EMPLOYEES RETIREMENT SYSTEM OF TEXAS
INCENTIVE COMPENSATION PLAN
FOR INVESTMENT PROFESSIONALS AND LEADERSHIP EMPLOYEES

Board Approved August ~~21, 2024~~20, 2025
Effective Date September 1, ~~2024~~2025

Table of Contents

1. Establishment and Purpose 3
2. Definitions 3
3. Eligibility and Participation 7
4. Establishment of Performance Goals 8
5. Calculation of Incentive Compensation Awards 11
6. Incentive Compensation Award Payments and Limitations 12
7. Plan Administration 15
8. Miscellaneous 16
   APPENDIX A 18
   APPENDIX B 19
   APPENDIX C 21
   APPENDIX D 22

1. Establishment and Purpose

1.1 The Employees Retirement System of Texas (ERS) hereby establishes the Employees Retirement System of Texas Incentive Compensation Plan (Plan) to provide meaningful incentives for key leadership and professional employees who are providing high-level, discretionary services related to the investment of ERS' assets. The primary goal of ERS' Investments Division is to earn an appropriate risk adjusted return, net of fees, on Trust Fund assets to provide funds for the benefit payments due to, or on behalf of, members, retirees, and beneficiaries of the retirement plans at a reasonable administrative cost. The Plan is intended to provide incentives to those participating employees who excel in carrying out the strategic performance priorities established by the Board and achieve the highest level of performance on behalf of ERS and its members, retirees, and beneficiaries while promoting behavior that is consistent with the risk parameters established in the Investment Policy. Specifically, the Plan is designed to:

(a) provide participating employees with the opportunity to earn reasonable incentive compensation for leadership and outstanding performance based on Global Composite Performance, as well as performance of applicable asset classes, and portfolios and individual contributions;

(b) encourage sustained levels of outstanding investment performance prudently achieved without undue risk;

(c) promote teamwork among employees;

(d) support ERS' strategic and operational goals;

(e) attract and retain key employees in a cost-effective manner; and

(f) focus employees on high quality outcomes.

1.2 The Board has determined that this Plan is necessary for the performance of its fiduciary duties and that it has the authority to establish and provide funds for this Plan as set forth herein pursuant to applicable laws and the Board's authority to approve ERS' annual operating budget.

2. Definitions

When used in this Plan, the following words and phrases shall have the following meanings:

2.1 "Asset Class" - a category of investments that exhibit similar characteristics, such as public equity, private equity, and fixed income - rates, as adopted by the Board in the Investment Policy.

2.2 "Basis Point" - a measure used in quoting investment returns. One basis point equals 0.01%.

2.3 "Benchmark" - (a) the applicable benchmark specified in Chapter V, Table 4, of the Investment Policy or otherwise approved by the Board in the Investment Policy for an Asset Class; or (b) reasonably derived benchmarks for subcategories of the Individual Portfolios identified in the Risk Budget as specified in Section 4.7.

2.4 "Board" - the ERS Board of Trustees, as constituted from time to time.

2.5 "CIO" - the Chief Investment Officer of ERS.

2.6 "CIO Goals Memo" - memo from the CIO (or the CIO's designee) to the Executive Director which defines the Benchmarks and other quantitative metrics to be used for the upcoming Plan Year. All quantitative measures that are not expressly stated in the Investment Policy are explained in the CIO Goals Memo, and changes from the prior Plan Year to the upcoming Plan Year are highlighted.

2.7 "Clawback" - a situation, as specified in Section 6.9, requiring that a Participant repay all or part of any Incentive Compensation Award previously paid to the Participant.

2.8 "Custodian" - the global custodian of the assets of the Trust Fund selected by the Board in accordance with Section 815.302 of the Texas Government Code.

2.9 "Disability" - physical or mental incapacity that would support a certification of disability under Section 814.203(a) of the Texas Government Code or a finding that a Participant is disabled within the meaning of Section 409A(a)(2)(C) of the Internal Revenue Code.

2.10 "Eligibility Date" - for any Participant, (a) the first day of the Plan Year, which is September 1 for those Participants eligible to participate on that date; or (b) the date determined pursuant to Section 3.2 for those Eligible Employees who become Participants after the beginning of the Plan Year.

2.11 "Eligible Employee" - a Leadership Employee or an Investment Professional who has been approved by the Board or Executive Director to participate in the Plan and whose job is part of one of the Plan Groups included in Appendix A and who has not been removed or otherwise made ineligible for participation in or payment of an award under the Plan.

2.12 "ERS Performance Evaluation" - an evaluation measuring the Participant's job performance, as provided in the ERS Personnel Policy and Procedure Manual.

2.13 "Excess Return" - actual return after subtracting the return of the applicable Benchmark. Excess Return may be positive or negative.

2.14 "Executive Director" - the Executive Director of ERS.

2.15 "Finance" - the Finance Division of ERS.

2.16 "Global Composite Performance" - Trust Fund performance results, net of fees as reported by the Custodian, and net of internal costs as calculated by Finance staff.

2.17 "Human Resources" - the Human Resources Division of ERS.

2.18 "Information Ratio" - a measure of the Excess Return of a composite or portfolio over a Benchmark given the level of risk permitted by the Board, as documented in the Risk Budget in Chapter V, Table 4, of the Investment Policy. The Information Ratio is calculated as: (actual return – benchmark return) / (Tracking Error).

2.19 "Incentive Compensation Award" - a contingent award to a Participant as determined pursuant to the Plan and subject to the terms and conditions of the Plan.

2.20 "Individual Portfolio" - a grouping of investments associated with a strategy, geography, or other distinguishing characteristic that is managed against a Benchmark as part of an approved Asset Class.

2.21 "Investment Consultant" - the consultant selected by the Board in accordance with Section 815.301(d) of the Texas Government Code to perform, among other responsibilities, an

evaluation and analysis of the investment results of the Trust Fund.

2.22 "Investment Operations" - the team within the Investments Division that acts largely in the capacity of data steward and supports Investment Professionals.

2.23 "Investment Policy" - the ERS Investment Policy Statement adopted by the Board, as amended from time to time.

