been in error, or if the senior executive has breached company policy or has engaged in misconduct that may be significantly detrimental to the company's financial position or reputation, or if the senior executive failed to manage or monitor risks that subsequently led to significant financial or reputational harm to the company. Many companies have adopted policies that permit recoupment in cases where an executive's fraud, misconduct, or negligence significantly contributed to a restatement of financial results that led to the awarding of unearned incentive compensation. However, such policies may be narrow given that not all misconduct or negligence may result in significant financial restatements. Misconduct, negligence, or lack of sufficient oversight by senior executives may lead to significant financial loss or reputational damage that may have long-lasting impact.

In considering whether to support such shareholder proposals, ISS will take into consideration the following factors:

- If the company has adopted a formal recoupment policy;
- The rigor of the recoupment policy focusing on how and under what circumstances the company may recoup incentive or stock compensation;

- Whether the company has chronic restatement history or material financial problems;
- Whether the company's policy substantially addresses the concerns raised by the proponent;
- Disclosure of recoupment of incentive or stock compensation from senior executives or lack thereof; or
- Any other relevant factors.

Severance Agreements for Executives/Golden Parachutes

- ▷ **General Recommendation:** Vote for shareholder proposals requiring that golden parachutes or executive severance agreements be submitted for shareholder ratification, unless the proposal requires shareholder approval *prior* to entering into employment contracts.

Vote case-by-case on proposals to ratify or cancel golden parachutes. An acceptable parachute should include, but is not limited to, the following:

- The triggering mechanism should be beyond the control of management;
- The amount should not exceed three times base amount (defined as the average annual taxable W-2 compensation during the five years prior to the year in which the change of control occurs);
- Change-in-control payments should be double-triggered, i.e., (1) after a change in control has taken place, and (2) termination of the executive as a result of the change in control. Change in control is defined as a change in the company ownership structure.

Share Buyback Impact on Incentive Program Metrics

- ▷ **General Recommendation:** Vote case-by-case on proposals requesting the company exclude the impact of share buybacks from the calculation of incentive program metrics, considering the following factors:

- The frequency and timing of the company's share buybacks;
- The use of per-share metrics in incentive plans;
- The effect of recent buybacks on incentive metric results and payouts; and
- Whether there is any indication of metric result manipulation.

Supplemental Executive Retirement Plans (SERPs)

- ▷ **General Recommendation:** Generally vote for shareholder proposals requesting to put extraordinary benefits contained in SERP agreements to a shareholder vote unless the company's executive pension plans do not contain excessive benefits beyond what is offered under employee-wide plans.

Generally vote for shareholder proposals requesting to limit the executive benefits provided under the company's supplemental executive retirement plan (SERP) by limiting covered compensation to a senior executive's annual salary or those pay elements covered for the general employee population.

Tax Gross-Up Proposals

- ▷ **General Recommendation:** Generally vote for proposals calling for companies to adopt a policy of not providing tax gross-up payments to executives, except in situations where gross-ups are provided pursuant to a plan, policy, or arrangement applicable to management employees of the company, such as a relocation or expatriate tax equalization policy.

Termination of Employment Prior to Severance Payment/Eliminating Accelerated Vesting of Unvested Equity

- ▷ **General Recommendation:** Vote case-by-case on shareholder proposals seeking a policy requiring termination of employment prior to severance payment and/or eliminating accelerated vesting of unvested equity.

The following factors will be considered:

- The company's current treatment of equity upon employment termination and/or in change-in-control situations (i.e., vesting is double triggered and/or pro rata, does it allow for the assumption of equity by acquiring company, the treatment of performance shares, etc.);
- Current employment agreements, including potential poor pay practices such as gross-ups embedded in those agreements.

Generally vote for proposals seeking a policy that prohibits automatic acceleration of the vesting of equity awards to senior executives upon a voluntary termination of employment or in the event of a change in control (except for pro rata vesting considering the time elapsed and attainment of any related performance goals between the award date and the change in control).

6. Routine/Miscellaneous

Adjourn Meeting

- ▶ **General Recommendation:** Generally vote against proposals to provide management with the authority to adjourn an annual or special meeting absent compelling reasons to support the proposal.

Vote for proposals that relate specifically to soliciting votes for a merger or transaction if supporting that merger or transaction. Vote against proposals if the wording is too vague or if the proposal includes "other business."

Amend Quorum Requirements

- ▶ **General Recommendation:** Vote against proposals to reduce quorum requirements for shareholder meetings below a majority of the shares outstanding unless there are compelling reasons to support the proposal.

Amend Minor Bylaws

- ▶ **General Recommendation:** Vote for bylaw or charter changes that are of a housekeeping nature (updates or corrections).

Change Company Name

- ▶ **General Recommendation:** Vote for proposals to change the corporate name unless there is compelling evidence that the change would adversely impact shareholder value.

Change Date, Time, or Location of Annual Meeting

- ▶ **General Recommendation:** Vote for management proposals to change the date, time, or location of the annual meeting unless the proposed change is unreasonable.

Vote against shareholder proposals to change the date, time, or location of the annual meeting unless the current scheduling or location is unreasonable.

Other Business

- ▶ **General Recommendation:** Vote against proposals to approve other business when it appears as a voting item.

7. Social and Environmental Issues

Global Approach

Issues covered under the policy include a wide range of topics, including consumer and product safety, environment and energy, labor standards and human rights, workplace and board diversity, and corporate political issues. While a variety of factors goes into each analysis, the overall principle guiding all vote recommendations focuses on how the proposal may enhance or protect shareholder value in either the short or long term.

