

**TEACHER RETIREMENT SYSTEM OF TEXAS MEETING
BOARD OF TRUSTEES
AND
COMPENSATION COMMITTEE**

(Committee Chair and Members are Subject to Change at the September Board Meeting - Mr. Kelly, Chair; Ms. Clifton; Mr. Colonna; Ms. Palmer & Ms. Sissney, Committee Members)

AGENDA

**September 13, 2012 – 11:00 a.m.
TRS East Building, 5th Floor, Boardroom**

1. Consider the approval of the proposed minutes of the September 15, 2011 committee meeting – Committee Chair.
2. Consider recommending to the Board adoption of a Performance Incentive Pay Plan for performance periods commencing October 1, 2012 and each October 1 thereafter – Jerry Albright.

NOTE: The Board of Trustees (Board) of the Teacher Retirement System of Texas will not consider or act upon any item before the Compensation Committee (Committee) at this meeting of the Committee. This meeting is not a regular meeting of the Board. However, because a quorum of the Board may attend the Committee meeting, the meeting of the Committee is also being posted as a meeting of the Board out of an abundance of caution.

Tab 1



Teacher Retirement System of Texas

Minutes of the Compensation Committee

September 15, 2011

The Compensation Committee of the Board of Trustees of the Teacher Retirement System of Texas (TRS) held a meeting on Thursday, September 15, 2011 in Room E 345 of the TRS East Building offices at 1000 Red River Street in Austin, Texas 78701.

The following members of the committee were present:

- David Kelly, Chair
- Charlotte Clifton
- Joe Colonna
- Anita Palmer
- Nanette Sissney

Other TRS Board members present:

- Todd Barth
- Karen Charleston
- Eric McDonald
- Chris Moss

Others present:

- Brian Guthrie, Executive Director, TRS
- Ronnie Jung, Executive Liaison to the Board of Trustees, TRS
- Conni Brennan, General Counsel, TRS
- Annette Dominguez, Director of Human Resources, TRS
- T. Britton Harris IV, Chief Investment Officer, TRS
- Betsey Jones, Director of Special Projects, TRS
- Jerry Albright, Deputy Chief Investment Officer, TRS
- Jase Auby, Director, Portfolio Strategy and Execution, TRS
- Tina Carnes, Assistant General Counsel, TRS
- Chi Kit Chai, Senior Managing Director, Internal Public Markets, TRS
- Mike Debbs, Compensation Analyst, TRS
- Lynn Lau, Assistant Secretary to the Board and Program Specialist
- Dale West, Senior Director, External Public Markets, TRS
- Brady O'Connell, Hewitt EnnisKnupp
- Ann Fickel, Texas Classroom Teachers Association
- Josh Sanderson, Association of Texas Professional Educators
- Ted Melina Raab, Texas AFT

Committee Chair David Kelly called the meeting to order at 1:55 p.m. with a quorum of committee members present.

1. Consider the approval of the proposed minutes of the August 12, 2011 committee meeting – David Kelly.

On a motion by Ms. Clifton, seconded by Ms. Sissney, the committee unanimously approved the minutes of the August 12, 2011 committee meeting, as presented.

2. Review and discuss the compensation structure for TRS investment personnel, including comparing TRS's base and performance incentive compensation to other public and private funds – Ronnie Jung and Brian Guthrie.

Per Mr. Kelly's request, Mr. Jung provided a historical overview of the development of the Performance Incentive Pay Plan. He stated that he first designed a performance incentive pay plan (plan) to recruit a chief investment officer (CIO). He stated that the plan was capped at 75 benchmark of base salary based on a 100 percent benchmark. He said that after the board hired Mr. Harris as the CIO, Mr. Harris established a new investment strategy, set a 10-year goal to add 130 basis points over the benchmark, and presented a new incentive pay plan for investment personnel. Mr. Jung said that Mr. Harris worked with McLagan Partners (McLagan) to achieve a top-quartile position among public funds for base pay. He said that upon the legislative authority, the board adopted the first plan. Mr. Kelly noted that it was a positive change made by the legislature to provide the board the autonomy to approve incentive pay plans.

Mr. Guthrie presented a detailed comparison of salaries and compensation of TRS investment staff by position to public and private sector market data. Mr. Guthrie stated that the comparison used market data from McLagan's private sector surveys and the public sector data from 60 participating public pension funds. He noted that McLagan had eliminated the stock grants/options ("long-term deferrals") from the compensation comparison as they are not available for the public sector. Mr. Guthrie confirmed for Mr. Barth that the charts reflect the actual salaries paid to TRS investment personnel in 2010. Mr. Jung noted that the actual bonuses were earned in 2010, half of which was paid in 2011, with the rest scheduled to be paid in 2012. Responding to a question from Mr. Barth, Mr. Albright explained that endowments were not included in the comparison because their salaries are much higher.

Mr. Guthrie presented a comparison of TRS investment staff base salaries and maximum payouts with those of public and private sectors. Presenting the public funds base pay targets, Mr. Guthrie stated that the guidelines TRS uses internally are consistent with the practice of other public funds, such as California Public Employee Retirement System (CalPERS) and California State Teacher Retirement System (CalSTRS). He presented a comparison of TRS' salary by position with large public funds and the private sector grouped at different percentiles. Based on the comparisons of base salary, minimum and maximum ranges of salaries, eligibility for an incentive, and maximum award in a percentage of their base pay, he said, TRS was in the range of other public funds that participated the study. Mr. Jung noted that University of Texas Investment Management Company (UTIMCO) and other Texas-based funds were included in this study. Responding to a question from Mr. Kelly relating to the current situation with retention, Mr. Albright stated that most of the turnovers occurred at the higher ranking level but it had been quite stable over the past two years.

Mr. Guthrie also presented a comparison of the incentive plan's key design elements. He noted that the surveyed plans were the same plans used in the salary comparison study, though three out of twelve funds contacted currently did not offer an incentive pay plan. Comparing the eligible positions for incentive pay, Mr. Guthrie stated that two funds expanded their plan to all investment management and support staff as TRS, four funds included only investment management staff and three included investment management staff and a few other positions. He also compared the maximum incentive and noted that UTIMCO had the 300 percent maximum, compared with 125 percent maximum of TRS' plan. Mr. Jung noted that historically there were CIOs who left TRS to work for an endowment.

Mr. Guthrie further compared how performance was measured among different funds. He stated that TRS' incentive pay was based on 50 percent performance to benchmarks, 30 percent to peer group, and 20 percent to qualitative measures. Compared with TRS, he said, five funds based their incentives on a mix of benchmarks and qualitative performance and four funds based that completely on performance to benchmarks. Mr. Jung stated that while TRS only had 50 percent tied to the benchmarks, none of the funds had less than 70 percent tied to their benchmarks, which made TRS deviate from the rest of the funds. He noted that TRS' plan design based 30 percent on whether the fund beat the median of the peers.

Responding to a question from Mr. Colonna, Mr. Albright explained that by peers, it was based on the TUCS peer group—funds with over \$10 billion of total asset. Mr. Jung noted that the plan required that investment staff would only be eligible for incentive compensation if the performance exceeded the benchmark or the fund was ranked in the top half of the peer group. Mr. Jung confirmed for Mr. Colonna that once that requirement was met, the 20 percent qualitative measures would be incorporated. Different from other funds, he said, the plan only required a performance to be in excess of the passive benchmarks or the peer group comparators in order to be eligible for compensation.

Responding to a question from Ms. Palmer regarding the performance prior to the implementation of the current incentive pay plan, Mr. Jung stated that it was in the 30 to 50 basis point range over the benchmarks. He stated that Mr. Harris' implementation of the new asset allocation and diversification strategy had significantly added alpha to the fund and thereby the performance goal as well as the incentives were set much higher.

Responding to a question from Mr. Kelly, Mr. Guthrie confirmed that none of the other funds included in the survey had a performance to peer group component in their plan design. Mr. Albright confirmed for Mr. Kelly that historically the peer group component had shown a normalizing effect which would lower the payouts but keep them more stable. Mr. Jung noted that the challenge of having the peer element was to testify to the legislature why incentives were being paid out in a down-year when the fund beat the peer without beating the benchmark. Responding to a question from Mr. Kelly, Mr. Jung stated the addition of the peer component was a policy decision and the plan design was overall very reasonable. He opined that although it is difficult to justify paying bonuses when the fund underperformed its benchmark, he understood that during the down years, the fund could still be in the top quartile on performance when it had lost less than other funds. He noted that he believed that the peer performance was driven by asset allocation, which had been driving at least 90 percent of the fund performance

and that staff should get credit for their recommendations to the board on asset allocation. Mr. Kelly opined that the peer group comparison over time should normalize out because it is an asset allocation issue, which is decided by the board with staff's recommendations.

Mr. Guthrie continued presenting the plan's key design elements: measurement period, payout period, and payout during negative return years. He stated that TRS' three-year performance period was in line with other funds that were surveyed. However, he noted, the payout period, which currently spread over two years (half paid the first year, and half the second), deviated from other funds, five of which paid annually in full, three spread over three years, and one spread over two years. Mr. Guthrie opined that TRS' current payout period worked out well and was a good plan design.

Concerning paying in a negative-return year, he said that at TRS, payments were deferred until the next positive return year, while three funds paid in full regardless of the value of the return, two funds forfeited the incentives entirely during negative return years, and two funds deferred the incentive at least one year. There was a discussion relating to the Senate Finance Committee hearing in 2009, in which UTIMCO was criticized for awarding their CEO a big bonus despite the fund's investment loss. Mr. Jung stated that the Senate Finance Committee members did not appreciate the argument that UTIMCO's loss in that down year was less than other funds. Mr. Kelly stated that the decision TRS had made during that time to defer payment was respectful and accepted by the legislature. Mr. Jung stated that TRS staff keeps the legislature abreast of TRS' policies and tries to accommodate their expectation.

3. Consider making recommendations to the Board regarding amendments to the Performance Incentive Pay Plan – Jerry Albright.

Mr. Albright presented the revised addendum C for the performance incentive pay plan. Mr. Albright stated that replacing the current addendum C with the revised version would keep the plan aligned with the Investment Policy Statement (IPS).

On a motion by Ms. Sissney, seconded by Ms. Clifton, the committee voted unanimously to recommend that the board adopt the revised addendum C presented by staff.

4. Consider recommending to the Board the adoption of a resolution regarding salary limits for the following particular employees: the Chief Investment Officer, Deputy Director Investment Officer, Deputy Administrative Officer, and the seven Investment Fund Directors listed as exempt positions in the 2012 - 2013 General Appropriations Act – Brian Guthrie.

Mr. Guthrie explained the background of the exempt position authority. He stated that the legislature controls the salaries of some of TRS staff through the exempt position authority provided in the appropriations bill. He stated that a maximum amount of salary was typically set for those positions. He noted that the board could override those limits and set a different upper limit for each position, which would be placed into the appropriations bill for the following biennium. If the board would like to make changes to those limits, Mr. Guthrie said, the board would need to take the action before he, as the executive director, could act within the limits set

for those positions. Responding to a question from Mr. Kelly, Mr. Guthrie stated that based on the survey presented today the current salaries for those positions were on target.

Mr. Guthrie presented the resolution with the amount left blank. He stated that the committee could choose to take no action, change the amount in percentage or dollar. He confirmed for Mr. Kelly that the resolution was intended to authorize the range of salary for the exempt positions. Responding to a question from Ms. Sissney, Mr. Guthrie stated that the salaries of the majority of those positions are beyond the salary structure set for most state employees. Mr. Harris stated that the investment personnel holding the exempt positions were satisfied with their salary range and would be comfortable with a recommendation of taking no action to the salary range regarding those exempt positions at this time. The committee decided not to recommend the resolution amending the not-to-exceed salary limits for the exempt positions and thereby took no action related to this matter.

The meeting adjourned at 2:40 p.m.

DAVID KELLY, CHAIR
COMPENSATION COMMITTEE
TRS BOARD OF TRUSTEES

Tab 2



Memorandum

DATE: August 30, 2012
TO: Compensation Committee; Board of Trustees
FROM: Legal Services
RE: Annual Review of Performance Incentive Pay Plan

Executive Summary of proposed changes to Performance Incentive Pay Plan for Performance Period commencing October 1, 2012

At its July 2012 meeting, the committee will review and discuss the Plan revisions proposed to be effective as of the commencement of the next Performance Period. The following materials are provided for your consideration:

1. Mr. Albright's presentation about the proposed Plan;
2. A proposed resolution to adopt the Plan;
3. A clean draft of the Plan, for ease of review;
4. A marked draft of the Plan, showing all proposed changes; and
5. A copy of Addendum A and Addendum B in the existing Plan effective October 1, 2011. The proposed plan has new addenda but they do not show marked changes, and inclusion of the existing addenda will aid comparison.

If acceptable, the Board will consider adoption in September. This memorandum summarizes the most significant revisions marked in the draft provided with your Board materials. Outside tax counsel has also reviewed the Plan revisions. Please note the following legend when reviewing the draft:

Additions are underlined in blue.

Deletions are ~~stricken through in red~~.

Moves within the document are double-underlined in green.

1. The proposed substantive changes are as follows:

- **Addendums A and B reflect IMD reorganization and revised performance comparison allocations.**

New Addendums A and B attached to the draft include the latest proposed changes that reflect changes in the “investment areas” and “peer groups within the IMD to be effective under the Plan as of October 1, 2012. In addition, the tables in those Addendums show as marked changes revisions to the allocations used to calculate Potential Awards under the Plan. These changes will affect the Potential Awards that can be earned in certain Eligible Positions.

- **Addendum C (IPS benchmarks) is deleted; IPS benchmarks, as modified from time to time, are incorporated by reference.**

In Section 4.6(a), the reference to Addendum C is deleted and replaced with language incorporating by reference the performance benchmarks adopted in the Investment Policy Statement, as amended from time to time, as the basis for calculating performance awards under the Plan. If a benchmark in the policy changes, the Plan benchmarks used for calculating performance awards are automatically changed on the same effective date (during a Performance Period). This fits the method actually used to calculate Potential Awards. This change is intended to obviate having to consider an amendment to the Plan when the Investment Policy Statement benchmarks have been amended. Addendum C is marked for deletion.