2.24 "Investment Professional" - an ERS employee (other than a Leadership Employee) who provides high-level, discretionary professional services related to the investment of the Trust Fund and serves in one of the Plan Groups reflected in Appendix A. For purposes of the Plan, an employee may not be an Investment Professional and a Leadership Employee at the same time.

2.25 "Investments Division" - the Investments Division of ERS.

2.26 "Leadership Employee" - the Executive Director, the CIO, and such other senior management employees of ERS as the Board or Executive Director designates.

2.27 "Maximum Incentive Award" - the Participant's Weighted Salary multiplied by the Maximum Incentive Award Percentage or, if applicable, the Weighted Maximum Incentive Award Percentage. See examples in Appendix D.

2.28 "Maximum Incentive Award Percentage" - the largest multiplier that may be used to calculate the Maximum Incentive Award identified in the Participant Goal Sheet. The Maximum Incentive Award Percentage must be approved by the Executive Director and may not exceed the percentage for such Participant set forth in Appendix A. In the case of the Executive Director, the Maximum Incentive Award Percentage must be approved by the Board.

2.29 "Maximum Performance Goals" - documented in the Participant Goal Sheet to provide prudent limits to Excess Returns as follows:

(a) for the Trust Fund - the weighted average of the target Excess Returns of all portfolios of the Trust Fund as recommended by the CIO and approved by the Executive Director;

(b) for public market portfolios - the target Excess Return identified for each Performance Goal, which shall be reasonably derived from the Information Ratio and target Tracking Error of the relevant Asset Class; and

(c) for private market portfolios - the target Excess Return established in consultation with ERS consultants and explained in the CIO Goals Memo.

2.30 "Net of Fees" - the calculation of performance after taking into consideration (a) all external advisor, management, and performance fees; (b) internal investments expenses as reported in the Annual Comprehensive Financial Report (ACFR); and (c) a reasonable allocation of other agency overhead expenses. For determining internal investments expenses, the draft ACFR shall be used for the one-year amount.

2.31 "Original Eligibility Date" - for any Eligible Employee, the initial Eligibility Date when he/she became a Participant in the Plan.

2.32 "Participant" - an Eligible Employee who is approved to participate in the Plan pursuant to Articles 3 and 4 and who has not ceased to be eligible to participate.

2.33 “Participant Goal Sheet” - the documentation of each Participant’s Performance Goals pursuant to Article 4 as recommended by the CIO or other applicable ERS division director and approved by the Executive Director or his/her designee. The Executive Director’s goals are approved by the Board.

2.34 “Payment Date” - with respect to a Plan Year, on or before February 1 following the end of the Plan Year. For purposes of the Plan, the Payment Date shall be for Incentive Compensation Awards earned in the most recently concluded Plan Year and prior Plan Years that remain to be paid according to the applicable Payment Schedule.

2.35 “Payment Schedule" - the period, as described in Section 6.2 and Section 6.3, over which Incentive Compensation Awards are payable to a Participant.

2.36 “Performance Goals” - (a) with respect to a Participant who is an Investment Professional, the quantitative and/or qualitative performance standards representing outstanding performance that are recommended by the CIO, or other applicable ERS division director, and approved by the Executive Director or his/her designee pursuant to Article 4; and (b) with respect to a Participant who is a Leadership Employee, the quantitative and qualitative performance standards representing performance exceeding the Participant’s job expectations that are established by the Board or Executive Director.

2.37 “Performance Goal Weighting” - the specified weighting (as a percentage of all applicable components) given to a particular Performance Goal. The weighting of a Participant's Performance Goals for a Performance Period shall total 100%.

2.38 “Performance Period” - the time period over which a Performance Goal is evaluated. For purposes of the Plan, the Performance Periods for a plan year are one, three, and five-year periods that end on the last day of such Plan Year as specified in Section 4.8 or as otherwise determined by the Executive Director.

2.39 “Performance Period Weighting" - the weighting given to a particular Performance Period as specified in Section 4.8. The weighting given to all applicable Performance Periods for a plan year for each Participant shall total 100%.

2.40 “Plan” - the Employees Retirement System of Texas Incentive Compensation Plan for Investment Professionals and Leadership Employees as set out herein and amended from time to time.

2.41 “Plan Group” - the grouping to which a Participant is assigned that determines the Participant’s Maximum Incentive Award Percentage as set forth in Appendix A. Each Participant is assigned to a Plan Group, based on his/her job responsibilities, by the CIO or other applicable division director. Leadership Employees are assigned to a Plan Group by the Executive Director. The Executive Director is assigned to a Plan Group by the Board. Plan Groups are distinct from the State of Texas payroll titles, although they may use similar terminology.

2.42 “Plan Year” - the consecutive 12-month period beginning on September 1 and ending on the following August 31.

2.43 “Realization Percentage” - a percentage, not greater than 100%, determined as specified in Section 5.5.

2.44 “Relative Global Composite Performance” - for a Performance Period, Excess Return resulting from actual Global Composite Performance relative to its Benchmark.

2.45 “Relative Performance” - for a Performance Period, Excess Return of a composite’s or portfolio’s actual return relative to its Benchmark return.

2.46 "Risk Budget" - the Risk Budget adopted by the Board as part of the Investment Policy (Chapter V, Table 4), which identifies the adopted Benchmarks for all asset classes and expected Information Ratios for the public market asset classes. The adopted Benchmarks and Information Ratios set the active return expected per unit of the active risk allowed within the risk tolerance of the Board.

2.47 "Special Performance Evaluation" - specified in Section 3.6.

2.48 "Third Party Reviewer" - An independent entity that contracts with ERS to perform a set of agreed upon procedures with the objective of validating the Incentive Compensation Award calculations against relevant source documents.

2.49 "Tracking Error" - a statistical measure of the divergence between the returns of a portfolio and those of its benchmark, which is typically calculated as the standard deviation of excess returns over a historical period.

2.50 "Trust Fund" - the trust funds administered by ERS by virtue of the authority provided in Article XVI, Section 67, Texas Constitution and applicable law.