- **General Recommendation:** Generally vote case-by-case, examining primarily whether implementation of the proposal is likely to enhance or protect shareholder value. The following factors will be considered:
- If the issues presented in the proposal are more appropriately or effectively dealt with through legislation or government regulation;
 - If the company has already responded in an appropriate and sufficient manner to the issue(s) raised in the proposal;
 - Whether the proposal's request is unduly burdensome (scope or timeframe) or overly prescriptive;
 - The company's approach compared with any industry standard practices for addressing the issue(s) raised by the proposal;
 - Whether there are significant controversies, fines, penalties, or litigation associated with the company's environmental or social practices;
 - If the proposal requests increased disclosure or greater transparency, whether reasonable and sufficient information is currently available to shareholders from the company or from other publicly available sources; and
 - If the proposal requests increased disclosure or greater transparency, whether implementation would reveal proprietary or confidential information that could place the company at a competitive disadvantage.

Endorsement of Principles

- **General Recommendation:** Generally vote against proposals seeking a company's endorsement of principles that support a particular public policy position. Endorsing a set of principles may require a company to take a stand on an issue that is beyond its own control and may limit its flexibility with respect to future developments. Management and the board should be afforded the flexibility to make decisions on specific public policy positions based on their own assessment of the most beneficial strategies for the company.

Animal Welfare

Animal Welfare Policies

- **General Recommendation:** Generally vote for proposals seeking a report on a company's animal welfare standards, or animal welfare-related risks, unless:
- The company has already published a set of animal welfare standards and monitors compliance;
 - The company's standards are comparable to industry peers; and
 - There are no recent significant fines, litigation, or controversies related to the company's and/or its suppliers' treatment of animals.

Animal Testing

➤ **General Recommendation:** Generally vote against proposals to phase out the use of animals in product testing, unless:

- The company is conducting animal testing programs that are unnecessary or not required by regulation;
- The company is conducting animal testing when suitable alternatives are commonly accepted and used by industry peers; or
- There are recent, significant fines or litigation related to the company's treatment of animals.

Animal Slaughter

➤ **General Recommendation:** Generally vote against proposals requesting the implementation of Controlled Atmosphere Killing (CAK) methods at company and/or supplier operations unless such methods are required by legislation or generally accepted as the industry standard.

Vote case-by-case on proposals requesting a report on the feasibility of implementing CAK methods at company and/or supplier operations considering the availability of existing research conducted by the company or industry groups on this topic and any fines or litigation related to current animal processing procedures at the company.

Consumer Issues

Genetically Modified Ingredients

➤ **General Recommendation:** Generally vote against proposals requesting that a company voluntarily label genetically engineered (GE) ingredients in its products. The labeling of products with GE ingredients is best left to the appropriate regulatory authorities.

Vote case-by-case on proposals asking for a report on the feasibility of labeling products containing GE ingredients, taking into account:

- The potential impact of such labeling on the company's business;
- The quality of the company's disclosure on GE product labeling, related voluntary initiatives, and how this disclosure compares with industry peer disclosure; and
- Company's current disclosure on the feasibility of GE product labeling.

Generally vote against proposals seeking a report on the social, health, and environmental effects of genetically modified organisms (GMOs). Studies of this sort are better undertaken by regulators and the scientific community.

Generally vote against proposals to eliminate GE ingredients from the company's products, or proposals asking for reports outlining the steps necessary to eliminate GE ingredients from the company's products. Such decisions are more appropriately made by management with consideration of current regulations.

Reports on Potentially Controversial Business/Financial Practices

➤ **General Recommendation:** Vote case-by-case on requests for reports on a company's potentially controversial business or financial practices or products, taking into account:

- Whether the company has adequately disclosed mechanisms in place to prevent abuses;
- Whether the company has adequately disclosed the financial risks of the products/practices in question;
- Whether the company has been subject to violations of related laws or serious controversies; and
- Peer companies' policies/practices in this area.

Pharmaceutical Pricing, Access to Medicines, and Prescription Drug Reimportation

- **General Recommendation:** Generally vote against proposals requesting that companies implement specific price restraints on pharmaceutical products unless the company fails to adhere to legislative guidelines or industry norms in its product pricing practices.

Vote case-by-case on proposals requesting that a company report on its product pricing or access to medicine policies, considering:

- The potential for reputational, market, and regulatory risk exposure;
- Existing disclosure of relevant policies;
- Deviation from established industry norms;
- Relevant company initiatives to provide research and/or products to disadvantaged consumers;
- Whether the proposal focuses on specific products or geographic regions;
- The potential burden and scope of the requested report;
- Recent significant controversies, litigation, or fines at the company.

Generally vote for proposals requesting that a company report on the financial and legal impact of its prescription drug reimportation policies unless such information is already publicly disclosed.

Generally vote against proposals requesting that companies adopt specific policies to encourage or constrain prescription drug reimportation. Such matters are more appropriately the province of legislative activity and may place the company at a competitive disadvantage relative to its peers.

Product Safety and Toxic/Hazardous Materials

- **General Recommendation:** Generally vote for proposals requesting that a company report on its policies, initiatives/procedures, and oversight mechanisms related to toxic/hazardous materials or product safety in its supply chain, unless:

- The company already discloses similar information through existing reports such as a supplier code of conduct and/or a sustainability report;
- The company has formally committed to the implementation of a toxic/hazardous materials and/or product safety and supply chain reporting and monitoring program based on industry norms or similar standards within a specified time frame; and
- The company has not been recently involved in relevant significant controversies, fines, or litigation.

Vote case-by-case on resolutions requesting that companies develop a feasibility assessment to phase-out of certain toxic/hazardous materials, or evaluate and disclose the potential financial and legal risks associated with utilizing certain materials, considering:

- The company's current level of disclosure regarding its product safety policies, initiatives, and oversight mechanisms;
- Current regulations in the markets in which the company operates; and
- Recent significant controversies, litigation, or fines stemming from toxic/hazardous materials at the company.