- **Employees leaving an Eligible Position within TRS can now earn an award for the final, partial Performance Period worked in the Eligible Position.**

Section 4.6(c) is marked for deletion. Section 4.6(c) currently provides that employees who leave Eligible Positions in the IMD for other positions within TRS during the Performance Period are *not eligible for an award under the Plan with respect to the partial Performance Period worked in an Eligible Position*. The proposed deletion would maintain the eligibility of an employee to receive an award in respect of the final, partial Performance Period. It is felt that the provision unfairly penalizes such employees by arbitrarily denying them a prorated award they might otherwise have earned during their final, partial Performance Period. Deleting the provision also removes any disincentive to voluntarily leave an Eligible Position during a Performance Period, even if that would be in the best interest of both of TRS and the employee. New Section 4.3(b)(v) addresses proration of awards for a partial Performance Period when a Participant accepts a TRS position outside the Plan.

- **Section 4.4(h) has been revised to provide that the qualitative performance component of the Maximum Award Opportunity will be based on a system of performance evaluation approved by the Executive Director.**

The existing language of Section 4.4(h) states that the intermediate levels of the qualitative component of the Potential Award are determined in “discrete quartiles.” This language is believed to be too narrow and that the Executive Director should have more flexibility to approve other systems of evaluation. Subsection (h) has also been reformatted for logical structure and readability.

- **The Plan has been clarified to provide that no changes will be applied retroactively, including benchmark or investment area changed, unless tax law requires it.**

Benchmark changes that occur because of changes in the Investment Policy Statement will take effect on the same date as they become effective in the Policy, but may not apply retroactively. However, if the IMD is reorganized during a Performance Period, the change will only be effective as of the commencement of the next Performance Period. The investment areas in effect at the beginning of the Performance Period will be used for all calculations relating to that period. However, if retroactive changes are required by tax laws or regulations, those will be permitted.

- **New Section 4.6(b) addresses the addition of new profit centers in the Investment Management Division.**

Calculation of performance for any new profit centers will be based on full Performance Periods. The provision also addresses allocations between one and three year performance by full Performance Periods.

- **Section 4.6(c) is no longer needed and has been deleted.**

The Plan now has three years of performance on which to base calculations of Potential Awards.

2. *Most of the marked changes are intended to clarify the Plan and improve readability.*

- Changes marked as moves are intended to improve the Plan's internal logical structure and improve readability.

- The Plan has been edited for consistent and uniform use of defined terms.

Examples: Replaced "investment division" with "IMD" throughout.

Replaced instances of "staff" with "employees" throughout.

- Undefined capitalized terms have been revised to lower case for readability.

Example: "Qualitative Performance" is now "qualitative performance."

- Long defined terms have been shortened to improve readability and reduce clutter.

Example: "Potential Performance Incentive Award" is now "Potential Award."

- Minor additions and clarifications have been added to Section 8, Definitions.

Example: Defined "investment area" and "profit center" by reference to Addendums A and B, where they are listed.

- Clarified when employment in an Eligible Position becomes effective during a Performance Period (Section 4.3(b)).

- Deleted transition language that is no longer needed (Section 4.6(c)).
- Section 7.2 further clarifies that the Plan creates no “property interest” with respect to any aspect of the Plan or an award.
- Addendums A and B have been edited to make it easier to read and understand the allocation plans in each Addendum and how they relate to the calculation of awards under the Plan.
- The investment areas in Addendums A and B have been updated to reflect organizational changes in the IMD.
- An automatically generated Table of Contents has been created to replace the manually prepared Table of Contents. This change will facilitate future editing if the Plan is amended in the future.



Performance Incentive Pay Plan

Jerry Albright
Deputy Chief Investment Officer
September 2012

Summary of Policy Changes

- Proposed Substantive Changes
 - Addendums A and B reflect IMD reorganization and revised performance comparison allocations

Fund Level	Total Fund	Internal Public	External Public	Private Equity	Risk		Real Assets	TAA	Public & Private	Natural Resources	Emerging Managers
					Risk ¹	Stable Value / SAA			SPN and Opportunistic ^{2, 3}		
Index	Total Fund Policy Composite Index	Global Equity Portfolio vs. MSCI ACWI Free (net)	Daily Weighted Excess Return Based on Actual Portfolio Weights	State Street Private Equity Index	Daily Weighted Excess Return Based on Actual Portfolio Weights		NCREIF	Total Profit & Loss for Incentive Period/Total Trust Average Daily Balance	Daily Weighted Excess Return Based on Actual Portfolio Weights		
Excess Return Target	100 bps	50 bps	100 bps	300 bps	75 bps	35 bps	250 bps	25 bps	175 bps	175 bps	100 bps

- Addendum C (IPS benchmark) is deleted; IPS benchmarks, as modified from time to time, are incorporated by reference
- Employee leaving an Eligible Position within TRS can now earn an award for the final, partial Performance Period worked in the Eligible Position
- Section 4.4(h) has been revised to provide that the qualitative performance component of the Maximum Award Opportunity will be based on a system of performance evaluation approved by the Executive Director
- The Plan has been clarified to provide that no changes will be applied retroactively, including benchmark or investment area changed, unless tax law requires it
- New Section 4.6(b) addresses the addition of new profit centers in the Investment Management Division
- Section 4.6(c) is no longer needed and has been deleted



¹Risk group allocation excludes Trust hedging activities

²Benchmark for Opportunistic portfolio is Total Fund Benchmark; Benchmark for Public SPN is the SPN Composite Index

³Daily weightings across Opportunistic portfolio, total Public SPN, total Private Equity SPN and total Real Asset SPN

Summary of Incentives

- Incentives Paid
 - Average amount earned since inception:

	<i>FY 2008</i>	<i>FY 2009</i>	<i>FY 2010</i>	<i>FY 2011</i>	<i>Total</i>
Maximum Award Potential	\$ 4,729,122	\$ 8,718,321	\$ 10,348,060	\$ 11,445,430	\$ 35,240,933
Total Calculated Award	\$ 2,470,537	\$ 4,414,985	\$ 6,308,748	\$ 6,144,861	\$ 19,339,131
% of Potential Awarded	52%	51%	61%	54%	55%
Actual Award Paid	\$ 2,165,241	\$ 4,342,234	\$ 6,158,703	\$ 3,072,430	\$ 15,738,608

- Approximate amount paid if 100% of excess is achieved for FY 2012 – FY 2013 is \$9 million



September 13 – 14, 2012
Board of Trustees

Item 7, Board Agenda

Whereas, the Board of Trustees (the "Board") of the Teacher Retirement System of Texas desires to adopt a Performance Incentive Compensation Plan for performance periods commencing on October 1, 2012 and each October 1 thereafter (the "Plan");

Now, therefore, be it

Resolved, That the Board hereby adopts the Plan as presented to be effective for the performance period commencing as of October 1, 2012 and ending on September 30, 2013;

Resolved, That the terms of the Plan will apply to each performance period commencing on each October 1 and ending on September 30, and will continue in effect for each subsequent performance period thereafter until the Plan is terminated, rescinded, superseded, repealed, or modified by further action of the Board or pursuant to applicable law; and

Resolved, That the Board's adoption of the Plan for the one-year performance period commencing on October 1, 2012 does not terminate, rescind, modify, repeal, or supersede the terms or conditions of any performance incentive compensation plans adopted by the Board relating to any prior performance period, as defined in each such plan.

Teacher Retirement System of Texas
PERFORMANCE INCENTIVE PAY PLAN

Effective October 1, 2012

This version of the Plan is effective for Performance Periods beginning on or after October 1, 2012. Any awards for performance in prior Performance Periods can become earned and payable subject to the terms and conditions stated in the versions of the Plan effective for those Performance Periods. No modification of the Plan may be given retroactive effect except as required to comply with applicable law, including federal tax laws and regulations.

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1. PERFORMANCE INCENTIVE PLAN PURPOSE AND AUTHORIZATION

To remain competitive in its efforts to attract and retain high caliber Investment Management Division (IMD) employees, the Teacher Retirement System of Texas (TRS) strives to offer a competitive compensation package. Awards of performance incentive pay based on specified performance criteria are an industry standard practice in the private investment sector and are rapidly becoming a standard practice in the public sector. By offering both a competitive base salary and performance incentive award opportunity, TRS enhances its ability to fulfill its mission to “prudently invest and manage the assets held in trust for members and beneficiaries in an actuarially sound system administered in accordance with applicable fiduciary principals.” Therefore, pursuant to the laws governing TRS, the TRS Board of Trustees (the “Board”) has determined that establishing and expending funds for this Performance Incentive Pay Plan (the “Plan”) is consistent with and in furtherance of the fiduciary duties of the Board in administering the retirement system.

2. PLAN OBJECTIVES AND STRATEGY

2.1 *Plan Objectives*

The Plan serves a number of objectives:

- To attract and retain IMD employees who have outstanding ability;
- To create incentives for IMD employees to develop a strong commitment to the long-term investment performance of the assets for which TRS has been delegated investment responsibility; and
- To motivate investment professionals to focus on maximizing real, long-term returns for all funds managed by TRS while assuming appropriate levels of risk.

2.2 *Plan Strategy*

The Plan strategy includes:

- Base salaries, targeted at competitive levels, as defined by the Executive Director and the Board with actual individual base salaries determined by an employee’s experience, education, knowledge, skills and overall job performance.
- Performance incentive pay award opportunities, calculated as a percentage of an employee’s base salary for performance above pre-determined standards, earned contingent upon continued employment in an Eligible Position at specified times and generally payable in two annual installments, subject to deferral as set forth in Section 4.8(b).

3. BASE SALARY ADMINISTRATION

3.1 *Salary Structure*

- (a) Notwithstanding any other law, the Board approves the rates of compensation of all IMD employees. Under state law, the Board’s Bylaws, and as part of the annual TRS budgeting process, the Board authorizes the Executive Director to determine and propose base salary rates of compensation generally based on the salary schedules, position classifications and salary administration practices of Article IX of the General Appropriations Act, Chapter 659 of the Texas Government Code and other relevant legislation to the extent the Executive Director determines a particular provision is in the best interest of the system and not in conflict with applicable law, fiduciary duty, or TRS policy.

- (b) Under the terminology of the state compensation program, “classified” employees are those employees whose position classification titles, pay groups and ranges, and pay administration practices are based on the State Position Classification Plan and related salary administration provisions.
- (c) Upon hiring or promotion, classified employees are assigned to a classification title that is consistent with assigned responsibilities. Initial base salaries for classified employees are set between the minimum and maximum of the assigned pay group, considering the employee’s experience, education, knowledge and skills, and issues of external competitiveness and internal equity.
- (d) “Exempt” employees’ job titles, pay groups and ranges, and pay administration practices are not based on the State Position Classification Plan and related salary administration system. For purposes of the Plan, the Chief Investment Officer and the Investment Fund Directors are considered exempt employees, while the remainder of IMD employees are considered classified for compensation and other purposes. Employees who are exempt from the salary classification schedules do not have base salary ranges. As part of the annual TRS budgeting process, the Board authorizes the Executive Director to determine base salaries for exempt positions up to a not-to-exceed rate specified in the General Provisions of the TRS Budget. Initial base salaries for exempt employees are set by the Executive Director at or below the applicable not-to-exceed rate, considering the employee’s experience, education, knowledge and skills, and issues of external competitiveness and internal equity.

3.2. *Salary Adjustments*

- (a) Classified employees may receive base salary increases for a number of reasons, including but not limited to career ladder promotions, and merit increases for individual performance. Exempt employees may receive base salary adjustments (increase within the not-to-exceed rate or decrease) at the discretion of the Executive Director.
- (b) Notwithstanding subsection 3.2(a), all base salary changes will be executed in accordance with TRS salary administration procedures.

4. INCENTIVE PAY PLAN

4.1. *Purpose of the Plan and Effective Date*

- (a) The purpose of the Plan is to provide the opportunity for IMD employees to receive performance incentive pay based on specific criteria relative to TRS’s investment performance and the employee’s job performance.
- (b) This version of the Plan is effective for Performance Periods beginning on or after the effective date shown on the cover page. A Potential Award for performance in prior Performance Periods can become earned and payable subject to the terms and conditions stated in the version of the Plan effective for those Performance Periods.

4.2. *Performance Period*

For purposes of the Plan, the “Performance Period” begins on October 1st of each year and ends the following September 30th.

4.3. *Participation in the Plan*

- (a) An IMD employee who is in an “Eligible Position” on October 1 of the Performance Period is eligible to participate in the Plan (a “Participant”) during that Performance Period.

- (b) Notwithstanding Section 4.3(a) above, an IMD employee who first begins employment in an Eligible Position (through new hire, promotion or reassignment) after the beginning of the Performance Period will become a Participant as follows:
 - (i) If an IMD employee begins employment in an Eligible Position with an official hire date or effective date after October 1 but no later than January 1 the employee will become a Participant on January 1 and the Participant's award opportunity will be prorated to 75% of the Potential Award for that Performance Period.
 - (ii) If an IMD employee begins employment in an Eligible Position with an official hire date or effective date after January 1 but no later than April 1 the employee will become a Participant on April 1 and the Participant's award opportunity will be prorated to 50% of the Potential Award for that Performance Period.
 - (iii) If an IMD employee begins employment in an Eligible Position with an official hire date or effective date after April 1 but no later than July 1 the employee will become a Participant on July 1 and the Participant's award opportunity will be prorated to 25% of the Potential Award for that Performance Period.
 - (iv) If an IMD employee begins employment in an Eligible Position with an official hire date or effective date after July 1 of a Performance Period the employee will not become a Participant until the beginning of the next Performance Period (assuming such employee is employed by TRS in an Eligible Position on October 1 of the Performance Period).
 - (v) If a Participant leaves an Eligible Position during a Performance Period and begins TRS employment in a non-Eligible Position, the Participant's Potential Award for the partial Performance Period will be prorated based on the number of completed calendar quarters worked in all Eligible Positions during that Performance Period.
- (c) Generally, all permanent, full time employee positions assigned to the IMD are Eligible Positions under the Plan. Each Eligible Position within the IMD is assigned to an investment area that determines the profit center allocations included in the Participant's Potential Award calculation under Addendums A and B.
- (d) Secondees, contract workers, and other temporary workers are not TRS employees and are not eligible to participate in the Plan.
- (e) An Eligible Position in one Performance Period is not automatically an Eligible Position in any subsequent Performance Period.
- (f) The Director of Human Resources will certify to the Executive Director in writing the name, base salary, hire date, effective date, Eligible Position title, and investment area assignment of each eligible Participant for the applicable Performance Period, including Participants employed in an Eligible Position for only a portion of the Performance Period.
- (g) After the beginning of a Performance Period, if a Participant moves from one Eligible Position to another Eligible Position with a different position title or area assignment, the Participant's Potential Award for that Performance Period and the measurement of the Participant's performance will be prorated between the award calculated for the former Eligible Position title or investment area assignment and the award calculated for the new Eligible Position or investment area assignment as follows:
 - (i) If a Participant moves to a new Eligible Position or investment area assignment after October 1 but no later than January 1 the Participant's Potential Award and the measurement of the Participant's performance will be based on the former Eligible Position or investment area assignment for the period October 1 through December 31,

and on the new Eligible Position or investment area assignment for the period January 1 through September 30.