2.51 "Underpayment" - a situation, as specified in Section 6.13, where an Incentive Compensation Award was incorrectly calculated and a Participant was underpaid.

2.52 "Weighted Maximum Incentive Award Percentage" - determined by adding together the Eligible Employee's Maximum Incentive Award Percentage for each month (taking into account Plan Year changes) during a Plan Year and then dividing that sum by the number of months the Participant participated in the Plan in such plan year. See example in Appendix D.

2.53 "Weighted Realization Percentage" - with respect to a Performance Period, the Realization Percentage multiplied by the Performance Goal Weighting.

2.54 "Weighted Salary" - determined by adding the Participant's monthly salaries together (taking into account plan year salary changes) for a plan year and then dividing that sum by the number of months the Participant participated in the Plan in such plan year. See example in Appendix D.

3. Eligibility and Participation

3.1 Before the beginning of each plan year, the Board or the Executive Director, as applicable, shall select those Eligible Employees to be designated as Participants for the plan year and, with the assistance of Human Resources, shall notify each Eligible Employee, the CIO, and any other applicable division director of the employee's eligibility to participate in the Plan and the criteria for determining an Incentive Compensation Award for the employee. The Board, before the beginning of each plan year, shall inform the Executive Director of the criteria for determining an Incentive Compensation Award for the Executive Director. If an employee becomes an Eligible Employee after the beginning of a plan year under Section 3.2, notification under this section shall occur by the employee's Eligibility Date.

3.2 The Board or the Executive Director, as applicable, may authorize an employee to become an Eligible Employee after the beginning of a plan year, with his/her Eligibility Date being the first day of the month following (a) completion of a waiting period of three full months of employment or (b) no waiting period, provided that the Board or Executive Director approves such earlier Plan Eligibility Date based on written justification.

The Board or the Executive Director, as applicable, may authorize continued eligibility of an

existing Eligible Employee who is transferred or promoted into another Plan Group included in Appendix A, with the employee's Incentive Compensation Award prorated effective as of the first day of the first full month after the transfer or promotion.

3.3 If an employee no longer holds an eligible employee position which is part of a Plan Group included in Appendix A, the employee's eligibility to participate in the Plan ends on the first date that the employee no longer holds such a position.

3.4 A Participant must exceed the Participant's Performance Goals and have a current ERS performance evaluation on file to receive an Incentive Compensation Award.

3.5 The Board or the Executive Director may remove or suspend a Participant from participation in the Plan and may suspend, cancel, prorate, reduce, or claw back an Incentive Compensation Award because of:

(a) a failure to satisfy any requirement of the Plan;

(b) a material violation of the Investment Policy, any other ERS policy or procedure, or any legal duty or requirement related to the Participant's employment;

(c) documented disciplinary action;

(d) a performance evaluation or other performance report that indicates the Participant did not consistently exceed overall performance expectations; or

(e) an inability to directly correlate a Participant's Performance Goal(s) with the Participant's actual performance.

3.6 If any of the circumstances described in Section 3.5 occurs, the Participant's supervisor and division director, in consultation with the Director of Human Resources, nonetheless may recommend the payment of an Incentive Compensation Award but must identify factual circumstances that support payment and must establish an action plan that sets detailed goals and expectations for evaluation in a subsequent Special Performance Evaluation. If the subsequent Special Performance Evaluation, which must be approved by the division director and the Director of Human Resources, reflects that the employee successfully met the goals and expectations set forth in the action plan, the Board or Executive Director may approve the payment of an Incentive Compensation Award to the employee. Regardless of any recommendation from a supervisor, division director, or Human Resources, the Board or Executive Director may determine that circumstances make the payment of an Incentive Compensation Award inappropriate and, therefore, decline to approve payment.

3.7 Designation as a Participant for a plan year does not entitle any employee to be designated as a Participant for any future plan year.

4. Establishment of Performance Goals

4.1 Before the beginning of each Plan Year, the CIO and other applicable ERS division directors shall recommend the Performance Goals for the upcoming plan year for each Participant. In the case of a Participant whose Eligibility Date is after the beginning of the plan year, such recommendations shall be made before the Participant's Eligibility Date. In establishing Performance Goals, the CIO and other applicable ERS division directors shall emphasize factors that objectively measure a Participant's contribution to the financial and strategic success of ERS, as well as individual contributions that represent outstanding performance. Performance Goals will be based on exceeding Benchmarks and other individual performance metrics to reward outstanding performance while promoting behavior that is consistent with the risk parameters established in the Investment Policy.

4.2 Performance Goals for each Participant shall be documented in the form of a Participant

Goal Sheet.

4.3 No later than June 30 preceding each plan year, a draft of the CIO Goals Memo, including any changes to Participant Goal Sheets and Maximum Performance Goals for the upcoming Plan Year, shall be submitted to Human Resources. Human Resources will review and generate a preliminary Participant Goal Sheet for each Eligible Employee.

4.4 Before the beginning of each plan year:

(a) The CIO and other applicable ERS division directors (or their designees) shall review the preliminary Participant Goal Sheet for each Eligible Employee and submit final changes to Human Resources. Human Resources will review and generate a final Participant Goal Sheet for each Eligible Employee.

(b) The CIO shall submit the CIO Goals Memo, including Maximum Performance Goals and Performance Goals for each Participant, to the Executive Director (or the Executive Director's designee) with sufficient time for review and approval before the beginning of the plan year.

(c) If a Participant's Performance Goals are approved after the beginning of the plan year, any Incentive Compensation Award based on those Performance Goals shall be prorated.

4.5 The Performance Goals for Leadership Employees other than the Executive Director shall be documented in Participant Goal Sheets by Human Resources and approved by the Executive Director before the beginning of the Plan Year. Leadership Employees are generally evaluated on Relative Global Composite Performance and/or other qualitative factors as the Board or Executive Director may determine to be appropriate. The Executive Director is generally evaluated on Relative Global Composite Performance and qualitative metrics reflecting overall agency leadership, management, communications, policy matters, staff development, and the implementation of agency strategic initiatives as reflected in ERS' Operating Budget.