Generally vote against resolutions requiring that a company reformulate its products.

Tobacco-Related Proposals

- **General Recommendation:** Vote case-by-case on resolutions regarding the advertisement of tobacco products, considering:

- Recent related fines, controversies, or significant litigation;
- Whether the company complies with relevant laws and regulations on the marketing of tobacco;

- Whether the company's advertising restrictions deviate from those of industry peers;
- Whether the company entered into the Master Settlement Agreement, which restricts marketing of tobacco to youth; and
- Whether restrictions on marketing to youth extend to foreign countries.

Vote case-by-case on proposals regarding second-hand smoke, considering;

- Whether the company complies with all laws and regulations;
- The degree that voluntary restrictions beyond those mandated by law might hurt the company's competitiveness; and
- The risk of any health-related liabilities.

Generally vote against resolutions to cease production of tobacco-related products, to avoid selling products to tobacco companies, to spin-off tobacco-related businesses, or prohibit investment in tobacco equities. Such business decisions are better left to company management or portfolio managers.

Generally vote against proposals regarding tobacco product warnings. Such decisions are better left to public health authorities.

Climate Change

Say on Climate (SoC) Management Proposals

► **General Recommendation:** Vote case-by-case on management proposals that request shareholders to approve the company's climate transition action plan²², taking into account the completeness and rigor of the plan. Information that will be considered where available includes the following:

- The extent to which the company's climate related disclosures are in line with TCFD recommendations and meet other market standards;
- Disclosure of its operational and supply chain GHG emissions (Scopes 1, 2, and 3);
- The completeness and rigor of company's short-, medium-, and long-term targets for reducing operational and supply chain GHG emissions (Scopes 1, 2, and 3 if relevant);
- Whether the company has sought and received third-party approval that its targets are science-based;
- Whether the company has made a commitment to be "net zero" for operational and supply chain emissions (Scopes 1, 2, and 3) by 2050;
- Whether the company discloses a commitment to report on the implementation of its plan in subsequent years;
- Whether the company's climate data has received third-party assurance;
- Disclosure of how the company's lobbying activities and its capital expenditures align with company strategy;
- Whether there are specific industry decarbonization challenges; and
- The company's related commitment, disclosure, and performance compared to its industry peers.


Say on Climate (SoC) Shareholder Proposals

► **General Recommendation:** Vote case-by-case on shareholder proposals that request the company to disclose a report providing its GHG emissions levels and reduction targets and/or its upcoming/approved climate transition action plan and provide shareholders the opportunity to express approval or disapproval of its GHG emissions reduction plan, taking into account information such as the following:

²² Variations of this request also include climate transition related ambitions, or commitment to reporting on the implementation of a climate plan.

- The completeness and rigor of the company's climate-related disclosure;
- The company's actual GHG emissions performance;
- Whether the company has been the subject of recent, significant violations, fines, litigation, or controversy related to its GHG emissions; and
- Whether the proposal's request is unduly burdensome (scope or timeframe) or overly prescriptive.

Climate Change/Greenhouse Gas (GHG) Emissions

 **General Recommendation:** Generally vote for resolutions requesting that a company disclose information on the financial, physical, or regulatory risks it faces related to climate change on its operations and investments or on how the company identifies, measures, and manages such risks, considering:

- Whether the company already provides current, publicly-available information on the impact that climate change may have on the company as well as associated company policies and procedures to address related risks and/or opportunities;
- The company's level of disclosure compared to industry peers; and
- Whether there are significant controversies, fines, penalties, or litigation associated with the company's climate change-related performance.


Generally vote for proposals requesting a report on greenhouse gas (GHG) emissions from company operations and/or products and operations, unless:

- The company already discloses current, publicly-available information on the impacts that GHG emissions may have on the company as well as associated company policies and procedures to address related risks and/or opportunities;
- The company's level of disclosure is comparable to that of industry peers; and
- There are no significant, controversies, fines, penalties, or litigation associated with the company's GHG emissions.

Vote case-by-case on proposals that call for the adoption of GHG reduction goals from products and operations, taking into account:

- Whether the company provides disclosure of year-over-year GHG emissions performance data;
- Whether company disclosure lags behind industry peers;
- The company's actual GHG emissions performance;
- The company's current GHG emission policies, oversight mechanisms, and related initiatives; and
- Whether the company has been the subject of recent, significant violations, fines, litigation, or controversy related to GHG emissions.

Energy Efficiency

 **General Recommendation:** Generally vote for proposals requesting that a company report on its energy efficiency policies, unless:

- The company complies with applicable energy efficiency regulations and laws, and discloses its participation in energy efficiency policies and programs, including disclosure of benchmark data, targets, and performance measures; or
- The proponent requests adoption of specific energy efficiency goals within specific timelines.

Renewable Energy

- ▷ **General Recommendation:** Generally vote for requests for reports on the feasibility of developing renewable energy resources unless the report would be duplicative of existing disclosure or irrelevant to the company's line of business.

Generally vote against proposals requesting that the company invest in renewable energy resources. Such decisions are best left to management's evaluation of the feasibility and financial impact that such programs may have on the company.

Generally vote against proposals that call for the adoption of renewable energy goals, taking into account:

- The scope and structure of the proposal;
- The company's current level of disclosure on renewable energy use and GHG emissions; and
- The company's disclosure of policies, practices, and oversight implemented to manage GHG emissions and mitigate climate change risks.

Diversity

Board Diversity

- ▷ **General Recommendation:** Generally vote for requests for reports on a company's efforts to diversify the board, unless:

- The gender and racial minority representation of the company's board is reasonably inclusive in relation to companies of similar size and business; and
- The board already reports on its nominating procedures and gender and racial minority initiatives on the board and within the company.