- (ii) If a Participant moves to a new Eligible Position or investment area assignment after January 1 but on or before April 1 the Participant's Potential Award and the measurement of the Participant's performance will be based on the former Eligible Position or investment area assignment for the period October 1 through March 31, and on the new Eligible Position or investment area assignment for the period April 1 through September 30.
 - (iii) If a Participant moves to the new Eligible Position or investment area assignment after April 1 but no later than July 1 the Participant's Potential Award and the measurement of the Participant's performance will be based on the former Eligible Position or investment area assignment for the period October 1 through June 30, and on the new Eligible Position or investment area assignment for the period July 1st through September 30.
 - (iv) If a Participant moves to a new Eligible Position or investment area assignment after July 1 of a Performance Period the Participant's Potential Award will be based on the former Eligible Position or investment area assignment for the entire Performance Period.
- (h) An employee will cease to be a Participant in the Plan on the earliest to occur of:
- (i) Except as specifically provided in Section 4.3(b)(v) with respect to continued TRS employment, the date the employee is no longer employed in an Eligible Position;
 - (ii) The date of termination of the employee's employment with TRS for any reason. (For purposes of the Plan, the date of termination is the employee's last day worked and does not include any leave the employee was allowed to use to extend their employment for payroll purposes.); or
 - (iii) The date of termination of the Plan.

4.4. *Investment Performance Components, Qualitative Components, and Potential Award*

- (a) Participants' Potential Awards will be based on a combination of investment performance and qualitative performance components.
- (b) The investment performance components comprise two performance categories: 1) performance measured against pre-determined benchmarks and applicable excess return targets, and 2) performance measured against pre-determined peer groups.
 - (i) The benchmark index category of the investment performance component will determine 50% of the total Potential Award.
 - (ii) The peer group category of the investment performance component will determine 30% of the total Potential Award.
- (c) Notwithstanding that the Performance Period is October 1 through September 30, due to the delay in availability of final performance data for Private Equity and Real Assets, performance measurements for these two investment areas will experience a one quarter time lag, such that all incentive calculations involving Private Equity and Real Assets performance will use data for the one and three year periods ending each June 30.
- (d) Each Eligible Position will be assigned specific weightings for Total Fund and investment area performance as shown in Addendums A and B.
 - (i) To encourage a focus on the "big picture" and a sense of shared mission, the investment performance component (both benchmark and peer group categories) for all Eligible Positions

will have a Total Fund weighting of at least 20%. Weightings for investment area performance categories will be divided among the Eligible Position’s primary investment area and other investment areas with which the Eligible Position has regular interaction.

- (ii) Where no investment area peer group performance measures are available, that investment area peer group performance weighting allocation is added to the Total Fund peer group performance weighting allocation.
- (e) The qualitative performance component will be measured as part of each Participant’s annual performance appraisal process and may include multi-rater feedback regarding a variety of contributions and behaviors needed for organizational success that are not directly measured in the investment performance component, such as interpersonal relationship skills, accountability, effective teamwork, etc.
 - (i) Regardless of a Participant’s performance towards the qualitative performance component, a Potential Award will only include the portion attributed to qualitative performance if the Participant has attained at least the threshold level of performance in the investment performance component.
 - (ii) To encourage appropriate organizational behaviors, the qualitative performance component for all Eligible Positions will be weighted at 20% of the Potential Award.
- (f) A Potential Award is the gross award amount calculated based on the actual performance achieved in the Performance Period. Depending on performance, the Potential Award in a Performance Period varies from zero to 100% of the Maximum Potential Award. The Maximum Potential Award that can become earned and payable under the Plan is limited to the percentage of a Participant’s Base Salary in an Eligible Position that is listed opposite each Eligible Position in the table below. The Maximum Potential Award applies regardless of whether a Participant has exceeded the stated maximum performance targets or the gross amount of the Potential Award calculated under the Plan.

ELIGIBLE POSITION	MAXIMUM POTENTIAL AWARD
Chief Investment Officer	125%
Deputy CIO	125%
Senior Managing Director	125%
Managing Director	125%
Senior Director	110%
Director	110%
Senior Investment Manager	90%
Investment Manager	85%
Senior Associate	65%
Associate	50%
Senior Analyst	35%
Analyst	25%
Administrative Assistants	5%

- (g) Notwithstanding the Maximum Potential Award listed in Section 4.4(f) above, those Participants titled “Senior Investment Manager” who remain in the Eligible Position that was titled “Lead

Investment Manager” or “Lead Trader” in the Plan effective October 1, 2007, will continue to have a Maximum Potential Award of 100% of Base Salary. If the Participant transfers to a different Eligible Position with a title other than Senior Investment Manager, the Maximum Potential Award will change to that appropriate for the new Eligible Position and be prorated as set forth in Section 4.3(g).

- (h) For each investment area, the profit center weighting and excess return relative to each assigned excess return target will combine to determine the Potential Award for each Eligible Position.
 - (i) The Potential Award includes a threshold, a maximum, and intermediate levels of Potential Award that correspond to specific levels of investment performance.
 - (ii) Intermediate levels of the Potential Award for investment performance are determined by linearly interpolating between the threshold and maximum.
 - (iii) For the qualitative component, intermediate levels of the Potential Award will be based on a system of annual performance evaluation approved by the Executive Director.

4.5. *Compliance with TRS Policies*

- (a) IMD employees exercise fiduciary responsibilities delegated by the Board under applicable law. Investment professionals manage the portfolio according to the Board’s policies, advise and inform the Executive Director and the Board about investments, and recommend modifications to the Investment Policy Statement. In addition, all IMD employees are responsible for complying with TRS policies, including without limitation the Investment Policy Statement, Ethics Policy, and the Fraud, Waste and Abuse Policy.
- (b) Excess performance by a Participant or Participants resulting from a failure to manage the assets of TRS in accordance with applicable law, the Investment Policy Statement, or TRS Ethics Policy will result in the forfeiture for that portion of the Potential Award for those Participants resulting from that excess performance for the Performance Period in which the noncompliance occurred. The Executive Director will make this determination on a case-by-case basis.
- (c) Serious violations of the TRS Investment Policy Statement, Ethics Policy, Fraud, Waste and Abuse Policy, or other TRS policy by a Participant, as determined by the Executive Director, will result in forfeiture of all Potential Awards for the Performance Period in which the violation(s) occurred, as well as for earlier Performance Periods that have not yet become earned (including without limitation any Potential Awards that are unearned and deferred as set forth in Section 4.8(b) below). Additionally, during the investigation of possible serious violations of law or policy, the Executive Director or the Board may suspend earning and payment of Potential Awards until the conclusion of the investigation.

4.6. *Performance Standards and Measurements*

- (a) Investment Performance (for both benchmark and peer group categories) is measured on one year and three year historical performance data, weighted at 33% for one year performance (i.e., performance during the Performance Period) and 67% for the historical three year performance that includes the Performance Period. Investment Performance is measured relative to appropriate pre-defined benchmarks as detailed in the asset allocation and benchmarks table, including applicable footnotes, in the Board’s Investment Policy Statement (“IPS”), as amended from time to time. For the purposes of this Plan, changes to the IPS benchmarks during a Performance Period will be effective from and after the effective date of such changes in the IPS, subject to revisions to the Plan adopted by the Board of Trustees. In no event may benchmark changes be applied retroactively except as required to comply with applicable law, including federal tax laws and regulations.

- (b) Notwithstanding Section 4.6(a), the performance of any new profit center will be calculated for purposes of the Plan as follows:
 - (i) The investment performance of any new profit center (for both benchmark and peer group categories) will commence with the first full Performance Period commencing on or after the date the profit center is created;
 - (ii) For a new profit center's first full Performance Period, the profit center's investment performance will be based 100% on the profit center's performance data for the first full Performance Period;
 - (iii) For a new profit center's second full Performance Period, the profit center's investment performance will be weighted (x) 50% on the profit center's performance during the second full Performance Period, and (y) 50% on the profit center's two-year performance during the first and second full Performance Periods.
 - (iv) For all Performance Periods commencing after the second full Performance Period, the investment performance of a new profit center will be weighted (x) 33% on the profit center's performance during the one-year Performance Period just ended, and (y) 67% on the profit center's three-year performance during the three full Performance Periods just ended.
 - (v) For the purposes of this Plan, no investment performance will be calculated for a Performance Period for a new profit center created during that Performance Period, unless it existed on October 1 of that Performance Period.
- (c) The qualitative performance component is measured annually as part of the Participant's current annual performance appraisal process.

4.7. *Potential Award Calculations*

- (a) Following the end of each Performance Period, the Executive Director will review the actual performance of each Participant relative to the applicable performance components.
- (b) Potential Awards are calculated based on the Participant's level of performance achieved in the applicable investment performance and qualitative performance components in each Performance Period.
- (c) Relative performance data and calculations may be reviewed by an external independent source selected by the Executive Director, but final calculations are approved by the Executive Director.

4.8. *Earning Potential Awards and Payouts*

- (a) Notwithstanding the Executive Director's approval of Potential Award calculations, Potential Awards will only become earned and payable as stated below:
 - (i) Subject to Section 4.8(b), if a Participant is employed by TRS on January 1 following the end of the Performance Period for which that employee was a Participant, 50% of the Potential Performance Incentive Award will become earned and payable. Payment of this award will generally be processed with that January payroll for delivery on or about February 1 of that calendar year; provided however that in no event will payment be made later than February 15 of that calendar year.
 - (ii) Subject to Section 4.8(b), if a Participant is employed by TRS on January 1 following the first anniversary of the end of the Performance Period for which that employee was a Participant, the remaining 50% of the Potential Performance Incentive Award will become earned and payable. Payment of this award will generally be processed with that

January payroll, for delivery on or about February 1 of that calendar year; provided however that in no event will payment be made later than February 15 of that calendar year.

The payment dates in respect of a Performance Period shall be the same for all Participants.

- (b) Notwithstanding subsection 4.8(a), no Potential Awards will become earned or payable following a Performance Period in which the Fund experiences a total return of zero or less. If this occurs, Potential Awards for that Performance Period that otherwise would have become earned on the January 1 next following the end of that Performance Period will not become earned until January 1 following the next Performance Period in which the Total Fund has a return greater than zero during a Performance Period, subject to the requirement that the employee be employed by TRS on that January 1. Payment of this award will be processed with the January payroll, typically issued on or about February 1 of that calendar year; provided however that in no event will payment be made later than February 15 of that calendar year.
- (c) If an employee ceases to be a Participant before the end of a Performance Period due to termination of employment with TRS for any reason other than involuntary termination of employment due to a Reduction in Force, death, or disability within the meaning of Section 409A of the Internal Revenue Code, a Potential Award for that Performance Period will not become earned and will not be paid. Potential Awards from earlier Performance Periods that have not yet become earned (as set forth in Section 4.8(b) above) will not become earned and will not be paid.
- (d) If an employee ceases to be a Participant before the end of a Performance Period due to involuntary termination of employment with TRS because of a Reduction in Force, death, or disability within the meaning of Section 409A of the Internal Revenue Code, a Potential Award for that Performance Period will not become earned and will not be paid. Notwithstanding Sections 4.8(a) – (b), Potential Awards from earlier Performance Periods will immediately become earned and payable. Payments under this subsection will be made to the terminated employee, or to the estate of the deceased employee, or to the disabled employee, or as otherwise provided by law. These payments will be made as soon as administratively practicable, but no later than 2½ months after the end of the calendar year in which the Reduction in Force, death or disability occurred.
- (e) If an employee ceases to be a Participant before the end of a Performance Period due to termination of the Plan (as provided for in Section 5.1), a Potential Award for that Performance Period will not become earned and will not be paid. Potential Awards from earlier Performance Periods that have not yet become earned (as set forth in this Section 4.8), can become earned and be paid according to the terms in this Section 4.8, if the Board determines that such payments continue to be consistent with and in furtherance of the fiduciary duties of the Board in administering the retirement system, and if such payments are not prohibited by applicable law.

5. PLAN AUTHORITY AND RESPONSIBILITY

5.1 *Plan Modification, Suspension and Termination*

The Board shall have the right in its sole discretion to modify the Plan or any portion thereof at any time. The Board shall have the right in its sole discretion to suspend or terminate the Plan entirely or any portion thereof at any time. For avoidance of doubt, no modification, amendment, suspension, or reinstatement of this Plan may be given retroactive effect in the administration of this Plan except as required to comply with applicable law, including federal tax laws and regulations.

5.2 Plan Administration

Consistent with the provisions of the Plan, the Executive Director has the sole discretion to administer and interpret the Plan. The Executive Director may adopt such procedures and practices as deemed advisable to carry out the Plan.

5.3 Record Keeping and Reporting

All employee performance, salary and incentive pay records for the Plan shall be maintained by the Director of Human Resources.

5.4 Compliance with State and Federal Law

If the Executive Director or a court with appropriate jurisdiction determines that any provision of the Plan violates applicable state or federal law, that provision shall not be given effect. The remaining provisions of the Plan shall remain in full force and effect to the maximum extent possible, and any amendments or modifications that are necessary to give effect to the remaining provisions will be deemed to have been made to allow proper administration of the Plan.

6. AT-WILL EMPLOYMENT

Nothing in the adoption of this Plan or the awarding of performance incentive pay alters the at-will nature of TRS employment, creates a contract between TRS and any TRS employee, confers on any TRS employee the right to continued employment with TRS, or affects in any way the right of TRS to terminate the employment of employees at any time.

7. OTHER PLAN PROVISIONS

7.1 Non-assignment and Non-transferability of Awards

Potential Awards or the actual awards under the Plan are non-assignable and non-transferable and are not subject to anticipation, adjustment, alienation, encumbrance, garnishment, attachment or levy of any kind.

7.2 Plan Does Not Create a Property Interest, Trust, or Entitlement

- (a) Neither the establishment of the Plan, the calculation of Potential Awards or the actual awards shall be deemed to create a property interest, trust or entitlement. The Plan is an unfunded, unsecured liability of TRS to make payments in accordance with the provisions of the Plan. Any amounts budgeted by TRS for awards earned under the Plan are TRS assets, and no employee or third party shall have any property, security, or other interest in any assets of TRS by reason of the Plan.
- (b) Nothing in the Plan shall be deemed to create or confer any right, interest, or title to any specific property of TRS to any Participant, or to any personal representative or beneficiary of a Participant.