4.6 Participants shall be notified of their Performance Goals before the beginning of the plan year or as soon as practicable thereafter. For an employee who becomes a Participant after the beginning of a plan year, the Participant shall be notified of his/her Performance Goals before his/her Eligibility Date or as soon as practicable thereafter. Any change to a Participant Goal Sheet during a plan year must be approved by the Executive Director. Any change to the Performance Goals of the Executive Director must be approved by the Board.

4.7 The following principles shall apply to the development of Performance Goals:

(a) All Investment Professionals shall be evaluated on qualitative and quantitative Performance Goals. Qualitative Performance Goals shall comprise 25% of each Investment Professional's overall Participant goals, and quantitative Performance Goals shall be the remaining 75% of overall Participant goals, with a minimum of 35% of overall Participant goals to be based on Relative Global Composite Performance. To the extent any Investment Professional does not have meaningful quantitative measures, such as comparisons to Benchmarks or other quantitative measures, the default will be to Relative Global Composite Performance for the entire 75% quantitative portion (see Appendix B).

(b) **Qualitative**. All Investment Professionals are evaluated on discretionary Performance Goals that are qualitative measures reflecting individual achievement, position-specific performance objectives, and ERS' strategic and operational goals.

(c) **Quantitative.** As reasonably and prudently possible, the Investments Division manages the Trust Fund consistent with the policy asset allocations set forth in the Investment Policy or, during any transition to a new asset allocation, as determined by the Board.

(i). Quantitative Performance Goals shall correlate to the Benchmarks and Information Ratios identified in the Risk Budget.

(ii). All Investment Professionals are evaluated on Relative Global Composite Performance to encourage focus on a shared mission for the prudent successful performance of the overall investment program.

(iii). In managing the Trust Fund, the Investments Division assigns individual Investment Professionals responsibility for managing subcategories of Asset Classes, Individual Portfolios reasonably derived from the Risk Budget. Performance Goals that include these subcategories must include the rationale for how each subcategory rolls up into the Asset Classes and how the proposed Benchmark and proposed Maximum Performance Goal for such subcategory are consistent with the Risk Budget so that it can be independently verified by internal and external auditors.

4.8 **Performance Period Weightings.** Participants shall have quantitative Performance Goals measured for the most recent one-year period until three-year and five-year records are available for the Participant, weighted consistent with Appendix B. For any Participant that has not completed a full three-year and/or five-year period of performance as of the end of the current plan year based on his/her Original Eligibility Date, the Participant's quantitative Performance Goals shall not include a three-year and/or five- year Performance Period, as applicable.

(a) **Less than Three Years of Performance.** If a Participant has fewer than three years of performance under the Plan, 100% weighting of all quantitative Performance Goals shall be attributed to the one-year Performance Period. A Participant with less than one year of performance under the Plan shall be limited to an Incentive Compensation Award for a prorated period from his/her Eligibility Date.

(b) **Three to Five Years of Performance.** If a Participant has at least three but fewer than five years of performance under the Plan, 40% weighting of all quantitative Performance Goals shall be attributed to the one-year Performance Period, and 60% weighting shall be attributed to the three-year Performance Period.

(c) **Five or More Years of Performance.** If a Participant has at least five years of performance under the Plan, 20% weighting of all quantitative Performance Goals shall be attributed to the one-year Performance Period, 30% weighting shall be attributed to the three-year Performance Period, and 50% weighting shall be attributed to the five-year Performance Period.

(d) **Inception-to-Date for Public Market Equivalents.** The public market equivalent Performance Goals shall be excluded from the one, three, and five-year Performance Period Weightings described above. The Realization Percentages for the public market equivalent Performance Goals shall be calculated based on an internal rate of return and measured using an inception-to-date Performance Period with a 100% weighting attributed to the inception-to-date Performance Period. Such calculation and measurement is consistent with industry practice for illiquid private-market investments where performance is reliant on the timing of cash flows.

4.9 Participant Goal Sheets shall include, but not be limited to, the following as applicable:

(a) Hire date, Original Eligibility Date, Weighted Salary, Performance Goal Weighting and Performance Period Weighting consistent with Appendix B, Maximum Incentive Award Percentage, Maximum Incentive Award, Plan Group, and payroll title.

(b) Sufficient detail for each Performance Goal, including whether the Performance Goal is quantitative or qualitative.

(c) For each quantitative public market equivalent Performance Goal as specified in Appendix B, the Benchmark and Maximum Performance Goal must be consistent with the Risk Budget.

(d) A written recommendation by the CIO or other applicable division director regarding the realization amount for each Participant's discretionary Performance Goals, subject to the approval of the Executive Director.

(e) The date of any change in job position, Asset Class, or Individual Portfolio if the change shall result in a prorated calculation of the Participant's Incentive Compensation Award. The date used for the prorated calculation will be the first day of the first full month following the date of any change.

(f) Any other factor that may be necessary to calculate an Incentive Compensation Award with justification for the additional factor(s). (For example, the plan year performance guidelines should reflect all changes to standard one-year, three-year, and five-year Performance Periods if performance cannot be reasonably calculated for those standard Performance Periods despite the Participant's having that period of service under the Plan.) Factors that should have been included in the Participant Goal Sheet but were omitted may not be used in the calculation of an Incentive Compensation Award unless those additional factors are approved by the Executive Director (or, in the case of the Executive Director, by the Board).

5. Calculation of Incentive Compensation Awards

5.1 Promptly after the end of each plan year, the Custodian shall summarize Relative Global Composite Performance and provide Relative Performance of Asset Classes and Individual Portfolios. The Investments Division shall review the information provided by the Custodian. All details regarding performance shall be provided directly from either the Custodian or the designated staff, as noted in this Section, to a Third Party Reviewer for independent validation. The records used to calculate performance for Incentive Compensation Awards shall be maintained for seven (7) years following the applicable plan year.

5.2 All performance measures, except for Relative Global Composite Performance, exclude risk management securities used for asset allocation rebalancing purposes. Risk management securities used to manage risk at the portfolio level are included in that portfolio's performance and are rolled into the applicable Asset Class performance and Relative Global Composite Performance.

