

# The Ambachtsheer Letter

Research and Commentary on Pension Governance, Finance and Investments

Letter # 299

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## PAYING FOR PERFORMANCE:

### THE CASE OF THE CPP INVESTMENT BOARD - PART I

*“We give due and careful consideration to management compensation. The CPPIB has developed a compensation framework that meets, and in many ways exceeds the best-practice principles set out by the G20 nations. This includes a pay-for-performance formula within a risk framework approved by the board of directors.”*

Robert Astley  
Board Chair, CPP Investment Board  
CPPIB 2010 Annual Report

#### A Case Study

This *Letter* continues to explore ‘Tomorrow’s Pension Fund’ with its five success drivers. Last month’s *Letter* studied one of these drivers, competitive compensation, in considerable detail. The result was a framework of the key issues pension fund boards and managements must address in effective compensation design for their organizations, and the principles that should guide that quest. A common thread to the feedback we received on last month’s *Letter* was: “yes, but can all this work in practice?” We address that question in this, and next month’s *Letter*.

Why use the organization created to manage the reserve assets of the Canada Pension Plan (CPP) as the case study to address the question? For two reasons. First, the CPP Investment Board 2010 Annual Report describes its current ‘pay for performance’ compensation scheme in considerable detail. Second, we had some involvement in the design of the organization in the 1990s. So we have been a keen observer of the evolution towards its status today as a C\$128B professional investment management organization employing 566 people, with offices in Toronto, London, and Hong Kong. Stating the second reason differently, an organization’s current governance and compensation practices cannot be fully understood without knowing the path it took to get there.

#### Compensation Principles

Maslow’s Hierarchy of Human Needs provided key insights to last month’s construction of a conceptual framework for compensation in pension funds. For example, once compensation is sufficient to meet basic physical needs such as food and shelter, meeting softer needs such as self-esteem, confidence, respect by, and service to others, takes over. A question Maslow’s framework raises is the role compensation plays in meeting these softer needs. Is money the main driver of meeting these needs? Or can pension funds offer other types of compensation (e.g., intellectual stimulation, a collegial environment) to the knowledge workers it needs to attract and retain to achieve its mission? Management philosopher Peter Drucker certainly thought so.

In acknowledging the power of today’s ‘pay for performance’ mantra, last month’s *Letter* noted the important distinction between the setting and achievement of corporate and investment goals:

- Setting and achieving corporate goals means assessing organizational effectiveness in such areas as strategic planning and organization design, branding and stakeholder relations, research and innovation, and attracting and retaining the right people.