7.3 Tax and Other Deductions

All payments under the Plan shall be subject to any deductions (1) for tax and withholding required by federal, state, or local law at the time of payment and (2) for any and all amounts owed by the employee to TRS at the time of payment. TRS is not obligated to advise an employee of the existence of any tax or the amounts that TRS will be required to withhold.

7.4 Payments Not Eligible for Retirement Purposes

Any payments made pursuant to the Plan are fringe benefits and are not eligible compensation for TRS pension plan purposes.

7.5 *Grievances*

All grievances related to the Plan will be addressed according to the TRS Grievance and Appeals Policy or any successor policy, as amended from time to time.

8. DEFINITIONS

Base Salary for use in the Plan is the Participant's annualized monthly salary as of October 1 of the applicable Performance Period (not including longevity or benefit replacement pay), or the annualized monthly salary of new Participants as of the date they first become a Participant, as certified by the Director of Human Resources.

Eligible Position is defined in Section 4.4(f). Eligible Position refers to the position, not the actual Participant in the position, and includes all positions assigned to the Investment Division and listed in Section 4.4(f).

Investment areas are listed in the first column of Addendums A and B.

Maximum Potential Award is defined in Section 4.4(f) and is the maximum Potential Award that can become earned and payable with respect to an Eligible Position during a Performance Period.

Participant is an employee in an Eligible Position on October 1 of the Performance Period, or who first is employed in an Eligible Position after the beginning of the Performance Period based on the schedule detailed in the Plan, as certified by the Director of Human Resources.

Performance Period is the period beginning on October 1 of each year and ending on September 30 of the following year.

Potential Award is defined in Section 4.4(f) and is the amount calculated based on the Participant's performance achieved in the applicable investment performance and qualitative performance components. A Potential Award is capped at the Maximum Potential Award, regardless of whether the Participant exceeds the stated maximum performance. The phrase "award opportunity" is synonymous with Potential Award.

Profit centers are listed in the first row of Addendum A, except that Trade Management is also listed as a profit center in the first row of Addendum B only for peer allocation purposes.

Reduction in Force for use in the Plan refers to termination of an employee due to elimination of the employee's position caused by a required reduction in the number of TRS Full-Time Equivalents (FTEs) or by a required reduction in expenses within the TRS operating budget. The Executive Director has sole discretion in determining whether an employee's termination is due to a Reduction in Force.

SAA means the Strategic Asset Allocation investment area.

SPN means a Strategic Partner Network investment area. TRS has both private markets and public markets SPNs.

TAA means the Tactical Asset Allocation investment area.

Total Fund means the TRS total or overall investment portfolio and includes all pension assets held in trust by TRS and invested by the IMD to provide retirement, death, and disability benefits administered by the system, including cash and cash equivalents. For avoidance of doubt, for the purposes of the Plan the Total Fund does not include the assets of health plans administered by TRS and held in trust by the Board of Trustees.

Administrative Policy

Reviewer: Executive Director, Chief Investment Officer, Human Resources & Legal Services

Review Cycle: Annually

Authorized by: TRS Board of Trustees

Approved: Brian Guthrie

Executive Director

*This version of the Plan is effective for performance periods beginning on or after October 1, 2012. Any awards for performance in prior Performance Periods can become earned and payable subject to the terms and conditions stated in the versions of the Plan effective for those Performance Periods.

Current Effective Date:
October 1, 2012*

First Issued: October 1,
2007

Last Reviewed/Revised:
September __, 2012

Next Review Due:
August, 2013

Date: September ____,
2012

Date: October ____, 2012

Addendum A

Performance Payout Allocation and Maximum Payout Targets vs. Passive Benchmark (50% of Potential Award)

Fund Level	Total Fund	Internal Public	External Public	Private Equity	Risk ¹	Stable Value / SAA	Real Assets	TAA	Public and Private SPN and Opportunistic ²	Natural Resources	Emerging Managers	Total
Index	Total Fund Policy Composite Index	Global Equity Portfolio vs. MSCI ACWI Free (net)	Daily Weighted Excess Return Based on Actual Portfolio Weights	State Street Private Equity Index	Daily Weighted Excess Return Based on Actual Portfolio Weights	Daily Weighted Excess Return Based on Actual Portfolio Weights	NCREIF	Total Profit & Loss for Incentive Period/Total Trust Average Daily Balance	Daily Weighted Excess Return Based on Actual Portfolio Weights	Daily Weighted Excess Return Based on Actual Portfolio Weights	Daily Weighted Excess Return Based on Actual Portfolio Weights	
Excess Return Target	100 bps	50 bps	100 bps	300 bps	75 bps	35 bps	250 bps	25 bps	175 bps	175 bps	100 bps	
CIO/Deputy CIO	75.00%					5.00%	5.00%		5.00%	5.00%	5.00%	100.00%
Risk	50.00%	5.00%	5.00%	5.00%	20.00%	5.00%	5.00%	5.00%				100.00%
Internal Public Markets	30.00%	60.00%	5.00%	5.00%								100.00%
External Public Markets	30.00%	5.00%	60.00%	5.00%								100.00%
Private Equity	30.00%	5.00%	5.00%	60.00%								100.00%
Stable Value / SAA	50.00%					50.00%						100.00%
Real Assets	30.00%						60.00%			10.00%		100.00%
Tactical Asset Allocation (TAA)	30.00%							60.00%	10.00%			100.00%
Public and Private SPN / Opportunistic	30.00%							10.00%	60.00%			100.00%
Natural Resources	30.00%	10.00%								60.00%		100.00%
Emerging Managers	30.00%		10.00%	10.00%			10.00%				40.00%	100.00%
Trade Management Group	30.00%	20.00%	10.00%			20.00%		20.00%				100.00%
Investment Operations	50.00%	10.00%	10.00%	5.00%		10.00%	5.00%	10.00%				100.00%

Notes: ¹ Risk group allocation excludes Trust hedging activities. ² Benchmark for Public SPN is the SPN Composite Index.

Addendum B
Performance Payout Allocation and Maximum Payout Targets vs. Peer Group Comparison
(30% of Potential Award)

Fund Level	Total Fund	Trade Management Group	Private Equity	Real Assets	Total
Index	TUCS Public Funds > \$10 Billion Universe	ITG / Plexus	TUCS Private Equity > \$1 billion Universe	Real Estate vs. TUCS Real Estate > \$1 billion Universe	
Excess Return Target	100 bps	8 bps	300 bps	250 bps	
CIO/Deputy CIO	90.00%	0.00%	5.00%	5.00%	100.00%
Risk	90.00%	0.00%	5.00%	5.00%	100.00%
Internal Public Markets	95.00%	0.00%	5.00%	0.00%	100.00%
External Public Markets	95.00%	0.00%	5.00%	0.00%	100.00%
Private Equity	40.00%	0.00%	60.00%	0.00%	100.00%
Stable Value / SAA	70.00%	30.00%	0.00%	0.00%	100.00%
Real Assets	40.00%	0.00%	0.00%	60.00%	100.00%
Tactical Asset Allocation (TAA)	100.00%	0.00%	0.00%	0.00%	100.00%
Public and Private SPN / Opportunistic	90.00%	10.00%	0.00%	0.00%	100.00%
Natural Resources	90.00%	0.00%	0.00%	10.00%	100.00%
Emerging Managers	80.00%	0.00%	10.00%	10.00%	100.00%
Trade Management Group	50.00%	50.00%	0.00%	0.00%	100.00%
Investment Operations	50.00%	40.00%	5.00%	5.00%	100.00%

Teacher Retirement System of Texas
PERFORMANCE INCENTIVE PAY PLAN

Effective October 1, ~~2011~~2012

This version of the Plan is effective for Performance Periods beginning on or after October 1, ~~2011~~2012. Any awards for performance in prior Performance Periods; can become earned and payable subject to the terms and conditions stated in the versions of the Plan effective for those ~~P~~performance ~~P~~periods. No modification of the Plan may be given retroactive effect except as required to comply with applicable law, including federal tax laws and regulations.

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1. [PERFORMANCE INCENTIVE](#) PLAN PURPOSE AND AUTHORIZATION

To remain competitive in its efforts to attract and retain high caliber Investment [Management](#) Division (IMD) [staffemployees](#), the Teacher Retirement System of Texas (TRS) strives to offer a competitive compensation package. [Awards of p](#)Performance incentive pay [based on specified performance criteria](#) ~~are is~~ an industry standard practice in the private ~~sector~~ investment ~~sector arena~~ and ~~are is~~ rapidly becoming a standard practice in the public sector. By offering both a competitive base salary and performance incentive [award opportunity](#) pay, TRS enhances its ability to fulfill ~~the its~~ mission to “prudently invest and manage the assets held in trust for members and beneficiaries in an actuarially sound system administered in accordance with applicable fiduciary principals.” Therefore, pursuant to the laws governing TRS, the TRS Board of Trustees (the “Board”) has determined that establishing and expending funds for this Performance Incentive Pay Plan (the “Plan”) is [consistent with and in furtherance of the](#) ~~required to perform the~~ fiduciary duties of the Board in administering the retirement system.

2. PLAN OBJECTIVES AND STRATEGY

2.1 *Plan Objectives*

The Plan serves a number of objectives:

- To attract and retain ~~Investment Division~~ [IMD staffemployees](#) who have outstanding ability;
- To [create incentives for](#) ~~encourage Investment Division~~ [IMD staffemployees](#) to develop a strong commitment to the [long-term investment](#) performance of the assets for which TRS has been delegated investment responsibility; and
- To motivate investment professionals to focus on maximizing real, long-term returns for all funds managed by TRS while assuming appropriate levels of risk.

2.2 *Plan Strategy*

The Plan strategy includes:

- Base salaries, targeted at competitive levels, as defined by the Executive Director and the Board with actual individual base salaries determined by an employee's experience, education, knowledge, skills and overall job performance.
- Performance incentive pay award opportunities, calculated as a percentage of an employee's base salary for performance above pre-determined standards, earned contingent upon continued employment in an Eligible Position at specified times and generally payable in two annual installments, subject to deferral as set forth in Section 4.8(b)-over a two-year period.

3. BASE SALARY ADMINISTRATION

3.1. *Salary Structure*

- (a) Notwithstanding any other law, the Board approves the rates of compensation of all ~~investment division~~ IMD employees. Under state law, the Board's Bylaws, and as part of the annual TRS budgeting process, tThe Board authorizes the Executive Director to determine and propose base salary adopt rates of compensation generally based on the salary schedules, position classifications and salary administration practices of Article IX of the General Appropriations Act, Chapter 659 of the Texas Government Code and other relevant legislation to the extent the Executive Director determines a particular provision is in the best interest of the system and not in conflict with applicable law, fiduciary duty, or TRS policy.
- (b) Under the terminology of the state compensation program, "classified" employees are those employees whose position classification titles, pay groups and ranges, and pay administration practices are based on the State Position Classification Plan and related salary administration provisions. ~~"Exempt" employees' job titles, pay groups and ranges, and pay administration practices are not based on the State Position Classification Plan and related salary administration system. For purposes of the Plan, the Chief Investment Officer and the Investment Fund Directors are considered exempt employees, while the remainder of TRS investment division employees are considered classified.~~
- (c) Upon hiring or promotion, classified employees are assigned to a classification title that is consistent with assigned responsibilities. Initial base salaries for classified employees are set between the minimum and maximum of the assigned pay group, considering the employee's experience, education, knowledge and skills, and issues of external competitiveness and internal equity.
- (d) ~~"Exempt" employees' job titles, pay groups and ranges, and pay administration practices are not based on the State Position Classification Plan and related salary administration system. For purposes of the Plan, the Chief Investment Officer and the Investment Fund Directors are considered exempt employees, while the remainder of IMD TRS investment division employees are considered classified for compensation and other purposes.~~ Exempt Employees who are exempt from the salary classification schedules do not have base salary ranges. As part of the annual TRS budgeting process, tThe Board authorizes the Executive Director to determine set base salaries for exempt positions up to a not-to-exceed rate specified in the General Provisions of the TRS Budget. Initial base salaries for exempt employees are set by the Executive Director at or below the applicable not-to-exceed rate, considering the employee's experience, education, knowledge and skills, and issues of external competitiveness and internal equity.

3.2. Salary Adjustments

- (a) Classified employees may receive base salary increases for a number of reasons, including but not limited to career ladder promotions, and merit increases for ~~demonstrated~~ individual performance. Exempt employees may receive base salary adjustments (increase within the not-to-exceed rate or decrease) at the discretion of the Executive Director.
- (b) Notwithstanding subsection 3.2-(a), all base salary changes will be executed in accordance with TRS salary administration procedures.

4. INCENTIVE PAY PLAN

4.1. Purpose of the Plan and Effective Date

- (a) The purpose of the Plan is to provide the opportunity for ~~Investment Division~~ IMD employees to receive performance incentive pay based on specific criteria relative to TRS's investment performance and the employee's job performance.
- (b) This version of the Plan is effective for Performance Periods ~~performance periods~~ beginning on or after the effective date shown on the cover page ~~October 1, 2010~~. A Potential Award ~~Any awards~~ for performance in prior Performance Periods can become earned and payable subject to the terms and conditions stated in the version of the Plan effective for those Performance Periods.

4.2. Performance Period

For purposes of the Plan, the "Performance Period" begins on October 1st of each year and ends the following September 30th.

4.3. Participation in the Plan

- (a) An IMD employee who is in an "Eligible Position" on October 1st of the Performance Period, is eligible to participate in the Plan (a "Participant") during that Performance Period.
- (b) Notwithstanding ~~section~~ Section 4.3-(a) above, an IMD employee who first begins employment in an Eligible Position (through new hire, promotion or reassignment) after the beginning of the Performance Period will become a Participant as follows:
 - (i) If ~~an the~~ IMD employee begins employment in an Eligible Position with an official hire date or effective date after October 1st but no later than January 1st the employee will become a Participant on January 1st and the Participant's award opportunity ~~Potential Performance Incentive Awards~~ will be prorated to 75% of the Incentive Potential Award for that Performance Period ~~Opportunity as defined in subsection 4.4 (f)~~.
 - (ii) If ~~an the~~ IMD employee begins employment in an Eligible Position with an official hire date or effective date after January 1st but no later than April 1st the employee will become a Participant on April 1st and the Participant's award opportunity ~~Potential Performance Incentive Awards~~ will be prorated to 50% of the Potential Award for that Performance Period ~~Incentive Award Opportunity as defined in subsection 4.4 (f)~~.
 - (iii) If ~~an the~~ IMD employee begins employment in an Eligible Position with an official hire date or effective date after April 1st but no later than July 1st the employee will become a Participant on July 1st and the Participant's award opportunity ~~Potential Performance Incentive Awards~~ will be prorated to 25% of the Potential Award for that Performance Period ~~Incentive Award Opportunity as defined in subsection 4.4 (f)~~.