5.3 All performance measures, except for Relative Global Composite Performance, exclude the effect of cash transfers in individual portfolios, due to asset allocation rebalancing transactions, between trade date and settlement date of the associated trade program.

5.4 Pursuant to Section 4.9(d), the Realization Percentages for each Participant's discretionary Performance Goals will be incorporated into the calculation of Incentive Compensation Awards subject to final approval by the Executive Director.

5.5 The Executive Director shall designate an individual to calculate Incentive Compensation Awards. The performance information provided by the Custodian and other sources as detailed in Sections 4.9(d) and 5.1 shall be used to calculate Incentive Compensation Awards for Participants based on achievement of the Performance Goals. For each Participant, calculations in the form of a final Participant Goal Sheet with actual performance and realization data shall be provided to the Director of Human Resources and other relevant Leadership Employees for review and approval. An independent review will be performed by a Third Party Reviewer to verify the accuracy of proposed compensation calculations prior to submission to the Executive Director.

5.6 The realization of each quantitative Performance Goal for each Participant, when applicable, is calculated as a two-step process. First, the realization of each Performance Goal (Realization Percentage) is expressed as a percentage up to a maximum of 100% for the Performance Goal. The Realization Percentage for each Performance Goal is then weighted by multiplying the applicable Performance Period Weighting by the applicable Performance Goal Weighting to determine Weighted Realization Percentage. The calculations are further discussed in Appendix C.

5.7 The Incentive Compensation Award for each Participant shall be the sum of all Weighted Realization Percentages as determined pursuant to Section 5.5. The aggregate Weighted Realization Percentages for all Performance Goals are then multiplied by the Maximum Incentive Award in the Participant's Participant Goal Sheet, consistent with the maximum percentages set forth in Appendix A.

5.8 Following a review and validation of the calculations of Incentive Compensation Awards by the Director of Human Resources and the Third Party Reviewer, the payment recommendations based on the Participant Goal Sheets shall be submitted to the Executive Director for final approval.

5.9 The Board must approve payment of Incentive Compensation Awards to the Executive Director. Such payment may be based on the Plan Year performance of the Executive Director, which may generally be reflected in the accomplishments contained within the annual operating budget approved by the Board, or any other manner as the Board may determine. The Executive Director's Performance Goals include those specified in Section 4.5 of the Plan or as otherwise determined by the Board.

6. Incentive Compensation Award Payments and Limitations.

6.1 Payments of Incentive Compensation Awards shall be subject to all terms and conditions of the Plan, including any Clawback as specified in Section 6.9. The Payment Schedule with respect to Incentive Compensation Awards for a plan year shall be the schedule specified in Section 6.2. In the event of non-positive Global Composite Performance for the one-year Performance Period, the Payment Schedule shall be extended to the extent provided in Section 6.3.

6.2 **Payment Schedule.** Subject to the terms and limits of the Plan and except as set forth in (d) and (e) below, payment with respect to an Incentive Compensation Award for a plan year shall be made in three (3) installments as follows:

(a) The first installment (year-one payment) shall be equal to 50% of the Incentive Compensation Award, and it shall be paid on the first Payment Date following the Plan Year in which the Incentive Compensation Award was earned.

(b) The second installment (year-two payment) shall be equal to 25% of the Incentive Compensation Award, and it shall be paid on the second Payment Date following the plan year in which the Incentive Compensation Award was earned.

(c) The third installment (year-three payment) shall be equal to 25% of the Incentive Compensation Award, and it shall be paid on the third Payment Date following the Plan Year in which the Incentive Compensation Award was earned.

(d) Payments with respect to Incentive Compensation Awards for Investment Operations Specialists shall be paid in two installments with each installment equal to 50% of the applicable Incentive Compensation Award. The first installment (year-one payment) shall be paid on the first Payment Date following the plan year in which the Incentive Compensation Award was earned, and the second installment (year-two payment) shall be paid on the second Payment Date following the plan year in which the Incentive Compensation Award was earned.

(e) Payments with respect to Incentive Compensation Awards for Investment Administrative Support shall be paid in one installment on the first Payment Date following the plan year in which the Incentive Compensation Award was earned.

(f) For Participants who change Payment Schedules during the plan year, the Incentive Compensation Awards will be prorated and paid out based on the Payment Schedule assigned to the respective Plan Groups at the time.

6.3 If Global Composite Performance for the one-year Performance Period in the current plan year is not positive, then all Incentive Compensation Awards that otherwise would have been paid on the next Payment Date (including incentive compensation based on Performance Goals not related to Global Composite Performance and previously earned Incentive Compensation Awards remaining to be paid pursuant to the respective Payment Schedule) shall not be paid until the first Payment Date immediately following the next plan year in which the one-year Performance Period for Global Composite Performance is positive.

6.4 The Board or Executive Director, as applicable, has the discretion to increase or decrease Incentive Compensation Awards earned and/or to limit payments of Incentive Compensation Awards even if there is positive Global Composite Performance.

6.5 A Participant must be an active full-time ERS employee on the Payment Date on which an Incentive Compensation Award is payable to receive any portion of the Incentive Compensation Award payable on such Payment Date, except to the extent Section 6.8 or Section 6.8.1 applies. Each Participant shall forfeit his/her right to any future payment under the Plan upon ceasing to be an active full-time ERS employee, except to the extent Section 6.8 or Section 6.8.1 applies. This Section is consistent with a principal purpose of the Plan, which is to encourage high-performing employees to remain with ERS. For the purposes of the Plan, an employee on approved extended leave such as sick leave, Family Medical Leave (FML), or Parental leave remains an active full-time ERS employee eligible to receive payment of an Incentive Compensation Award subject to the limitations of Section 6.7 and other applicable limitations of the Plan.

6.6 If an employee is a Participant for part but not all of a Plan Year, the amount of the employee's Incentive Compensation Award for such Plan Year shall not be greater than the amount of the award that the Participant would have received had he/she been a Participant for the entire Plan Year. In this instance, the Incentive Compensation Award shall be limited to a pro rata portion of the award for the entire Plan Year as set out in Section 3.2.