Vote case-by-case on proposals asking a company to increase the gender and racial minority representation on its board, taking into account:

- The degree of existing gender and racial minority diversity on the company's board and among its executive officers;
- The level of gender and racial minority representation that exists at the company's industry peers;
- The company's established process for addressing gender and racial minority board representation;
- Whether the proposal includes an overly prescriptive request to amend nominating committee charter language;
- The independence of the company's nominating committee;
- Whether the company uses an outside search firm to identify potential director nominees; and
- Whether the company has had recent controversies, fines, or litigation regarding equal employment practices.

Equality of Opportunity

- ▷ **General Recommendation:** Generally vote for proposals requesting a company disclose its diversity policies or initiatives, or proposals requesting disclosure of a company's comprehensive workforce diversity data, including requests for EEO-1 data, unless:

- The company publicly discloses equal opportunity policies and initiatives in a comprehensive manner;
- The company already publicly discloses comprehensive workforce diversity data; and
- The company has no recent significant EEO-related violations or litigation.

Generally vote against proposals seeking information on the diversity efforts of suppliers and service providers. Such requests may pose a significant burden on the company.

Gender Identity, Sexual Orientation, and Domestic Partner Benefits

- ▷ **General Recommendation:** Generally vote for proposals seeking to amend a company's EEO statement or diversity policies to prohibit discrimination based on sexual orientation and/or gender identity, unless the change would be unduly burdensome.

Generally vote against proposals to extend company benefits to, or eliminate benefits from, domestic partners. Decisions regarding benefits should be left to the discretion of the company.

Gender, Race/Ethnicity Pay Gap

- ▷ **General Recommendation:** Vote case-by-case on requests for reports on a company's pay data by gender or race/ethnicity, or a report on a company's policies and goals to reduce any gender or race/ethnicity pay gaps, taking into account:

- The company's current policies and disclosure related to both its diversity and inclusion policies and practices and its compensation philosophy on fair and equitable compensation practices;
- Whether the company has been the subject of recent controversy, litigation, or regulatory actions related to gender, race, or ethnicity pay gap issues;
- The company's disclosure regarding gender, race, or ethnicity pay gap policies or initiatives compared to its industry peers; and
- Local laws regarding categorization of race and/or ethnicity and definitions of ethnic and/or racial minorities.

Racial Equity and/or Civil Rights Audit Guidelines

- ▷ **General Recommendation:** Vote case-by-case on proposals asking a company to conduct an independent racial equity and/or civil rights audit, taking into account:

- The company's established process or framework for addressing racial inequity and discrimination internally;
- Whether the company has issued a public statement related to its racial justice efforts in recent years, or has committed to internal policy review;
- Whether the company has engaged with impacted communities, stakeholders, and civil rights experts;
- The company's track record in recent years of racial justice measures and outreach externally;
- Whether the company has been the subject of recent controversy, litigation, or regulatory actions related to racial inequity or discrimination; and
- Whether the company's actions are aligned with market norms on civil rights, and racial or ethnic diversity.

Environment and Sustainability

Facility and Workplace Safety


- ▷ **General Recommendation:** Vote case-by-case on requests for workplace safety reports, including reports on accident risk reduction efforts, taking into account:

- The company's current level of disclosure of its workplace health and safety performance data, health and safety management policies, initiatives, and oversight mechanisms;
- The nature of the company's business, specifically regarding company and employee exposure to health and safety risks;
- Recent significant controversies, fines, or violations related to workplace health and safety; and
- The company's workplace health and safety performance relative to industry peers.

Vote case-by-case on resolutions requesting that a company report on safety and/or security risks associated with its operations and/or facilities, considering:


- The company's compliance with applicable regulations and guidelines;
- The company's current level of disclosure regarding its security and safety policies, procedures, and compliance monitoring; and
- The existence of recent, significant violations, fines, or controversy regarding the safety and security of the company's operations and/or facilities.

General Environmental Proposals and Community Impact Assessments

 **General Recommendation:** Vote case-by-case on requests for reports on policies and/or the potential (community) social and/or environmental impact of company operations, considering:


- Current disclosure of applicable policies and risk assessment report(s) and risk management procedures;
- The impact of regulatory non-compliance, litigation, remediation, or reputational loss that may be associated with failure to manage the company's operations in question, including the management of relevant community and stakeholder relations;
- The nature, purpose, and scope of the company's operations in the specific region(s);
- The degree to which company policies and procedures are consistent with industry norms; and
- The scope of the resolution.

Hydraulic Fracturing

 **General Recommendation:** Generally vote for proposals requesting greater disclosure of a company's (natural gas) hydraulic fracturing operations, including measures the company has taken to manage and mitigate the potential community and environmental impacts of those operations, considering:


- The company's current level of disclosure of relevant policies and oversight mechanisms;
- The company's current level of such disclosure relative to its industry peers;
- Potential relevant local, state, or national regulatory developments; and
- Controversies, fines, or litigation related to the company's hydraulic fracturing operations.

Operations in Protected Areas

 **General Recommendation:** Generally vote for requests for reports on potential environmental damage as a result of company operations in protected regions, unless:

- Operations in the specified regions are not permitted by current laws or regulations;
- The company does not currently have operations or plans to develop operations in these protected regions; or
- The company's disclosure of its operations and environmental policies in these regions is comparable to industry peers.

Recycling

 **General Recommendation:** Vote case-by-case on proposals to report on an existing recycling program, or adopt a new recycling program, taking into account:

- The nature of the company's business;
- The current level of disclosure of the company's existing related programs;
- The timetable and methods of program implementation prescribed by the proposal;
- The company's ability to address the issues raised in the proposal; and
- How the company's recycling programs compare to similar programs of its industry peers.