- (iv) If an IMD ~~the~~-employee begins employment in an Eligible Position with an official hire date or effective date after July 1st of a Performance Period the employee will not become a Participant until the beginning of the next Performance Period (assuming such employee is employed by TRS in an Eligible Position on October 1st of the Performance Period).
- (v) If a Participant leaves an Eligible Position during a Performance Period and begins TRS employment in a non-Eligible Position, the Participant's Potential Award for the partial Performance Period will be prorated based on the number of completed calendar quarters worked in all Eligible Positions during that Performance Period.
- (c) Generally, all permanent, full time employee positions assigned to the ~~Investment Division~~IMD are Eligible Positions under the Plan. ~~However, contract workers are not TRS employees and thus not eligible to participate in the Plan~~Each Eligible Position within the IMD is assigned to an investment area that determines the profit center allocations included in the Participant's Potential Award calculation under Addendums A and B. Section 4.4 (f) contains a list of Eligible Position titles.
- (d) Secondees, contract workers, and other temporary workers are not TRS employees and are not eligible to participate in the Plan.
- (de) An Eligible Position in one Performance Period is not automatically an Eligible Position in any subsequent Performance Period.
- (ef) The Director of Human Resources will certify to the Executive Director in writing the name, base salary, hire date, effective date, Eligible Position title, and investment area assignment of each eligible Participant for the applicable Performance Period, including Participants employed in an Eligible Position for only a portion of the Performance Period. ~~The Director of Human Resources will also certify the base salary, position title and Area assignment for each participant~~
- (fg) After the beginning of a Performance Period, if a Participant moves from one Eligible Position to another Eligible Position with a different position title or area assignment, the Participant's Potential ~~Performance Incentive~~ Awards for that Performance Period and the measurement of the Participant's performance will be prorated between ~~that the award calculated appropriate~~ for the former Eligible Position ~~old position~~-title or investment area assignment and the award calculated ~~that appropriate~~ for the new Eligible Position ~~position title~~-or investment area assignment as follows:
 - (i) If a Participant ~~the employee~~ moves to a ~~the~~-new Eligible Position ~~position title~~-or investment area assignment after October 1st but no later than January 1st the Participant's ~~employee's~~-Potential ~~Performance Incentive~~ Awards and the measurement of the Participant's performance will be based on the former Eligible Position ~~old position title~~ or investment area assignment for the period October 1st through December 31st, and on the new Eligible Position ~~position title~~-or investment area assignment for the period January 1st through September 30th.
 - (ii) If a Participant ~~the employee~~ moves to a~~the~~-new Eligible Position ~~position title~~-or investment area assignment after January 1st but on or before ~~no later than~~ April 1st the Participant's ~~employee's~~-Potential ~~Performance Incentive~~ Awards and the measurement of the Participant's performance will be based on the former Eligible Position ~~old position title~~-or investment area assignment for the period October 1st through March 31st, and on the new Eligible Position ~~position title~~-or investment area assignment for the period April 1st through September 30th.

- (iii) If a Participant ~~the employee~~ moves to the new Eligible Position title or investment area assignment after April 1st but no later than July 1st the Participant's employee's Potential Performance Incentive Awards and the measurement of the Participant's performance will be based on the former Eligible Position old position title or investment area assignment for the period October 1st through June 30th, and on the new Eligible Position position title or investment area assignment for the period July 1st through September 30th.
 - (iv) If a Participant ~~the employee~~ moves to a new Eligible Position position title or investment area assignment after July 1st of a Performance Period the Participant's employee's Potential Performance Incentive Awards will be based on the former Eligible Position old position title or investment area assignment for the entire Performance Period.
- (gh) An employee will cease to be a Participant in the Plan on the earliest to occur of:
- (i) Except as specifically provided in Section 4.3(b)(v) with respect to continued TRS employment, ~~The~~ the date the employee is no longer employed in an Eligible Position;
 - (ii) The date of termination of the employee's employment with TRS for any reason. (For purposes of the Plan, the date of termination is the employee's last ~~physical~~ day worked and does not include any leave the employee was allowed to use to extend their employment for payroll purposes.); or
 - (iii) The date of termination of the Plan.

4.4. Investment Performance Components, Qualitative Components, and ~~Incentive~~ Potential Award Opportunity

- (a) ~~Generally,~~ Participants' ~~Potential Potential Performance Incentive AA~~ awards will be based on a combination of investment performance and qualitative performance components. ~~The Investment Performance Component includes a pre-defined combination of Fund and Area performance versus benchmarks and versus peer groups of other large public funds. The Qualitative Performance Component includes performance in a variety of contributions and behaviors needed for organizational success.~~
 - (b) The investment performance components ~~Investment Performance Component~~ comprise ~~includes~~ two Performance Categories: – 1) Benchmark Performance measured against pre-determined benchmarks and applicable excess return targets, and 2) performance measured against pre-determined Peer-peer Group groups. ~~Where applicable, each Performance Category contains two Performance Sub-Categories—Fund Performance and Area Performance.~~
 - (i) The benchmark index category of the investment performance component will determine 50% of the total Potential Award.
 - (ii) The peer group category of the investment performance component will determine 30% of the total Potential Award.
- ~~(i) The Fund Benchmark Performance sub-category measures the performance of the total fund relative to a predetermined benchmark.~~
 - ~~(ii) The Fund Peer Group Performance sub-category measures the performance of the total fund relative to the performance of a predefined universe of large public funds. The Area Benchmark Performance sub-category measures the performance of specific sub-groups (“Areas”) of the total fund relative to predetermined benchmarks.~~

- ~~(iii) The Area Benchmark Performance sub-category measures the performance of sub-groups (“Areas”) of the total fund relative to predetermined benchmarks.~~
- ~~(iv) Where available, the Area Peer Group Performance sub-category measures the performance of investment Areas relative to the performance of similar investment Areas of a predefined universe of large public funds.~~

~~Investment Areas include:~~

- ~~• Strategic Partner Management~~
- ~~• Internal Public Markets~~
- ~~• External Public Markets~~
- ~~• Real Asset~~
- ~~• Private Equity~~
- ~~• Trade Management Group~~

- (c) ~~Notwithstanding that the Performance Period is October 1st through September 30th, due to the delay in availability of final performance data for Private Equity and Real Assets~~Private Equity and Real Assets~~, performance measurements for these two Investment Areas will experience a one quarter time lag, such that all incentive calculations involving Private Equity and Real Assets performance will use data for the one and three year ~~twelve month~~ periods ending each June 30th.~~

~~For the first year of this change in measurement period for Private Equity and Real Assets, incentive calculations will use data for the nine-month period beginning October 1, 2009 and ending June 30, 2010 for one-year performance. Measurement of three-year performance for these Investment Areas during the first year of this change will use data from October 1, 2007 through June 30, 2010. Benchmark targets and participant performance during the first year of this change will be prorated proportionately to the change in the measurement period.~~ (d) Each Eligible Position will be assigned specific weightings for Total Fund and investment area performance ~~Area Performance~~ as shown in Addendums A and B.

- (i) To encourage a focus on the “big picture” and a sense of shared mission, the investment performance component ~~Investment Performance Component~~ (both benchmark and peer group categories ~~Benchmark and Peer Group Categories~~) for all Eligible Positions will have a Total Fund weighting of at least 20%. Weightings for investment area performance ~~Area Performance~~ Sub-categories will be divided among the Eligible Position’s primary investment area ~~Area~~ and other investment areas ~~Areas~~ with which the Eligible Position has regular interaction.
- (ii) Where no investment area peer group ~~Area Peer Group P~~ performance measures are available, that investment area peer group performance ~~Area Peer Group Performance~~ weighting allocation is added to the Total Fund peer group performance ~~Peer Group Performance~~ weighting allocation.
- (e) The qualitative performance component ~~Qualitative Performance Component~~ will be measured as part of the each Participant’s annual performance appraisal process and may include multi-rater feedback regarding a variety of contributions and behaviors needed for organizational success that are not directly measured in the investment performance component ~~Investment Performance Component~~, such as interpersonal relationship~~al~~ skills, accountability, effective teamwork, etc.
 - (i) (e) Regardless of a Participant’s performance towards the qualitative performance component ~~Qualitative Performance Component~~, a Potential Performance Incentive Awards will

only include the portion attributed to qualitative performance Qualitative Performance if the Participant has attained at least the threshold level of performance in the investment performance component Investment Performance Component.

(ii) To encourage appropriate organizational behaviors, the qualitative performance component Qualitative Performance Component for all Eligible Positions will be weighted at 20% of the Potential Award.

~~Where no Area Peer Group Performance measures are available, that Area Peer Group Performance weighting allocation is added to the Fund Peer Group Performance weighting allocation.~~

~~To encourage appropriate organizational behaviors, the Qualitative Performance Component for all Eligible Positions will be weighted at 20~~

~~(e) Regardless of a Participant's performance towards the Qualitative Performance Component, Potential Performance Incentive Awards will only include the portion attributed to Qualitative Performance if the Participant has attained at least the threshold level of performance in the Investment Performance Component.~~

(f) A Potential Award is the gross award amount calculated based on the actual performance achieved in the Performance Period. Depending on performance, the Potential Award in a Performance Period varies from zero to 100% of the Maximum Potential Award. The "Incentive Award Opportunity" for a Performance Period is expressed as a percentage of the "Maximum Potential Award that can become earned and payable under the Plan is limited to Opportunity," which the percentage ranges from 5% to 125% of a Participant's Base Salary the employee's base salary, depending on in an the Eligible Position that is listed opposite each Eligible Position detailed in the table below. The Maximum Potential Award applies regardless of whether a Participant has exceeded the stated maximum performance targets or the gross amount of the Potential Award calculated under the Plan.

<u>ELIGIBLE POSITION</u>	<u>MAXIMUM POTENTIAL AWARD OPPORTUNITY</u>
Chief Investment Officer	125%
Deputy CIO	125%
Senior Managing Director	125%
Managing Director	125%
Senior Director	110%
Director	110%
Senior Investment Manager	90%
Investment Manager	85%
Senior Associate	65%
Associate	50%
Senior Analyst	35%
Analyst	25%
Administrative Assistants	5%

(g) Notwithstanding the Maximum Potential Award listed Opportunities detailed in Section 4.4(f) above, those Participants titled "Senior Investment Manager" who remain in the Eligible Position

that was titled “Lead Investment Manager” or “Lead Trader” in the Plan effective October 1, 2007, will continue to have a Maximum Potential Award Opportunity of 100% of Base Salary. If the Participant transfers to a different Eligible Position with a title other than Senior Investment Manager, the Maximum Potential Award Opportunity will change to that appropriate for the new Eligible Position and be prorated as set forth detailed in Section 4.3(g) ~~(f)~~.

- (h) For each investment area, the profit center weighting and excess return relative to each assigned excess return target will combine to determine the Potential Award for each Eligible Position.
- (i) The ~~Incentive Award Opportunity~~ Potential Award includes a threshold, a maximum, and intermediate levels of Potential Award ~~potential award~~ that correspond to specific levels of investment performance.
- (ii) For the Investment Performance Component, I intermediate levels of the Potential Award for investment performance ~~potential award~~ are determined by linearly interpolating between the threshold and maximum.
- (iii) For the qualitative component ~~Qualitative Component~~, intermediate levels of the Potential Award ~~potential award~~ will be based on a system of annual performance evaluation approved by the Executive Director ~~determined in discrete quartiles~~
- ~~(i) — “Potential Performance Incentive Awards” are the amounts calculated based on the actual performance achieved in the Performance Period. The Incentive Award Opportunity in a Performance Period ranges from zero to 100% of the Maximum Award Opportunity and Potential Performance Incentive Awards are capped at the Maximum Award Opportunity, regardless of whether a Participant exceeds the stated maximum performance levels.~~

4.5. Compliance ~~w~~ With TRS Policies

- (a) IMD Investment Division staff employees exercise fiduciary responsibilities delegated by the Board under applicable law. Investment professionals manage the portfolio according to the Board’s policies, advise and inform the Executive Director and the Board about investments, and recommend modifications to the Investment Policy Statement. In addition, all IMD Investment Division staff employees are responsible for complying with TRS policies, including without limitation the ~~TRS~~ Investment Policy Statement, Ethics Policy, and the Fraud, Waste and Abuse Policy.
- (b) Excess performance by a Participant or Participants resulting from a failure to manage the assets of TRS in accordance with applicable law, the Investment Policy Statement, or TRS Ethics Policy will result in the forfeiture for that portion of the Potential ~~Performance Incentive~~ Awards for those Participants ~~that individual~~ resulting from that excess performance for the Performance Period in which the noncompliance occurred. The Executive Director will make this determination on a case-by-case basis.
- (c) Serious violations of the TRS Investment Policy Statement, Ethics Policy, Fraud, Waste and Abuse Policy, or other TRS policy by a Participant, as determined by the Executive Director, will result in forfeiture of all Potential ~~Performance Incentive~~ Awards ~~calculated~~ for the Performance Period in which the violation(s) occurred, as well as for earlier Performance Periods that have not yet become earned (including without limitation any Potential Awards that are unearned and deferred as set forth in Section 4.8(b) below). Additionally, during the investigation of possible serious violations of law or policy, the Executive Director or the Board may suspend earning and payment of Potential ~~Performance Incentive~~ Awards until the conclusion of the investigation.