6.7 **Extended Leave.** Incentive Compensation Awards are for outstanding performance while at work. Excluding sick leave, FML, and Parental leave (for which no proration is required), if a Participant is absent from work for more than thirty (30) days during a plan year resulting from an approved extended leave, any Incentive Compensation Award for such plan year

may be prorated to reflect the Participant's absence from work.

6.8 **Death/Disability.** In the event of death or termination of employment due to Disability, a Participant forfeits any Incentive Compensation Award for the current Plan Year unless the termination of employment occurs on August 31st of the current Plan Year. Incentive Compensation Awards earned for prior plan years that have not been paid pursuant to Section 6.2 or 6.3 shall become payable as soon as administratively practicable. Payments under this Section shall be made either to the estate of the deceased employee or the employee terminated due to Disability, subject to the terms and limits of the Plan.

6.8.1 **Retirement.** In the event of termination of employment due to retirement, a Participant forfeits any Incentive Compensation Award for the current Plan Year unless the termination of employment occurs on August 31st of the current Plan Year. Incentive Compensation Awards earned for prior plan years that have not been paid pursuant to Section 6.2 or 6.3 shall be payable on the next Payment Date that follows the Participant's retirement and is not deferred under Section 6.3, subject to the terms and limits of the plan. In the event of death after retirement, section 6.8 shall apply. For purposes of this section, retirement occurs when:

(a) the Executive Director (or the Board, in the case of the Executive Director's retirement) receives a retirement request from a Participant at least 60 days prior to the retirement date;

(b) the Executive Director (or the Board) determines that the Participant is in good standing and approves the retirement date in advance;

(c) the Participant retires under the jurisdiction of ERS or retires under the jurisdiction of the Teacher Retirement System of Texas (TRS) as the result of a transfer of ERS service credit under Chapter 805 of the Texas Government Code (regarding credit transfers between ERS and TRS); and

(d) the Participant is immediately eligible to receive and receives a retirement annuity that is based on age and amount of service credit or based on combined service credit under Chapter 803 of the Texas Government Code (regarding the Proportionate Retirement Program)

Pursuant to Treasury Regulation Sections 1.409A-2(b)(2)(i) and 1.457-12(d)(2), the payment under this Section 6.8.1 shall for all purposes be treated as a separately identifiable payment to which a Participant is entitled under the Plan. This Section 6.8.1 shall be administered in accordance with Code Section 409A and 457(f).

6.9 **Clawback.** If a Participant is found to have (a) materially violated any provision of the Plan, (b) managed or invested the assets of ERS in a manner that is not considered prudent or failed to exercise reasonable care consistent with ERS' fiduciary duty, (c) been awarded, whether paid or not, any Incentive Compensation Award based on materially incorrect information, or (d) otherwise failed to act in accordance with the requirements of applicable law, ERS' Standards of Conduct, ERS' fiduciary authority, or any other ERS policy or procedure, the Board or the Executive Director, in their sole discretion, may require the Participant to repay all or part of any incentive compensation paid to Participant. This Section shall apply to the extent a violation is discovered within four (4) years from any payment of an Incentive Compensation Award unless circumstances later come to the attention of the Board or Executive Director that could not reasonably have been discovered within four (4) years, in which case the four-year period shall run from the date such circumstances were or reasonably should have been discovered. The Board, as it relates to the Executive Director, and the Executive Director, as it relates to all other Participants, has the

discretionary authority to make all final determinations with regard to mismanagement or noncompliance on a case-by-case basis. Mismanagement and/or noncompliance with the Plan and/or the Trust Fund rules could also result in disciplinary action, up to and including removal of the Participant from the Plan, termination of employment, and referral to the appropriate law enforcement authority, if appropriate.

6.10 **Funding of the Plan.** The Plan shall be funded with dollars generated by Global Composite Performance, Net of Fees. Before each Plan Year as part of the budget process, the Chief Financial Officer shall develop a Statement of Financial Impact for the plan year estimating the total potential cost of the Plan based upon achievement of the maximum payments to be awarded if all Performance Goals established in the Participant Goal Sheets were fully realized to the maximum level. Annually, prior to the beginning of each plan year, the Board shall approve the Statement of Financial Impact for the plan year to provide funds for the Plan in connection with ERS' annual operating budget. The funding of the Plan shall be sufficient to pay all Incentive Compensation Awards, both current and previously earned but not yet paid pursuant to the terms of the Plan. If there are insufficient funds to pay all Incentive Compensation Awards, the Executive Director shall have the discretion to decrease awards earned and/or limit payments.

6.11 **Reporting.** The Board may receive summarized reporting of Incentive Compensation Awards to be paid to Participants each plan year. This reporting is provided following the final approval of Incentive Compensation Awards by the Executive Director. The reporting may include details of any discretion exercised by the Executive Director pursuant to Section 6.4.

6.12 Human Resources and Finance shall review payments of Incentive Compensation Awards to confirm that all payments are made consistent with the payment recommendations approved by the Executive Director and/or the Board.

6.13 **Underpayment.** If it is discovered that an Incentive Compensation Award was incorrectly calculated and the Participant was underpaid, the Executive Director may approve a supplemental payment to make up the difference between the earned amount and the previously paid amount. In addition, any previously earned Incentive Compensation Award remaining to be paid pursuant to the respective Payment Schedule will be corrected to reflect the Underpayment. This Section shall apply to the extent that an Underpayment is discovered within four (4) years from any payment of an Incentive Compensation Award. The Participant must be an active, full-time ERS employee to be compensated for an Underpayment.

7. Plan Administration

7.1 The Plan shall be administered by the Board, as it relates to participation of the Executive Director, and by the Executive Director, as it relates to participation of other ERS employees, in accordance with the terms hereof, as amended from time to time. In administering the Plan, the Board or Executive Director, with input from ERS senior management, shall have discretionary authority to interpret the Plan and to administer the Plan in accordance with its terms.