Sustainability Reporting

- ▷ **General Recommendation:** Generally vote for proposals requesting that a company report on its policies, initiatives, and oversight mechanisms related to social, economic, and environmental sustainability, unless:
- The company already discloses similar information through existing reports or policies such as an environment, health, and safety (EHS) report; a comprehensive code of corporate conduct; and/or a diversity report; or
 - The company has formally committed to the implementation of a reporting program based on Global Reporting Initiative (GRI) guidelines or a similar standard within a specified time frame.

Water Issues

- ▷ **General Recommendation:** Vote case-by-case on proposals requesting a company report on, or adopt a new policy on, water-related risks and concerns, taking into account:
- The company's current disclosure of relevant policies, initiatives, oversight mechanisms, and water usage metrics;
 - Whether or not the company's existing water-related policies and practices are consistent with relevant internationally recognized standards and national/local regulations;
 - The potential financial impact or risk to the company associated with water-related concerns or issues; and
 - Recent, significant company controversies, fines, or litigation regarding water use by the company and its suppliers.

General Corporate Issues

Charitable Contributions

- ▷ **General Recommendation:** Vote against proposals restricting a company from making charitable contributions. Charitable contributions are generally useful for assisting worthwhile causes and for creating goodwill in the community. In the absence of bad faith, self-dealing, or gross negligence, management should determine which, and if, contributions are in the best interests of the company.

Data Security, Privacy, and Internet Issues

- ▷ **General Recommendation:** Vote case-by-case on proposals requesting the disclosure or implementation of data security, privacy, or information access and management policies and procedures, considering:
- The level of disclosure of company policies and procedures relating to data security, privacy, freedom of speech, information access and management, and Internet censorship;
 - Engagement in dialogue with governments or relevant groups with respect to data security, privacy, or the free flow of information on the Internet;
 - The scope of business involvement and of investment in countries whose governments censor or monitor the Internet and other telecommunications;
 - Applicable market-specific laws or regulations that may be imposed on the company; and
 - Controversies, fines, or litigation related to data security, privacy, freedom of speech, or Internet censorship.


Environmental, Social, and Governance (ESG) Compensation-Related Proposals

- ▷ **General Recommendation:** Vote case-by-case on proposals to link, or report on linking, executive compensation to sustainability (environmental and social) criteria, considering:
- The scope and prescriptive nature of the proposal;
 - Whether the company has significant and/or persistent controversies or regulatory violations regarding social and/or environmental issues;
 - Whether the company has management systems and oversight mechanisms in place regarding its social and environmental performance;

- The degree to which industry peers have incorporated similar non-financial performance criteria in their executive compensation practices; and
- The company's current level of disclosure regarding its environmental and social performance.

Human Rights, Human Capital Management, and International Operations

Human Rights Proposals

-  **General Recommendation:** Generally vote for proposals requesting a report on company or company supplier labor and/or human rights standards and policies unless such information is already publicly disclosed.


Vote case-by-case on proposals to implement company or company supplier labor and/or human rights standards and policies, considering:

- The degree to which existing relevant policies and practices are disclosed;
- Whether or not existing relevant policies are consistent with internationally recognized standards;
- Whether company facilities and those of its suppliers are monitored and how;
- Company participation in fair labor organizations or other internationally recognized human rights initiatives;
- Scope and nature of business conducted in markets known to have higher risk of workplace labor/human rights abuse;
- Recent, significant company controversies, fines, or litigation regarding human rights at the company or its suppliers;
- The scope of the request; and
- Deviation from industry sector peer company standards and practices.

Vote case-by-case on proposals requesting that a company conduct an assessment of the human rights risks in its operations or in its supply chain, or report on its human rights risk assessment process, considering:

- The degree to which existing relevant policies and practices are disclosed, including information on the implementation of these policies and any related oversight mechanisms;
- The company's industry and whether the company or its suppliers operate in countries or areas where there is a history of human rights concerns;
- Recent significant controversies, fines, or litigation regarding human rights involving the company or its suppliers, and whether the company has taken remedial steps; and
- Whether the proposal is unduly burdensome or overly prescriptive.

Mandatory Arbitration

-  **General Recommendation:** Vote case-by-case on requests for a report on a company's use of mandatory arbitration on employment-related claims, taking into account:

- The company's current policies and practices related to the use of mandatory arbitration agreements on workplace claims;
- Whether the company has been the subject of recent controversy, litigation, or regulatory actions related to the use of mandatory arbitration agreements on workplace claims; and
- The company's disclosure of its policies and practices related to the use of mandatory arbitration agreements compared to its peers.

Operations in High Risk Markets

- ▷ **General Recommendation:** Vote case-by-case on requests for a report on a company's potential financial and reputational risks associated with operations in "high-risk" markets, such as a terrorism-sponsoring state or politically/socially unstable region, taking into account:
- The nature, purpose, and scope of the operations and business involved that could be affected by social or political disruption;
 - Current disclosure of applicable risk assessment(s) and risk management procedures;
 - Compliance with U.S. sanctions and laws;
 - Consideration of other international policies, standards, and laws; and
 - Whether the company has been recently involved in recent, significant controversies, fines, or litigation related to its operations in "high-risk" markets.

Outsourcing/Offshoring

- ▷ **General Recommendation:** Vote case-by-case on proposals calling for companies to report on the risks associated with outsourcing/plant closures, considering:
- Controversies surrounding operations in the relevant market(s);
 - The value of the requested report to shareholders;
 - The company's current level of disclosure of relevant information on outsourcing and plant closure procedures; and
 - The company's existing human rights standards relative to industry peers.

Sexual Harassment

- ▷ **General Recommendation:** Vote case-by-case on requests for a report on company actions taken to strengthen policies and oversight to prevent workplace sexual harassment, or a report on risks posed by a company's failure to prevent workplace sexual harassment, taking into account:
- The company's current policies, practices, oversight mechanisms related to preventing workplace sexual harassment;
 - Whether the company has been the subject of recent controversy, litigation, or regulatory actions related to workplace sexual harassment issues; and
 - The company's disclosure regarding workplace sexual harassment policies or initiatives compared to its industry peers.