4.6. Performance Standards and Measurements

- (a) Investment Performance (for both bBenchmark and pPeer gGroup cCategories) is measured on one year and three year historical performance data, weighted at 33% for one year performance (i.e., performance during the Performance Period) and 67% for the historical three year performance that includes the Performance Period. Investment Performance is measured relative to appropriate pre-defined benchmarks as detailed in the asset allocation and benchmarks table, including applicable footnotes, in the Board's Investment Policy Statement ("IPS"), as amended from time to time-Addendum C. For the purposes of this Plan, changes to the IPS benchmarks during a Performance Period will be effective from and after the effective date of such changes in the IPS, subject to revisions to the Plan adopted by the Board of Trustees. In no event may benchmark changes be applied retroactively except as required to comply with applicable law, including federal tax laws and regulations.
- (b) Notwithstanding Section 4.6(a), the performance of any new profit center will be calculated for purposes of the Plan as follows:
- (i) The investment performance of any new profit center (for both benchmark and peer group categories) will commence with the first full Performance Period commencing on or after the date the profit center is created;
 - (ii) For a new profit center's first full Performance Period, the profit center's investment performance will be based 100% on the profit center's performance data for the first full Performance Period;
 - (iii) For a new profit center's second full Performance Period, the profit center's investment performance will be weighted (x) 50% on the profit center's performance during the second full Performance Period, and (y) 50% on the profit center's two-year performance during the first and second full Performance Periods.
 - (iv) For all Performance Periods commencing after the second full Performance Period, the investment performance of a new profit center will be weighted (x) 33% on the profit center's performance during the one-year Performance Period just ended, and (y) 67% on the profit center's three-year performance during the three full Performance Periods just ended.
 - (v) For the purposes of this Plan, no investment performance will be calculated for a Performance Period for a new profit center created during that Performance Period, unless it existed on October 1 of that Performance Period.
- (c) The qualitative performance ~~Qualitative Performance~~ component is measured annually as part of the Participant's current annual performance appraisal process.
- ~~(e) During the initial implementation of the Plan, Investment Performance will be measured as follows:~~
- ~~(i) For the first year of the Plan (the October 1, 2008 through September 30, 2009 Performance Period), Investment Performance will be measured on two years of historical performance data, weighted at 50% for one year performance (i.e., performance during the Performance Period) and 50% for the performance in the year prior to the Performance Period, except that Fund Performance will be based on one full year of historical performance.~~
 - ~~(ii) For the second year (the October 1, 2009 through September 30, 2010 Performance Period) and subsequent years of the Plan, Investment Performance will be based on one year and three year historical performance as detailed in section 4.6 (a) above, except~~

~~that, for the second year only, Fund Performance will be based on 2 years of historical performance, weighted at 50% for one year performance (i.e., performance during the Performance Period) and 50% for the performance in the year prior to the Performance Period.~~

4.7. ~~Potential Performance Incentive~~ Award Calculations

- (a) Following the end of each Performance Period, the Executive Director will review the actual performance of each Participant relative to the applicable performance components~~Performance Components~~.
- (b) Potential ~~Performance Incentive~~ Awards are calculated based on the Participant's level of performance achieved in the applicable investment performance~~Investment~~ and qualitative performance components~~Qualitative Performance Components~~ in each Performance Period.
- (c) Relative performance data and calculations may be reviewed by an external independent source selected by the Executive Director, but final calculations are approved by the Executive Director.

4.8. ~~Earning Potential Performance Incentive~~ Awards and Payouts

- (a) Notwithstanding the Executive Director's approval of Potential ~~Performance Incentive~~ Award calculations, Potential ~~Performance Incentive~~ Awards will only become earned and payable as stated below:
 - (i) Subject to Section 4.8(b), if a Participant~~the employee~~ is employed by TRS on January 1st following the end of the Performance Period for which that employee was~~they were~~ a Participant, 50% of the Potential Performance Incentive Award will become earned and payable. Payment of this award will generally be processed with that January payroll; for delivery typically issued~~on or about February 1st of that calendar year~~; provided however that in no event will payment be made later than February 15th of that calendar year.
 - (ii) Subject to Section 4.8(b), if a Participant~~the employee~~ is employed by TRS on January 1st following the first anniversary of the end of the Performance Period for which that employee was~~they were~~ a Participant, the remaining 50% of the Potential Performance Incentive Award will become earned and payable. Payment of this award will generally be processed with that January payroll, for delivery typically issued~~on or about February 1st of that calendar year~~; provided however that in no event will payment be made later than February 15th of that calendar year.

The payment dates in respect of a Performance Period shall be the same for all Participants.

- (b) Notwithstanding subsection 4.8-(a), no Potential ~~Performance Incentive~~ Awards will become earned or payable following a Performance Period in which the Fund experiences a total return of zero or less. If this occurs, In this situation, Potential ~~Performance Incentive~~ Awards for that Performance Period that otherwise would~~might~~ have become earned on the January 1st next following the end of that Performance Period will not become earned until January 1st following the next a Performance Period in which the Total Fund experiences has a return greater than zero during a Performance Period, subject to the requirement that assuming the employee be employed by~~is employed by~~ TRS on that January 1st. Payment of this award will be processed with the January payroll, typically issued on or about February 1st of that calendar year; provided however that in no event will payment be made later than February 15thof that calendar year.

- ~~(c) If an employee ceases to be a Participant before the end of a Performance Period due to no longer being employed in an Eligible Position (but is still employed by TRS), Potential Performance Incentive Awards for that Performance Period will not become earned and will not be paid. Potential Performance Incentive Awards from earlier Performance Periods that have not~~

~~yet become earned (as set forth in section 4.8 above), can become earned and be paid according to the terms in section 4.8 above, unless such payments are prohibited by applicable law or conflict with the Board's fiduciary duties.~~

- (~~dc~~) If an employee ceases to be a Participant before the end of a Performance Period due to termination of employment with TRS for any reason other than involuntary termination of employment due to a Reduction in Force ~~reduction in force~~, death, or disability within the meaning of Section 409A of the Internal Revenue Code, a Potential ~~Performance Incentive Awards~~ for that Performance Period will not become earned and will not be paid. Potential ~~Performance Incentive Awards~~ from earlier Performance Periods that have not yet become earned (as set forth in Ssection 4.8(b) above) will not become earned and will not be paid.
- (~~ed~~) If an employee ceases to be a Participant before the end of a Performance Period due to involuntary termination of employment with TRS because of a Reduction in Force ~~reduction in force~~, death, or disability within the meaning of Section 409A of the Internal Revenue Code, a Potential ~~Performance Incentive Awards~~ for that Performance Period will not become earned and will not be paid. Notwithstanding ~~subs~~Sections 4.8(a) – (b), Potential ~~Performance Incentive Awards~~ from earlier Performance Periods will immediately become earned and payable. Payments under this subsection will be made to the terminated employee, or to the estate of the deceased employee, or to the disabled employee, or as otherwise provided by law. These payments will be made as soon as administratively practicable, but no later than 2-½ months after the end of the calendar year in which the Reduction in Force ~~reduction in force~~, death or disability occurred.
- (~~fe~~) If an employee ceases to be a Participant before the end of a Performance Period due to termination of the Plan (as provided for in Section 5.1), a Potential ~~Performance Incentive Awards~~ for that Performance Period will not become earned and will not be paid. Potential ~~Performance Incentive Awards~~ from earlier Performance Periods that have not yet become earned (as set forth in this section~~Section~~ 4.8 ~~above~~), can become earned and be paid according to the terms in this section~~Section~~ 4.8 ~~above~~, if the Board determines that such payments continue to be consistent with and in furtherance of ~~required to perform~~ the fiduciary duties of the Board in administering the retirement system, and if such payments are not prohibited by applicable law.

5. PLAN AUTHORITY AND RESPONSIBILITY

5.1 *Plan Modification, Suspension and Termination*

The Board shall have the right in its sole discretion to modify the Plan or any portion thereof at any time. The Board shall have the right in its sole discretion to suspend or terminate the Plan entirely or any portion thereof at any time. For avoidance of doubt, no modification, amendment, suspension, or reinstatement of this Plan may be given retroactive effect in the administration of this Plan except as required to comply with applicable law, including federal tax laws and regulations.

5.2 *Plan Administration*

Consistent with the provisions of the Plan, the Executive Director has the sole discretion to administer and interpret the Plan. The Executive Director may adopt such procedures and practices as deemed advisable to carry out the Plan.

5.3 *Record Keeping and Reporting*

All employee performance, salary and incentive pay records for the Plan shall be maintained by the Director of Human Resources.

5.4 Compliance ~~w~~With State and Federal Law

If the Executive Director or a court with appropriate jurisdiction determines that ~~any~~ provision ~~portion(s)~~ of the Plan violates applicable state or federal law, that provision ~~portion(s)~~ shall not be given in effect at any time. The remaining provisions ~~portions~~ of the Plan shall remain in full force and effect to the maximum extent possible, and any amendments or modifications that are necessary to give effect to the remaining provisions will be deemed to have been made to allow proper administration of the Plan.

6. AT-WILL EMPLOYMENT

Nothing in the adoption of this Plan or the awarding of performance incentive pay alters the at-will nature of TRS employment ~~that TRS has with its employees~~, creates a contract between TRS and any TRS employee, confers on any TRS employee the right to continued employment with TRS, or affects in any way the right of TRS to terminate the employment of ~~its~~ employees at any time.

7. OTHER PLAN PROVISIONS

7.1. Non-assignment and Non-transferability of Awards

~~Except as authorized in applicable law,~~ Potential ~~Performance Incentive~~ Awards or the actual awards under the Plan are non-assignable and non-transferable and are not subject to anticipation, adjustment, alienation, encumbrance, garnishment, attachment or levy of any kind.

7.2 Plan Does Not Create a Property Interest, Trust, or Entitlement

- (a) Neither the establishment of the Plan, the calculation of Potential ~~Performance Incentive~~ Awards or the actual awards shall be deemed to create a property interest, trust or entitlement. The Plan is an unfunded, unsecured liability of TRS to make payments in accordance with the provisions of the Plan. Any amounts budgeted by TRS for ~~Potential Performance Incentive A~~ awards earned under the Plan shall be the TRS assets ~~of the TRS pension fund~~, and no employee or third party shall have any property, security, or other interest in any assets of TRS by reason of the Plan.
- (b) Nothing ~~contained~~ in the Plan shall be deemed to create or confer ~~give~~ any right, interest, or title to any specific property of TRS to any Participant ~~employee~~, or to any personal representative or beneficiary of a Participant.

7.3 Tax and Other Deductions

All payments under the Plan shall be subject to any deductions (1) for tax and withholding required by federal, state, or local law at the time of payment and (2) for any and all amounts owed by the employee to TRS at the time of payment. TRS is not obligated to advise an employee of the existence of any the tax or the amounts that TRS will be required to withhold.

7.4 Payments Not Eligible for Retirement Purposes

~~There is no intention for payments made pursuant to the Plan to be eligible compensation for TRS pension plan purposes, and, as currently written, a~~ Any payments made pursuant to the Plan are fringe benefits and are not eligible compensation for TRS pension plan purposes.

7.5 Grievances

All grievances related to the Plan will be addressed according to the TRS Grievance and Appeals Policy or any successor policy, as amended from time to time.

8. DEFINITIONS

Base Salary for use in the Plan is the Participant's annualized monthly salary as of October 1st of the applicable Performance Period (not including longevity or benefit replacement pay), or the annualized monthly salary of new Participants as of the date they first become a Participant, as certified by the Director of Human Resources.

Eligible Position is defined in Section 4.4(f). Eligible Positions refers to the positions ~~themselves~~, not the actual Participants in the positions, and includes all positions assigned to the Investment Division and listed ~~as designated in Section 4.4(f) the Plan~~.

~~Incentive Award Opportunity is expressed as a percentage of the Maximum Award Opportunity for a Performance Period.~~

Investment areas are listed in the first column of Addendums A and B.

~~Maximum Potential Award Award Opportunity~~ is defined in Section 4.4(f) and is the maximum Potential Award Incentive Award Opportunity that can become earned and payable with respect ~~available~~ to an Eligible Position during a Performance Period. ~~Depending on the Eligible Position, the Maximum Award Opportunity ranges from 5% to 125% of the Participant's base salary.~~

Participant is an employee in an Eligible Position on October 1st of the Performance Period, or who first is employed in an Eligible Position after the beginning of the Performance Period based on the schedule detailed in the Plan, as certified by the Director of Human Resources.

Performance Period is the period beginning on October 1st of each year and ending on September 30th of the following year.

~~Potential Performance Incentive Awards~~ is defined in Section 4.4(f) and is ~~are~~ the amounts calculated based on the Participant's ~~level of~~ performance achieved in the applicable ~~I~~investment performance and Qualitative Performance Component ~~qualitative performance components~~. A Potential ~~Performance Incentive Awards~~ is ~~are~~ capped at the Maximum Potential Award Award Opportunity, regardless of whether ~~the a~~ Participant exceeds the stated maximum ~~P~~performance. The phrase "award opportunity" is synonymous with Potential Award.

Profit centers are listed in the first row of Addendum A, except that Trade Management is also listed as a profit center in the first row of Addendum B only for peer allocation purposes.

Reduction in Force for use in the Plan refers to termination of an employee due to elimination of the employee's position caused by a required reduction in the number of TRS Full-Time Equivalents (FTEs) or by a required reduction in expenses within the TRS operating budget. The Executive Director has sole discretion in determining whether an employee's termination is due to a Reduction in Force ~~reduction in force~~.

SAA means the Strategic Asset Allocation investment area.

SPN means a Strategic Partner Network investment area. TRS has both private markets and public markets SPNs.

TAA means the Tactical Asset Allocation investment area.

Total Fund means the TRS total or overall investment portfolio and includes all pension assets held in trust by TRS and invested by the IMD to provide retirement, death, and disability benefits administered by the system, including cash and cash equivalents. For avoidance of doubt, for the purposes of the Plan the Total Fund does not include the assets of health plans administered by TRS and held in trust by the Board of Trustees.

Administrative Policy

Reviewer: Executive Director, Chief Investment Officer, Human Resources & Legal Services

Review Cycle: Annually

Authorized by: TRS Board of Trustees

Approved: Brian Guthrie
Executive Director

*This version of the Plan is effective for performance periods beginning on or after October 1, 2012~~2011~~. Any awards for performance in prior Performance Periods can become earned and payable subject to the terms and conditions stated in the versions of the Plan effective for those Performance Periods.