7.2 All decisions of the Board and Executive Director, as applicable, shall be binding and conclusive on Participants and ERS. Subject to the provisions of the Plan, the Board or Executive Director, as applicable, shall have the discretionary authority to:

(a) approve participation in the Plan, including determining eligibility and Eligibility Dates for Participants;

(b) approve Participant Goal Sheets and all aspects of the calculations for computing Incentive Compensation Awards;

(c) evaluate the performance of Participants and grant Incentive Compensation Awards;

(d) exercise discretion in payment of Incentive Compensation Awards as discussed in Article 6;

(e) establish policies and procedures for the administration of the Plan;

(f) interpret the Plan and make all decisions necessary to administer the Plan; and

(g) delegate the authority to administer all or any part of the Plan to ERS employees who are not Participants in the Plan during the plan year.

7.3 The Board shall review the Plan annually, and it shall have the right to modify, or terminate the Plan entirely, or any portion thereof, at any time. Any modification to the Plan during a plan year shall not become effective until the beginning of the next plan year unless required by applicable law, regulation, or the Board's fiduciary duties.

7.4 If the Board or the Executive Director or a court, administrative body, or regulatory authority with appropriate jurisdiction determines that any portion of the Plan violates applicable state or federal laws or regulations, such portion(s) shall be deemed null and void, and the remaining provisions of the Plan shall remain in full force and effect to the extent consistent with the purposes of the Plan.

7.5 All incentive compensation records for the Plan shall be maintained by Human Resources. All performance records shall be calculated by the Custodian or an independent Asset Class consultant. All records shall be maintained for seven (7) years following the applicable Plan Year.

8. Miscellaneous

8.1 Participants are not permitted to and shall not voluntarily or involuntarily assign, encumber, or transfer their rights under the Plan, and such rights are not subject to anticipation, adjustment, alienation, encumbrance, garnishment, attachment, or levy of any kind. Any attempt to do so will render the Participant's rights under the Plan null and void.

8.2 Nothing in the Plan shall be deemed to give any interest in or right or title to any specific property of ERS to any employee or Participant or any heir, estate, personal representative, or beneficiary of any Participant, and neither the establishment of the Plan nor the earnings calculation or payment of Incentive Compensation Awards shall be deemed to create a trust, entitlement, property right, or contract right on behalf of any Participant, heir, estate, personal representative, or beneficiary. The Plan is an unfunded, unsecured contingent liability of ERS to make payments in accordance with the provisions of the Plan. All amounts budgeted for Incentive Compensation Award payments by ERS shall be considered assets of the Trust Fund, and no employee or Participant shall have any contract or property right, security, or other interest in any asset of ERS by reason of the Plan.

8.3 ERS shall withhold from any payment made hereunder such amounts as it, in its reasonable judgment, deems necessary to comply with the withholding requirements of applicable federal, state, and local income and employment tax laws.

8.4 At no time shall any ERS employee:

(a) have any right to be selected as a Participant for any plan year or, if selected as a

Participant, remain in the Plan even if he/she received or earned an Incentive Compensation Award in a prior plan year; or

(b) have any right or be entitled to receive, earn, or be paid an Incentive Compensation Award under the Plan, even if selected as a Participant for the plan year.

8.5 The Plan is not a contract for employment or for any other purpose. All grievances related to the Plan must comport with and shall be addressed in accordance with the ERS General Complaint Policy, as set out in the ERS Personnel Policy and Procedure Manual. ERS is an "at will" employer. The Executive Director serves at the pleasure of the Board, and other Participants serve at the pleasure of the Executive Director. Nothing in the Plan, eligibility to participate in the Plan, or the earning or awarding of Incentive Compensation Awards shall affect the at-will nature of employment of ERS employees or impair ERS' right to terminate a Participant's employment at any time with or without cause.

8.6 All Incentive Compensation Awards shall be based on pre-determined goals for prospective performance only. No incentive compensation shall be awarded retrospectively for past performance, to a Participant who has been placed on employment probation, or to a Participant who fails to meet any requirement of the Plan.

8.7 All Incentive Compensation shall be treated as wages for federal income tax purposes but shall not be considered for purposes of the calculation of retirement benefits or disability, life, or accidental death insurance or other death benefits.

8.8 The Plan is intended to comply with the short-term deferral exemptions from Internal Revenue Code Sections 409A and 457, as provided in federal tax regulations and other guidance issued pursuant to those Code Sections. It is intended that all amounts payable under the Plan be subject to a substantial risk of forfeiture within the meaning of the Internal Revenue Code Section 457(f) until paid, and the Plan shall be interpreted and administered in accordance with such intent. If the Plan is determined by an appropriate authority to be inconsistent or in conflict with any applicable law, regulation, or ERS policy, the Participant agrees that he or she shall not be entitled to receive, and ERS shall not be obligated to pay, any payment pursuant to the Plan, even if the Participant has already satisfied the requirements for such payment of the Incentive Compensation Award. It is intended that the provisions of the Plan be construed and administered in such a manner that it will be considered in compliance with all applicable state and federal laws and regulations.

8.9 Either the Board or the Executive Director may amend any provision of the Plan or add or delete language that they deem necessary to ensure the Plan's compliance with applicable laws and regulations, including those provisions of the Internal Revenue Code governing the intended tax consequences of the Plan. Any reference in the Plan to “retirement” or "termination of employment" or a similar term shall be deemed to mean "separation from service" within the meaning of Internal Revenue Code Section 409A(a)(2)(A)(i).

APPENDIX A

Plan Groups	Maximum Incentive Award Percentages	Payment Schedules (Year 1/2/3, see Section 6.2)
Executive Director	100%	50/25/25
Chief Investment Officer	100%	50/25/25
Deputy Chief Investment Officer	100%	50/25/25
Managing Director	100%	50/25/25
Program Director	90%	50/25/25
Supervising Portfolio Manager	90%	50/25/25
Portfolio Manager IV, V & VI	80%	50/25/25
Portfolio Manager I, II & III	70%	50/25/25
Chief Trader I & II	70%	50/25/25
Investment Analyst V & VI	70%	50/25/25
Trader I, II & III	65%	50/25/25
Investment Analyst III & IV	58%	50/25/25
Investment Operations Manager	50%	50/25/25
Investment Analyst I & II	35%	50/25/25
Performance Specialist	35%	50/25/25
Investment Operations Specialist	25%	50/50/0
Investment Administrative Support	5%	100/0/0
Deputy General Counsel (Investment Attorney)	90%	50/25/25
Senior Investment Attorney	80%	50/25/25
Investment Attorney	70%	50/25/25
Investments and Securities, Paralegal	35%	50/25/25

APPENDIX B

PERFORMANCE GOAL WEIGHTINGS FOR INVESTMENT PROFESSSIONALS AND LEADERSHIP EMPLOYEES

Any variations from these weightings shall be approved by the Executive Director.