Weapons and Military Sales

- ▷ **General Recommendation:** Vote against reports on foreign military sales or offsets. Such disclosures may involve sensitive and confidential information. Moreover, companies must comply with government controls and reporting on foreign military sales.

Generally vote against proposals asking a company to cease production or report on the risks associated with the use of depleted uranium munitions or nuclear weapons components and delivery systems, including disengaging from current and proposed contracts. Such contracts are monitored by government agencies, serve multiple military and non-military uses, and withdrawal from these contracts could have a negative impact on the company's business.

Political Activities

Lobbying

- ▷ **General Recommendation:** Vote case-by-case on proposals requesting information on a company's lobbying (including direct, indirect, and grassroots lobbying) activities, policies, or procedures, considering:

- The company's current disclosure of relevant lobbying policies, and management and board oversight;
- The company's disclosure regarding trade associations or other groups that it supports, or is a member of, that engage in lobbying activities; and
- Recent significant controversies, fines, or litigation regarding the company's lobbying-related activities.

Political Contributions

▷ **General Recommendation:** Generally vote for proposals requesting greater disclosure of a company's political contributions and trade association spending policies and activities, considering:

- The company's policies, and management and board oversight related to its direct political contributions and payments to trade associations or other groups that may be used for political purposes;
- The company's disclosure regarding its support of, and participation in, trade associations or other groups that may make political contributions; and
- Recent significant controversies, fines, or litigation related to the company's political contributions or political activities.

Vote against proposals barring a company from making political contributions. Businesses are affected by legislation at the federal, state, and local level; barring political contributions can put the company at a competitive disadvantage.

Vote against proposals to publish in newspapers and other media a company's political contributions. Such publications could present significant cost to the company without providing commensurate value to shareholders.

Political Ties

▷ **General Recommendation:** Generally vote against proposals asking a company to affirm political nonpartisanship in the workplace, so long as:

- There are no recent, significant controversies, fines, or litigation regarding the company's political contributions or trade association spending; and
- The company has procedures in place to ensure that employee contributions to company-sponsored political action committees (PACs) are strictly voluntary and prohibit coercion.

Vote against proposals asking for a list of company executives, directors, consultants, legal counsels, lobbyists, or investment bankers that have prior government service and whether such service had a bearing on the business of the company. Such a list would be burdensome to prepare without providing any meaningful information to shareholders.

8. Mutual Fund Proxies

Election of Directors

- ▶ **General Recommendation:** Vote case-by-case on the election of directors and trustees, following the same guidelines for uncontested directors for public company shareholder meetings. However, mutual fund boards do not usually have compensation committees, so do not withhold for the lack of this committee.

Closed End Funds- Unilateral Opt-In to Control Share Acquisition Statutes

- ▶ **General Recommendation:** For closed-end management investment companies (CEFs), vote against or withhold from nominating/governance committee members (or other directors on a case-by-case basis) at CEFs that have not provided a compelling rationale for opting-in to a Control Share Acquisition statute, nor submitted a by-law amendment to a shareholder vote.

Converting Closed-end Fund to Open-end Fund

- ▶ **General Recommendation:** Vote case-by-case on conversion proposals, considering the following factors:
 - Past performance as a closed-end fund;
 - Market in which the fund invests;
 - Measures taken by the board to address the discount; and
 - Past shareholder activism, board activity, and votes on related proposals.

Proxy Contests

- ▶ **General Recommendation:** Vote case-by-case on proxy contests, considering the following factors:
 - Past performance relative to its peers;
 - Market in which the fund invests;
 - Measures taken by the board to address the issues;
 - Past shareholder activism, board activity, and votes on related proposals;
 - Strategy of the incumbents versus the dissidents;
 - Independence of directors;
 - Experience and skills of director candidates;
 - Governance profile of the company;
 - Evidence of management entrenchment.

Investment Advisory Agreements

- ▶ **General Recommendation:** Vote case-by-case on investment advisory agreements, considering the following factors:
 - Proposed and current fee schedules;
 - Fund category/investment objective;
 - Performance benchmarks;
 - Share price performance as compared with peers;
 - Resulting fees relative to peers;
 - Assignments (where the advisor undergoes a change of control).

Approving New Classes or Series of Shares

- ▶ **General Recommendation:** Vote for the establishment of new classes or series of shares.

Preferred Stock Proposals

- ▶ **General Recommendation:** Vote case-by-case on the authorization for or increase in preferred shares, considering the following factors:

- Stated specific financing purpose;
- Possible dilution for common shares;
- Whether the shares can be used for antitakeover purposes.

1940 Act Policies

➤ **General Recommendation:** Vote case-by-case on policies under the Investment Advisor Act of 1940, considering the following factors:

- Potential competitiveness;
- Regulatory developments;
- Current and potential returns; and
- Current and potential risk.

Generally vote for these amendments as long as the proposed changes do not fundamentally alter the investment focus of the fund and do comply with the current SEC interpretation.

Changing a Fundamental Restriction to a Nonfundamental Restriction

➤ **General Recommendation:** Vote case-by-case on proposals to change a fundamental restriction to a non-fundamental restriction, considering the following factors:

- The fund's target investments;
- The reasons given by the fund for the change; and
- The projected impact of the change on the portfolio.

Change Fundamental Investment Objective to Nonfundamental

➤ **General Recommendation:** Vote against proposals to change a fund's fundamental investment objective to non-fundamental.

Name Change Proposals

➤ **General Recommendation:** Vote case-by-case on name change proposals, considering the following factors:

- Political/economic changes in the target market;
- Consolidation in the target market; and
- Current asset composition.