Current Effective Date:
October 1, 2012~~1~~*

First Issued: October 1, 2007

Last Reviewed/Revised:
September 15, 2012~~1~~

Next Review Due:
August, 2013~~2~~

Date: September 15, 2012~~1~~

Date: October 13, 2012~~1~~

Addendum A

Performance Payout Allocation and Maximum Payout Targets vs. Passive Benchmark (50% of Potential Award)

Fund Level	Total Fund	Internal Public	External Public	Private Equity	Risk ¹	Stable Value / SAA	Real Assets	TAA	Public and Private SPN and Opportunistic ²	Natural Resources	Emerging Managers	Total
Index	Total Fund Policy Composite Index	Global Equity Portfolio vs. MSCI ACWI Free (net)	Daily Weighted Excess Return Based on Actual Portfolio Weights	State Street Private Equity Index	Daily Weighted Excess Return Based on Actual Portfolio Weights	Daily Weighted Excess Return Based on Actual Portfolio Weights	NCREIF	Total Profit & Loss for Incentive Period/Total Trust Average Daily Balance	Daily Weighted Excess Return Based on Actual Portfolio Weights	Daily Weighted Excess Return Based on Actual Portfolio Weights	Daily Weighted Excess Return Based on Actual Portfolio Weights	
Excess Return Target	100 bps	50 bps	100 bps	300 bps	75 bps	35 bps	250 bps	25 bps	175 bps	175 bps	100 bps	
CIO/Deputy CIO	75.00%					5.00%	5.00%		5.00%	5.00%	5.00%	100.00%
Risk	50.00%	5.00%	5.00%	5.00%	20.00%	5.00%	5.00%	5.00%				100.00%
Internal Public Markets	30.00%	60.00%	5.00%	5.00%								100.00%
External Public Markets	30.00%	5.00%	60.00%	5.00%								100.00%
Private Equity	30.00%	5.00%	5.00%	60.00%								100.00%
Stable Value / SAA	50.00%					50.00%						100.00%
Real Assets	30.00%						60.00%			10.00%		100.00%
Tactical Asset Allocation (TAA)	30.00%							60.00%	10.00%			100.00%
Public and Private SPN / Opportunistic	30.00%							10.00%	60.00%			100.00%
Natural Resources	30.00%	10.00%		-	-					60.00%		100.00%
Emerging Managers	30.00%		10.00%	10.00%			10.00%				40.00%	100.00%
Trade Management Group	30.00%	20.00%	10.00%			20.00%		20.00%				100.00%
Investment Operations	50.00%	10.00%	10.00%	5.00%		10.00%	5.00%	10.00%				100.00%

Notes: ¹ Risk group allocation excludes Trust hedging activities. ² Benchmark for Public SPN is the SPN Composite Index.

Addendum B
Performance Payout Allocation and Maximum Payout Targets vs. Peer Group Comparison
(30% of Potential Award)

Fund Level	Total Fund	Trade Management Group	Private Equity	Real Assets	Total
Index	TUCS Public Funds > \$10 Billion Universe	ITG / Plexus	TUCS Private Equity > \$1 billion Universe	Real Estate vs. TUCS Real Estate > \$1 billion Universe	
Excess Return Target	100 bps	8 bps	300 bps	250 bps	
CIO/Deputy CIO	90.00%	0.00%	5.00%	5.00%	100.00%
Risk	90.00%	0.00%	5.00%	5.00%	100.00%
Internal Public Markets	95.00%	0.00%	5.00%	0.00%	100.00%
External Public Markets	95.00%	0.00%	5.00%	0.00%	100.00%
Private Equity	40.00%	0.00%	60.00%	0.00%	100.00%
Stable Value / SAA	70.00%	30.00%	0.00%	0.00%	100.00%
Real Assets	40.00%	0.00%	0.00%	60.00%	100.00%
Tactical Asset Allocation (TAA)	100.00%	0.00%	0.00%	0.00%	100.00%
Public and Private SPN / Opportunistic	90.00%	10.00%	0.00%	0.00%	100.00%
Natural Resources	90.00%	0.00%	0.00%	10.00%	100.00%
Emerging Managers	80.00%	0.00%	10.00%	10.00%	100.00%
Trade Management Group	50.00%	50.00%	0.00%	0.00%	100.00%
Investment Operations	50.00%	40.00%	5.00%	5.00%	100.00%

ADDENDUM C Benchmark Plan for Performance Period Commencing On October 1, 2011

(Note: The benchmarks in Addendum C shall be revised, if necessary, at the beginning of each performance period (October 1) to conform to the benchmarks in the TRS Investment Policy Statement in effect on that date, subject to other action of the Board to modify the Plan.)

Asset Class	Benchmark¹	Bloomberg Ticker	Target
Global Equity:			
US Large Cap	MSCI USA Standard	GDDUUS	18%
US Small Cap	MSCI USA Small Cap	GCUDUS	2%
Non-US Developed	MSCI EAFE and Canada	NDDUEC	15%
Emerging Markets	MSCI EM	NDUEEGF	10%
Directional Hedge Funds	HFRI Fund of Funds Composite	HFRIFOF	5%
<i>Total Public Equity</i>	<i>Target weighted Blend</i>		<i>50%</i>
Private Equity	State Street Private Equity Index—lagged one quarter ²		12%
Total Global Equity	Target weighted Blend		62%
Stable Value:			
US Treasuries	Barclays Capital (BarCap) Long Treasury Index	LUTLTRUU	13%
Absolute Return (Including Credit Sensitive Investments)	3-Month LIBOR + 2%	USC0TR03 (plus 2%)	0%
Stable Value Hedge Funds	HFRI Fund of Funds Conservative	HFRIFOFC	4%
Cash	Citigroup 90-day US Treasury	SBMMTB3	1%
Total Stable Value	Target weighted Blend		18%
Real Return:			
Global Inflation Linked Bonds	BarCap US Treasury TIPS index	LBUTTRUU	5% ³
Real Assets	NCREIF ODCE—lagged one quarter ²		15% ³
Commodities	Goldman Sachs Commodity Index	SPGCCITR	0% ³
REITS	MSCI US REIT	RMS-G	0% ³
Total Real Return	Target weighted Blend		20%
TOTAL PLAN	Target weighted Blend		100%

¹ The table in Addendum A will reference the MSCI ACWI Free (net) index for the columns titled “External Public Markets” (with respect to those external managers benchmarked to the MSCI ACWI) and “Total Internal Public Markets”.

² Due to the delay in availability of final performance data for Private Equity and Real Assets, performance measurements for these two Investment Areas will experience a one quarter time lag, such that all incentive calculations involving Private Equity and Real Assets performance will use data for the 12-month period ending each June 30th.

³ On October 1 of each year, the Target for Real Assets for the following twelve months will be reset by the CIO to the averaged funded level of Real Assets for such succeeding twelve months as projected by the Real Assets investment management team (rounded to the nearest whole percentage); provided, the Target for Real Assets may not be more than 15%. Any decrease to the Target for Real Assets below 15% will result in an equivalent amount of increase allocated to the Targets for first, REITS (until REITS is 2%), second, Commodities (until Commodities is 2%) and, third, Global Inflation Linked Bonds.

ADDENDUM A
Performance Payout Allocation and Maximum Payout Targets vs. Passive Benchmark
(50% of Incentive Award Opportunity)

Fund Level	Total Fund	Strategic Partners	Total Internal Public Markets	External Public Markets	Private Equity	Real Return	Total Incentive Weight
Index	Policy / Transition Index	SPN Composite Index	Global Equity Portfolio vs. MSCI ACWI Free (net)	Daily Weighted Excess Return Based on Actual Portfolio Weights	State Street Private Equity Index	NCREIF	
Excess Return Target	100 bps	130 bps	50 bps	100 bps	300 bps	250 bps	
CIO/Deputy CIO	70.0%		10.0%	10.0%	5.0%	5.0%	100.0%
SRRM Group	60.0%	10.0%	10.0%	10.0%	5.0%	5.0%	100.0%
Internal Public Markets	30.0%		60.0%	10.0%			100.0%
External Public Markets	30.0%		5.0%	60.0%	5.0%		100.0%
Private Equity	30.0%		5.0%	5.0%	30.0%	30.0%	100.0%
Real Estate	30.0%		5.0%	5.0%	30.0%	30.0%	100.0%
Trade Management Group	30.0%		60.0%	10.0%			100.0%
Administrative Center	70.0%		10.0%	10.0%	5.0%	5.0%	100.0%



Memorandum

DATE: September 7, 2012
TO: Compensation Committee; Board of Trustees
FROM: Janet Bray, Scot Leith, Dennis Gold
RE: Supplemental Materials for Annual Review of Performance
Incentive Pay Plan commencing October 1, 2012

To aid your further review and discussion of the proposed Plan, attached are the following supplemental materials:

1. A manually marked draft of Addendum A showing the proposed changes to last year's adopted version;
2. A manually marked draft of Addendum B showing the changes proposed changes to last year's adopted version;
3. Two charts prepared by Scot Leith, Investment Accounting, describing performance benchmark development for the calculation of performance and Potential Awards under the Plan;
4. A condensed version of the Plan overview delivered by Janet Bray, Director of Human Resources, at the July 2012 meeting; and
5. A draft organizational chart for the Investment Management Division that illustrates changes made in July 2012. For purposes of the Plan, these changes will be effective only as of October 1.
6. For comparison purposes, an organization chart for the IMD as of February 2012.

Items 1 and 2 include explanatory notes at the foot of each addendum. The proposed changes to the investment areas derive from organizational changes in the Investment Management Division, but also include revisions of the percentage allocations of performance among the various investment areas. Note that the new Natural Resources investment area has not yet begun operations.

Item 3 provides details about the benchmarking process. Note that Addendum A specifies excess return targets (3rd row) for each investment area as compared to a passive benchmark for each area, and that this calculation represents 50 percent of a Potential Award. Addendum B specifies excess return targets for each investment area as compared to defined peer groups for each area, and that this calculation represents 30 percent of a Potential Award. Note that the Trading Management Group investment area does not have a benchmark listed on Addendum A because there is no *investment performance benchmark* for that area. For that reason, that area is not listed in **Item 3**. However, a *peer group comparison* for the Trading Management Group area is listed on Addendum B, which is defined as the ITG / Plexus reporting on industry trade execution. Qualitative Factors are 20 percent of a Potential Award (see **Item 4, Incentive Calculation Basis**, and related note).

Item 4 provides a summary overview of the key characteristics of the Plan, including the Plan philosophy regarding compensation.

Item 5 illustrates the investment areas that are listed in Addendum A and Addendum B to the Plan.

Item 6 shows the organizational structure prior to the recent reorganization.

We hope this additional information is helpful.

September 6, 2012 marked draft Addendum A

Performance Payout Allocation and Maximum Payout Targets vs. Passive Benchmark (50% of Potential Award)

Fund Level	Total Fund	Strategic Partners	Total-Internal Public Markets	External Public Markets	Private Equity	Risk ¹	Stable Value / SAA	Real Assets Return	TAA	Public and Private SPN and Opportunistic ²	Natural Resources	Emerging Managers	Total Incentive Weight
Index	Total Fund Policy Composite/ Transition Index	SPN Composite Index	Global Equity Portfolio vs. MSCI ACWI Free (net)	Daily Weighted Excess Return Based on Actual Portfolio Weights	State Street Private Equity Index	Daily Weighted Excess Return Based on Actual Portfolio Weights	Daily Weighted Excess Return Based on Actual Portfolio Weights	NCREIF	Total Profit & Loss for Incentive Period / Total Trust Average Daily Balance	Daily Weighted Excess Return Based on Actual Portfolio Weights	Daily Weighted Excess Return Based on Actual Portfolio Weights	Daily Weighted Excess Return Based on Actual Portfolio Weights	
Excess Return Target	100 bps	130 bps	50 bps	100 bps	300 bps	75 bps	35 bps	250 bps	25 bps	200 bps	175 bps	100 bps	
CIO/Deputy CIO	75%70%		10%	10%	5%	0%	5%	5%		5%	5%	5%	100%
Risk SRRM Group	50%60%	10%	5%10%	5%10%	5%	20%	5%	5%	5%				100%
Internal Public Markets	30%		60%60%	5%10%	5%-								100%
External Public Markets	30%		5%5%	60%60%	5%								100%
Private Equity	30%		5%5%	5%5%	60%30%			30%					100%
Stable Value / SAA	50%	[NA]					50%						
Real Assets Estate	30%		5%	5%	30%			60%30%			10%		100%
Tactical Asset Allocation (TAA)	30%	[NA]							60%	10%			
Public and Private SPN / Opportunistic	30%	[NA]							10%	60%			
Natural Resources	30%	[NA]	10%								60%		
Emerging Managers	30%	[NA]		10%	10%			10%				40%	
Trade Management Group	30%		20%60%	10%			20%		20%				100%
Investment Operations Administrative Center	50%70%		10%10%	10%	5%		10%	5%	10%				100%

Notes: ¹ Risk group allocation excludes Trust hedging activities. ² Benchmark for Public SPN is the SPN Composite Index.

Notes to draft:

- Unnecessary decimals have been deleted without marking that change.
- The SRRM Group has been divided into these discrete new investment areas: Risk; Stable Value / Strategic Asset Allocation (“SAA”); and Tactical Asset Allocation (“TAA”) (see IMD Org Chart).
- Management of the public external manager and private markets strategic partnerships network (“SPN”) has been consolidated into a separate new investment area called “Public and Private SPN / Opportunistic” (see IMD Org Chart).
- Management of the emerging managers programs has been consolidated into a new investment area called “Emerging Managers” (see IMD Org Chart).
- Investment management is creating a new investment area called “Natural Resources,” which will have a dedicated team of IMD investment employees led by a new hire (See IMD Org Chart).

September 6, 2012 marked draft ADDENDUM B
Performance Payout Allocation and Maximum Payout Targets vs. Peer Group Comparison
(30% of Potential Incentive-Award Opportunity)

Fund Level	Total Fund	Trade Management Group	Internal Public Markets	External Public Markets	Private Equity	Real Assets Return	Total
Index	Total Fund vs. TUCS Public Funds >\$10 Billion Universe	ITG / Plexus	No-Peer	No-Peer	TUCS Private Equity >\$1Billion Universe	Real Estate TUCS Real Estate >\$1Billion Universe	
Excess Return over Median Target	100 bps	8 bps			300 bps	250 bps	
CIO/Deputy CIO	90% 70%	0%	10%	10%	5%	5%	100%
Risk SRRM Group	90% 50%	0% 10%	10%	10%	10%	10%	100%
Internal Public Markets	95% 30%	0%	60%	10%	5%	0%	100%
External Public Markets	95% 30%	0%	5%	60%	5%	0%	100%
Private Equity	40% 30%	0%	5%	5%	30%	30%	100%
Stable Value / SAA	70%	30%	[NA]	[NA]	0%	0%	100%
Real Assets Estate	40% 30%	0%	5%	5%	0% 30%	60% 30%	100%
Tactical Asset Allocation (TAA)	100%	0%	[NA]	[NA]	0%	0%	100%
Public and Private SPN / Opportunistic	90%	10%	[NA]	[NA]	0%	0%	100%
Natural Resources	90%	0%	[NA]	[NA]	0%	10%	100%
Emerging Managers	80%	0%	[NA]	[NA]	10%	10%	100%
Trade Management Group	50% 30%	50% 60%	10%	0%	0%	0%	100%
Investment Operations Administrative Center	50%	40%	10%	10%	5% 10%	5% 10%	100%

Notes to draft:

- Unnecessary decimals have been deleted without marking that change.
- The SRRM Group has been divided into these discrete new investment areas: Risk; Stable Value / Strategic Asset Allocation (“SAA”); and Tactical Asset Allocation (“TAA”) (see IMD Org Chart).
- Management of the public external manager and private markets strategic partnerships network (“SPN”) has been consolidated into a separate new investment area called “Public and Private SPN / Opportunistic.”
- Management of the emerging managers programs has been consolidated into a new investment area called “Emerging Managers.”
- Investment management is creating a new investment area called “Natural Resources,” which will have a dedicated team of IMD investment employees led by a new hire.