Main Category Weights	Main Category	Sub Category	Exec. Director	~~CIO Dep. CIO Inv. Serv.~~ Investment Admin. & Solutions	Credit & Hedge Funds	Portfolio Mgmt.	Private Equity	Public Equity	Real Assets	Treasury & Trading	Legal Services
25% Maximum (excluding ED)	Discretionary		50% (5)	25%	25%	25%	25%	25%	25%	25%	25%
35% Minimum	Global Composite Performance		50%	75%	35%	~~X~~75%	35%	35%	35%	35%	35%
40% Maximum		A combination of one or more of the following, as indicated below (1):									
		Global Public Equity						X			
		Internal Global Public Equity						X			
		Individual Portfolios			X	~~X~~		X		X	
		~~Internally Traded Portfolios~~								~~X~~	
		~~Trading Performance~~								~~X~~	
		Public Credit			X						
		Private Credit			X						X
		Rates								X	
		Private Equity Public Market Equivalent (2)					10%				X
		Private Equity Peer Comparison (3)					30%				X
		Private Real Estate Public Market Equivalent (2) (4)							X		X
		Public Real Estate							X		
		Private Infrastructure Public Market Equivalent (2)							X		X
		Hedge Funds			X						X

See footnotes on the following page.

APPENDIX B

Footnotes:

1) When fixed percentages are not set forth above (as indicated with an "X"), category weightings will be determined at the individual level based on the Asset Class and individual responsibilities. These weightings will be determined prior to the Plan Year and approved by the Executive Director.
2) The Public Market Equivalent is a calculation that determines a comparable internal rate of return assuming ERS invested in a public benchmark while accounting for its specific cash flows.
3) Peer group comparison will be provided by ERS' external consultant and compares ERS investments to a universe of comparable funds.
4) The Private Real Estate asset class benchmark is a blended public real estate benchmark to account for core and non-core funds.
5) Based on overall agency leadership, management, communications, policy matters, staff development, and the implementation of agency strategic initiatives. The agency's strategic initiatives are reflected in the Operating Budget as approved by the Board of Trustees in its August meeting.

APPENDIX C

Plan Calculation Methodologies

The realization of each Performance Goal for each Participant, when applicable, is calculated as a two-step process. First, the realization of each Performance Goal is expressed as a percentage *up to a maximum of 100% for the Performance Goal*. Percentages realized for each Performance Goal are then weighted by multiplying the applicable Performance Goal Weighting. The calculation is demonstrated as follows:

Trust Fund, Asset Class, and Individual Portfolios. To determine the Realization Percentage for a Performance Period, the calculation is Relative Performance for such Performance Period, then divided by the Maximum Performance Goal for the relevant Performance Period. The resulting Realization Percentage is then multiplied by the Performance Goal Weighting to determine the Weighted Realization Percentage. This calculation is reflected in the following formulas.

STEP 1:

Realization Percentage (Cannot be greater than 100%) = **Relative Performance / Maximum Performance Goal**

STEP 2:

Weighted Realization Percentage = **Realization Percentage (Step 1)** x **Performance Goal Weighting**

Hedge Funds Portfolio. The hedge fund portfolio will be measured against a quantitative metric of a target return as detailed in a memo approved by the Executive Director before the start of each Plan Year..

Private Equity. The private equity portfolio will be measured against a Private Equity Peer Comparison benchmark and a Private Equity Public Market Equivalent benchmark as detailed in a memo approved by the Executive Director before the start of each Plan Year.

Private Real Estate. The private real estate portfolio will be measured against a Private Real Estate Peer Comparison benchmark as detailed in a memo approved by the Executive Director before the start of each plan year.

Private Infrastructure. The private infrastructure portfolio will be measured against a Private Infrastructure Public Market Equivalent benchmark as detailed in a memo approved by the Executive Director before the start of each plan year.

APPENDIX D
Maximum Incentive Award Calculations

Example 1
Salary increase (e.g. merit or equity) for Financial Analyst IV effective March 1 with no change in Participant's **Maximum Incentive Award Percentage** of **25%**.

Month	Annual Salary	
Sep	$95,000	
Oct	$95,000	
Nov	$95,000	
Dec	$95,000	
Jan	$95,000	
Feb	$95,000	
Mar	$105,000	Salary increase effective March 1
Apr	$105,000	
May	$105,000	
Jun	$105,000	
Jul	$105,000	
Aug	$105,000	

Weighted Salary = **$100,000** (calculated by averaging the figures from each month)

Maximum Incentive Award = **Weighted Salary** X **Maximum Incentive Award Percentage**
= **$100,000** X **25%**
= **$25,000**

Example 2
Promotion from Financial Analyst IV to Investment Analyst I effective March 1 with a change in Participant's **Maximum Incentive Award Percentage** from **25%** to **35%**.

Month	Annual Salary	Maximum Incentive Award %	
Sep	$95,000	25%	
Oct	$95,000	25%	
Nov	$95,000	25%	
Dec	$95,000	25%	
Jan	$95,000	25%	
Feb	$95,000	25%	
Mar	$105,000	25%	Salary increase effective March 1
Apr	$105,000	35%	Maximum Incentive Award Percentage increase effective April 1
May	$105,000	35%	
Jun	$105,000	35%	
Jul	$105,000	35%	
Aug	$105,000	35%	

Weighted = **$100,000** & **29.16667%** (calculated by averaging the figures from each month)

Maximum Incentive Award = **Weighted Salary** X **Weighted Maximum Incentive Award Percentage**
= **$100,000** X **29.16667%**
= **$29,166.67**