Change in Fund's Subclassification

➤ **General Recommendation:** Vote case-by-case on changes in a fund's sub-classification, considering the following factors:

- Potential competitiveness;
- Current and potential returns;
- Risk of concentration;
- Consolidation in target industry.

Business Development Companies—Authorization to Sell Shares of Common Stock at a Price below Net Asset Value

➤ **General Recommendation:** Vote for proposals authorizing the board to issue shares below Net Asset Value (NAV) if:

- The proposal to allow share issuances below NAV has an expiration date no more than one year from the date shareholders approve the underlying proposal, as required under the Investment Company Act of 1940;
- The sale is deemed to be in the best interests of shareholders by (1) a majority of the company's independent directors and (2) a majority of the company's directors who have no financial interest in the issuance; and

- The company has demonstrated responsible past use of share issuances by either:
- Outperforming peers in its 8-digit GICS group as measured by one- and three-year median TSRs; or
- Providing disclosure that its past share issuances were priced at levels that resulted in only small or moderate discounts to NAV and economic dilution to existing non-participating shareholders.

Disposition of Assets/Termination/Liquidation

▷ **General Recommendation:** Vote case-by-case on proposals to dispose of assets, to terminate or liquidate, considering the following factors:

- Strategies employed to salvage the company;
- The fund's past performance;
- The terms of the liquidation.

Changes to the Charter Document

▷ **General Recommendation:** Vote case-by-case on changes to the charter document, considering the following factors:

- The degree of change implied by the proposal;
- The efficiencies that could result;
- The state of incorporation;
- Regulatory standards and implications.

Vote against any of the following changes:

- Removal of shareholder approval requirement to reorganize or terminate the trust or any of its series;
- Removal of shareholder approval requirement for amendments to the new declaration of trust;
- Removal of shareholder approval requirement to amend the fund's management contract, allowing the contract to be modified by the investment manager and the trust management, as permitted by the 1940 Act;
- Allow the trustees to impose other fees in addition to sales charges on investment in a fund, such as deferred sales charges and redemption fees that may be imposed upon redemption of a fund's shares;
- Removal of shareholder approval requirement to engage in and terminate subadvisory arrangements;
- Removal of shareholder approval requirement to change the domicile of the fund.

Changing the Domicile of a Fund

▷ **General Recommendation:** Vote case-by-case on re-incorporations, considering the following factors:

- Regulations of both states;
- Required fundamental policies of both states;
- The increased flexibility available.

Authorizing the Board to Hire and Terminate Subadvisers Without Shareholder Approval

▷ **General Recommendation:** Vote against proposals authorizing the board to hire or terminate subadvisers without shareholder approval if the investment adviser currently employs only one subadviser.

Distribution Agreements

▷ **General Recommendation:** Vote case-by-case on distribution agreement proposals, considering the following factors:

- Fees charged to comparably sized funds with similar objectives;
- The proposed distributor's reputation and past performance;
- The competitiveness of the fund in the industry;
- The terms of the agreement.

Master-Feeder Structure

- ▶ **General Recommendation:** Vote for the establishment of a master-feeder structure.

Mergers

- ▶ **General Recommendation:** Vote case-by-case on merger proposals, considering the following factors:

- Resulting fee structure;
- Performance of both funds;
- Continuity of management personnel;
- Changes in corporate governance and their impact on shareholder rights.

Shareholder Proposals for Mutual Funds

Establish Director Ownership Requirement

- ▶ **General Recommendation:** Generally vote against shareholder proposals that mandate a specific minimum amount of stock that directors must own in order to qualify as a director or to remain on the board.

Reimburse Shareholder for Expenses Incurred

- ▶ **General Recommendation:** Vote case-by-case on shareholder proposals to reimburse proxy solicitation expenses. When supporting the dissidents, vote for the reimbursement of the proxy solicitation expenses.

Terminate the Investment Advisor

- ▶ **General Recommendation:** Vote case-by-case on proposals to terminate the investment advisor, considering the following factors:

- Performance of the fund's Net Asset Value (NAV);
- The fund's history of shareholder relations;
- The performance of other funds under the advisor's management.

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EXHIBIT 3

Managers Not Using VRS's ISS Proxy Voting Platform – FY 2022

Defined Benefit Managers

Arrowstreet Global 130/30

Baillie Gifford Global

Baillie Gifford Emerging Markets

Jackson Square U.S. SMID

J.P. Morgan U.S. Market Neutral

Lansdowne Global Long Only

BlackRock GTAA

All hedge funds except for Advent

Defined Contribution Managers

All

Optional Retirement Plan for Higher Education Managers

All



Resolution of Appreciation

PRESENTED TO

Troilen Gainey Seward, Ed.S.

*W*HEREAS, Troilen Gainey Seward, Ed.S., was first appointed to serve on the Virginia Retirement System Board of Trustees in March 2012, and in recognition of her extensive knowledge of the system, she was subsequently reappointed for a second term in March 2017; and

*W*HEREAS, Mrs. Seward served as a Member and as a Vice Chair of the Benefits and Actuarial Committee, evaluating information presented on plan benefits, funding, and actuarial principles, contributing to committee discussions and serving in these roles with commitment and distinction; and

*W*HEREAS, Mrs. Seward served as a Member of the Administration and Personnel Committee, Investment Policy Committee, the Strategic Projects Committee, and the Chief Investment Officer Search Committee, sharing her insights, which contributed greatly to these deliberations; and

*W*HEREAS, Mrs. Seward served the members and retirees of the system with steady leadership and integrity, paired with in-depth experience in and extensive knowledge of the public education system in the Commonwealth; and

*W*HEREAS, Mrs. Seward frequently and estimably served as the Board's ambassador at meetings of the Virginia Retired Teachers Association, where she engaged with members and presented the audience with legislative, administrative, and benefit updates concerning the system;

*N*OW, THEREFORE, BE IT RESOLVED, that on October 18, 2022, we, the members of the Board of Trustees of the Virginia Retirement System, hereby acknowledge Mrs. Seward's loyal and faithful service to the Board of Trustees, the Virginia Retirement System, its members, retirees, and the Commonwealth of Virginia, and are grateful for her contributions, stewardship, and commitment.