Incentive Plan Benchmark Comparison

Investment Area	PureView / Policy Benchmark	Incentive Compensation Benchmark
Total Fund	Daily calculation based on the IPS Normal Asset Allocation	Same
Total Internal Public Markets	Global Best Ideas vs. MSCI All Country World Index	Same
Private Equity	State Street Private Equity Index	Same
Real Assets	NCREIF	Same
External Public Markets	Daily Weighted Excess Return Based on Actual Portfolio Weights	Same: Every day, the sum of each portfolio group's weights across each asset class multiplied by the appropriate index return of each asset class determines the daily index for the specific portfolio group
Risk	Daily Weighted Excess Return Based on Actual Portfolio Weights	
Stable Value / SAA	Daily Weighted Excess Return Based on Actual Portfolio Weights	
Public and Private SPN and Opportunistic	Daily Weighted Excess Return Based on Actual Portfolio Weights	
Natural Resources	Daily Weighted Excess Return Based on Actual Portfolio Weights	
Emerging Managers	Daily Weighted Excess Return Based on Actual Portfolio Weights	
TAA	Total Profit & Loss for Incentive Period / Total Trust Average Daily Balance	Same: Calculated by dividing the Total Value Added across all TAA controlled accounts by the Average Daily Trust Net Asset Value during the incentive period.

Incentive Plan Benchmark Details

Investment Area	PureView / Policy Benchmark	Incentive Compensation Benchmark
Total Fund	Daily calculation based on the IPS Normal Asset Allocation	Same
Total Internal Public Markets	Global Best Ideas Flagship Portfolio vs. MSCI All Country World Index	Same
Private Equity	State Street Private Equity Index	Same
Real Assets	NCREIF ODCE	Same
External Public Markets	Daily Weighted Excess Return Based on Actual Portfolio Weights across MSCI USA Standard, MSCI USA Small Cap, MSCI EAFE and Canada, MSCI EM, HFRI Fund of Funds Composite, HFRI Fund of Funds Conservative and 3 Month LIBOR + 2%	<p>Same:</p> <p>Every day, the sum of each portfolio group's weights across each asset class multiplied by the appropriate index return of each asset class determines the daily index for the specific portfolio group</p>
Risk	Daily Weighted Excess Return Based on Actual Portfolio Weights initially across HFRI Fund of Funds Composite with MSCI USA Standard added in 2014 and other benchmarks as needed.	
Stable Value / SAA	Daily Weighted Excess Return Based on Actual Portfolio Weights across HFRI Fund of Funds Composite, Barclays Capital Long Treasury Index, Citigroup 90-day US Treasury Index, HFRI Fund of Funds Conservative, 3 Month LIBOR + 2% and Barclays Capital US Treasury TIPS Index	
Public and Private SPN and Opportunistic	Daily Weighted Excess Return Based on Actual Portfolio Weights across Public SPN Benchmark ¹ , State Street Private Equity Index and NCREIF ODCE.	
Natural Resources	Daily Weighted Excess Return Based on Actual Portfolio Weights initially across NCREIF ODCE, State Street Private Equity Index, and Goldman Sachs Commodity Index with other benchmarks as needed.	
Emerging Managers	Daily Weighted Excess Return Based on Actual Portfolio Weights across MSCI USA Standard, MSCI USA Small Cap, MSCI EAFE and Canada, MSCI EM, State Street Private Equity Index and NCREIF ODCE.	
TAA	Total Profit & Loss for Incentive Period / Total Trust Average Daily Balance.	<p>Same:</p> <p>Calculated by dividing the Total Value Added across all TAA controlled accounts by the Average Daily Trust Net Asset Value during the incentive period.</p>

¹ Public SPN Benchmark mirrors the trust public benchmark allocation.

Performance Pay Plan Overview

Plan Characteristics for 2012 Plan

Start Date	October 1, 2011
Performance Period (Plan Year)	October 1, 2011- September 30, 2012
Payout Date	February 1st

Incentive Calculation Basis	
Excess of Benchmark	50%
Peer Group Comparison	30%
*Qualitative Factor	20%

Excess Above Benchmark for Max (total fund)	100 basis points
Target Peer Group Comparison	Basis points above median (max payout at 100 bp)
Performance Measured (for benchmark and peer group)	3 year and 1 year returns

Maximum Award Opportunity	
CIO, Deputy CIO, Sr. Managing Directors & Managing Directors	125%
Sr. Directors and Directors	110%
Sr. Investment Managers and Investment Managers	90% to 85%
Investment Analysts, Operations, Administrative and Support	65% to 5%

# of Staff Eligible for Incentive	up to 112
Maximum Cost	\$11.3 million
Expected Value Added at Max.	at least \$1.1 billion

*Qualitative factor is only paid if either Benchmark or Peer Group factor is achieved.

Quick Facts on Performance Pay

Plan start date:	Established by the TRS Board in 2007
Purpose:	Attract, motivate and retain highly talented investors with a unique dedication to teachers
Philosophy:	Competition for investment talent is with top <u>private</u> sector funds <ul style="list-style-type: none"> ▪ <u>First quartile base pay</u> (among large <u>public</u> funds) ▪ <u>Fourth quartile performance pay</u> (among small <u>private</u> funds) ▪ Address remaining compensation gap with purpose, leadership, place and culture
Plan Basics:	<ul style="list-style-type: none"> ▪ Performance awards are based primarily on value added above "passive benchmarks" and/or returns earned by comparable pension funds (peer groups) ▪ Performance awards are based on one-year (33%) and three-year results (67%) ▪ Performance awards earned are paid over two years (50% each year) ▪ Payouts are made only when the overall Trust has a positive return ▪ Payouts are deferred if value is added but Trust returns are negative until the overall trust has a positive return ▪ Payouts are forfeited if employee leaves TRS or if an employee willfully violates an approved risk constraint
Key Performance Components:	<ul style="list-style-type: none"> ▪ 50% versus passive benchmark(s) ▪ 30% versus peer group results ▪ 20% based on individual productivity rankings of all IMD employees (productivity payouts only made if value added is achieved) <ul style="list-style-type: none"> ▪ Nine-Box Productivity Rating system used to determine productivity rankings
Performance Pay:	<ul style="list-style-type: none"> ▪ Maximum payout ranges between 5% and 125% of base salary ▪ Higher percentages are due to increased seniority and responsibility

BRITT HARRIS, Chief Investment Officer

Jerry Albright, Deputy CIO

Susan Wade

Stacy Sakoulas

Deputy Admin Support

Marina Salazar

Debbie Ferguson

Nonique Gonzalez

Paul Waclawsky

Admins

Sharon Toalson
Susan K. White

Chief of Staff

David Veal
Tommy Albright

Risk

Jase Auby
Managing Dir

TAA

Curt Rogers
Managing Dir

James Nield
Matt Talbert
Mark Telschow
Stephen Kim
Mike Simmons

JB Daumerie
Jingshan Fu
Daniel Ting
West Garrett

Strategic Partners

Ashley Baum
Grant Birdwell

Energy/Natural Resources

Investment Operations
Sylvia Bell
Director

Bus Center

Cash Securities

Patricia Cantu
Sheila Anderson
Maribel Nesuda
Hugo Rangel
Becky Van Eenemaan
Kristi Vorce
Irma Z-Castillo

Kendall Courtney
Karoline Freeman
LeeAnn Gola
Sean Letcher
Lilly Rodgers
Babette Ruiz

Derivatives

Kelly Newhall
Steven Lambert
Christopher Pan
Anthony Paolini

IIS

David Cox
Barbara Forssell
DC Gunnia
Roy Kurian
Jelena Melesenko
Scott Sewell

Performance

Craig McCullough
Ranu Dutta
Jared Simpson
Barbara Woodard
Layne Haggberg

STABLE VALUE-18%

Passive Portfolios
Mohan Balachandran
Managing Director
Bernie Bozzelli

Stable Value

Mohan Balachandran
Tim Jones
Tony Yiu
Hasim Mardin

Trading

Bernie Bozzelli
Pat Barker
Jaime Llano
Scott Moore
Steven Peterson
Demetrius Pope
Komson Silapachi
Jared Morris

GLOBAL EQUITY -62%

Ext Public-12/6
Dale West
Managing Director

Ext Mgrs

Susanne Gealy
Rusty Guinn
Joe Tannehill

Hedge Funds

Brad Gilbert
Todd Centurino
Rachel Clark

Fixed Income

Katy Hoffman
Lulu Llano
Jonathan Klekman
Steven Wilson

Scott Gonsoulin
Mikhael Rawls
Kyle Schmidt
Patty Steinwedell
Courtney Yarbrough

Int Public
Chi Chai
Sr. Managing Director

Portfolio Management

David DeStefano
Kay Cuclis
Patrick Cosgrove
Jon Hook
Ralph Linn
Shayne McGuire

Quant

Janis Hydak
Mark Albert
Jeremy Aston
Terri Krumnow
Monica Larson
Matt Robertson
Wayne Speer
Solomon Gold

Research

Shayne McGuire
Phillip Auth
Tom Cammack
Richard Campbell
Lee Carter
Mark Cassens
John DeMichele
Marissa Hogan
Kevin Lincoln
Stacey Peot
Marshall Reid
Corina Scoggins
Dan Steinberg
KJ VanAckeren
John Watkins

Ext Public
Rich Hall
Managing Director

Private Equity

Michael Lazorik
Allen MacDonell
Gracie Marsh

Scott Ramsower
Neil Randall
Molly Rose
Brad Thawley
Courtney Villalta
Ross Willman

Kamal Maruf
Carter Ware

REAL RETURN-20%

Real Assets
Eric Lang
Managing Director

Brian Baumhover
Chase Hill
Melissa Kleihege
Michael Pia
John Ritter
Craig Rochette
Grant Walker
Jennifer Wenzel
Nathan Zinn

**Emerging Mgrs/
Investor Relations**

Stuart Bernstein
Andy Cronin

Red font-contractors

Note: contractors are not eligible for performance pay.

Draft; subject to change.

Jerry Albright, Deputy Chief Investment Officer*

Professional Development

Susan Wade Stacy Sakoulas

Deputy Admin Support
Marina Salazar

PROFIT CENTERS

INVESTMENT OPERATIONS

External Public
Dale West*
Managing Director

Internal Public
Chi Chai*
Sr. Managing Director

Sylvia Bell*
Director

External Managers

Susanne Gealy
Rusty Guinn
Joe Tannehill

Portfolio Management

David DeStefano
Kay Cuclis
Patrick Cosgrove
Jon Hook
Ralph Linn
Shayne McGuire
Macro, Themes & Quant
Janis Hydak

Business Center

Travel, Budget, Staff Svc, Reporting
Patricia Cantu
Rachel Anderson
Sheila Anderson
Becky Van Eenemaan
Debbie Ferguson
Nonique Gonzalez
Hugo Rangel
Maribel Nesuda
Kristi Vorce
Irma Zavaleta-Castillo

Performance Analytics

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Ranu Dutta
Felicia Jones
Jared Simpson
Barbara Woodard
Layne Haggberg

Hedge Funds

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Todd Centurino
Rachel Clark

Mark Albert
Jeremy Aston

Fixed Income Strategies

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Katy Hoffman
Lulu Llano
Jonathan Klekman

Terri Krumnow
Monica Larson
Matt Robertson
Wayne Speer
Solomon Gold

Research

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Phillip Auth
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Richard Campbell
Mark Cassens
John DeMichele
Amit Kumar
Kevin Lincoln
Stacey Peot
Marshall Reid
Corina Scoggins
Tayyib Shah
Dan Steinberg
KJ VanAckeren
John Watkins

Derivatives

Kellv Newhall
Steven Lambert
Christopher Pan
Anthony Paolini

Cash Settlements

Kendall Courtney
Karoline Freeman
Lilly Rodgers
Babette Ruiz
Scott Gonsoulin

Information Systems

David Cox
Barbara Forssell
DC Gunnia
Roy Kurian
Jelena Melesenko
Scott Sewell

IIC Members*

Britt Harris	Chi Chai
Jerry Albright	Steve LeBlanc
Jase Auby	Nigel Lewis
Sylvia Bell	Dale West

Red font-contractors

CIO Chief of Staff
Ashley Baum

CIO Admin Support
Sharon Toalson Susan K. White

PROFIT CENTERS

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Sr. Managing Director

Portfolio Strategy and Execution

Strategic Research
Nigel Lewis*
Sr. Managing Director

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Brian Baumhover
Andy Cronin
Chase Hill
Michael Pia
John Ritter
Craig Rochette
Molly Rose
Grant Walker
Jennifer Wenzel
Nathan Zinn

Tactical Asset Alloc

Curt Rogers
Grant Birdwell
JB Daumerie
Tim Jones
Brandon Kunz
Tony Yiu
Hasim Mardin
West Garrett

Mike Simmons
Kyle Boyd
Patrick Meyer

PE & Principal

Richard Hall, MD
Michael Lazorik
Allen MacDonell
Scott Ramsower
Neil Randall
Brad Thawley
Courtney Villalta
Ross Willman
Muhammad Mian
Kamal Maruf

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Jingshan Fu
James Nield
Matt Talbert
Mark Telschow

Trade Management

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Pat Barker
Jaime Llano
Scott Moore
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Demetrius Pope
Komson Silapachi
Jared Morris

Emerging Managers

Stuart Bernstein

EPM Support
Melissa Kleihege
Gracie Marsh
Cynthia Mendoza

Superseded