A. SCOTT ANDREWS, CHAIR



Resolution of Appreciation

PRESENTED TO

Deborah Allen Hewitt, Ph.D.

*W*HEREAS, Deborah Allen Hewitt, Ph.D., began her service to the Virginia Retirement System in October 2002 by serving as a member of the Investment Advisory Committee and continued her faithful service to the members, retirees, and beneficiaries of the system through 2022; and

*W*HEREAS, by virtue of Dr. Hewitt's academic background and in-depth knowledge and understanding of investment, financial, and economic matters, she contributed rigor to the Investment Advisory Committee discussions; and

*W*HEREAS, Dr. Hewitt gained knowledge and understanding of other countries and their economies by traveling extensively abroad, then returning and sharing these insights with the Committee, resulting in interesting and engaging Committee conversations and dialogue; and

*W*HEREAS, Dr. Hewitt possessed a keen interest in enhancing institutional investor knowledge and education, which served to enrich the Committee; and

*W*HEREAS, Dr. Hewitt, one of the longest serving members of the Investment Advisory Committee, served during the challenging investor environment of the Financial Crisis and Great Recession, and with her calm demeanor and steady influence provided value to the Committee discussions and to the Virginia Retirement System Board of Trustees;

*N*OW, THEREFORE, BE IT RESOLVED, that on October 18, 2022, we, the members of the Board of Trustees of the Virginia Retirement System, hereby recognize Dr. Hewitt's loyal and unswerving service to the Investment Advisory Committee and acknowledge her long-standing contributions for the betterment of the System, including her faithful service to the Investment Advisory Committee, the Board of Trustees, members, and beneficiaries of the System, and to the Commonwealth of Virginia.

A. SCOTT ANDREWS, CHAIR

Operational/Ongoing Activities	Strategic Alignment	Status	2022						2023							
			Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun		
Annual Roadmap Review		N/S														
FYE 2023		N/S														
Retirement Wave 2023		N/S														
Commonwealth Bond Disclosure		N/S														
ORPHE Surcharge Billing for FY 2024		N/S														
Data Fixes		●														
ALM Backlog Prioritization		●														
Employer VNAV Security Review		N/S														
VRS Fund Sensitivity and Stress Testing Report for GA		●														
Legislation FY 2023		N/S														

¹Initiatives led directly by Technology Services.

²Other initiatives are led by other business units and supported by Technology Services.

Yellow Status Items

Item	Due Date	Comments
N/A		

Red Status Items

Item	Due Date	Comments
N/A		

Realignments/Adjustments

Item	Due Date	Comments
N/A		

New Coverage Elections



Coverage Elected

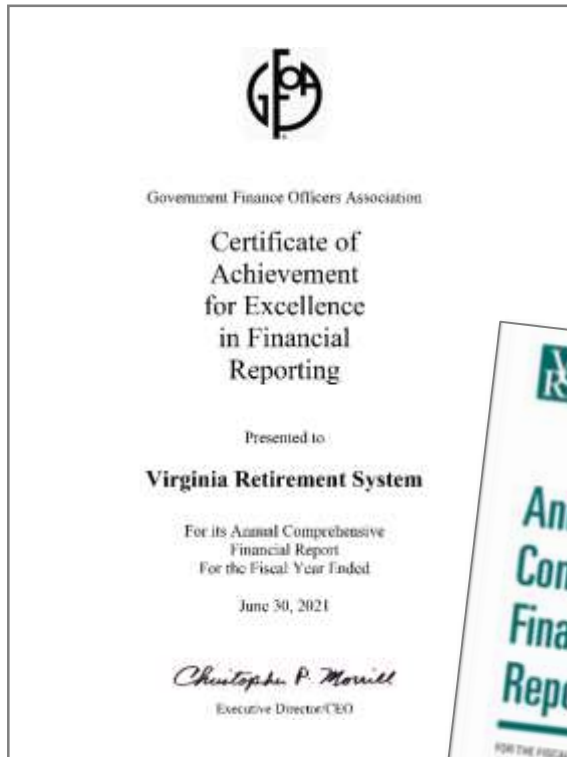
Details

New State Agency

- **Puller Veterans Care Center (Fauquier County)**
Effective August 1, 2022
- **Jones & Cabacoy Veterans Care Center (City of Virginia Beach)**
Effective August 1, 2022
- **Virginia Housing Commission (City of Richmond)**
Effective September 1, 2022

Enhanced Hazardous Duty Benefits for Emergency Medical Technicians

- **City of Hampton**
Effective October 1, 2022
-



VRS is pleased to announce the successful achievement of the **Certificate of Excellence in Financial Reporting** for the 2021 Annual Comprehensive Financial Report (ACFR).

This was the **40th** report for which we received the award from the Government Finance Officers Association (GFOA).

The Certificate of Achievement is the **highest form of recognition** in the area of governmental accounting and financial reporting.



Customer Service Week



Virginia
Retirement
System

VRS celebrated Customer Service Week during the week of October 3. This year's theme, "Celebrate Service," was especially fitting for VRS' milestone anniversary. We have been serving public servants for 80 years!



Customer Service Week allows VRS to honor all our employees who serve members, retirees and employers.

Employees participated in various activities during the week. A favorite was the "coffee cart" where executive staff members served coffee and other treats from a cart and visited with each work area.