

HIGH PAY, LOW RETURNS: WHY ARE OMERS' EXECUTIVES PAID SO MUCH?

February 2022



The Ontario Municipal Employees' Retirement System (OMERS) is the province's defined benefit (DB) pension plan for municipal, school board and child welfare workers. CUPE Ontario represents 125,000 of 289,000 OMERS plan members – just under half of OMERS active membership.

CUPE Ontario strongly believes that DB pension plans are the best way to provide a decent and secure retirement for our hard-working members. Large public sector DB plans, like OMERS, allow for an efficient pooling and sharing of costs and risks between employers and plan members. DB plans allow members to know what their pensions will be in retirement. This retirement income security is incredibly important for plan members and their communities.

How OMERS operates, performs, and provides pension benefits is of the utmost importance to CUPE because it directly impacts a large portion of our Ontario membership. As a jointly sponsored pension plan, our members share in risks associated with poor performance returns and high costs.

CUPE Ontario has raised concerns with the administration of OMERS in the past. Last year, we published, "Not Just One Tough Year" which clearly showed that over the past decade, OMERS investment returns have underperformed its own investment benchmarks and the investment returns of comparable defined benefit pension plans and funds.

A second related issue that has consistently concerned CUPE members in OMERS is the high levels of compensation provided to executives at OMERS; especially in light of their history of investment underperformance. OMERS executives each earn millions of dollars annually. OMERS executives receive a generous base salary, attractive bonus compensation and an additional non-registered pension which is rich enough to exceed the regulated pension limits under the *Income Tax Act*.

Like most large Canadian pension plans, OMERS posts the annual compensation provided to its top five executives. When we compare this remuneration, OMERS appears to provide a more generous compensation packages to their top brass than what is provided to the top executives of other large Canadian pension plans. When we control for the size of the plan, its performance, and its success in achieving benchmarks, the compensation paid to OMERS' executives are even more excessive.

This is particularly concerning given that the average OMERS pensioner received just over \$24,000 per year in pension in 2020¹ with many receiving pensions well below that average, particularly lower-waged workers who are disproportionately female and racialized. Also, OMERS is currently conducting a risk review which



CUPE Ontario fears could lead to proposals to reduce pension benefits for plan members in the future. Given this context and the dismal underperformance of OMERS investments over the past decade, the pension plan's executive compensation bears scrutiny.

In this paper we compare OMERS executive compensation to its own investment performance and to other large (\$50 billion+) pension plans and funds in Canada. OMERS themselves refer to this club of large plans and funds as the "eight leading Canadian pension plan investment managers" and occasionally undertakes coordinated activity with them.

Because compensation varies with performance, we looked at the compensation for the top five executive positions over a ten-year period from 2011 until 2020.

The pension plans we looked at are:²

Canada Pension Plan Investment Board (CPPIB)*

Caisse de dépôt et placement du Québec (CDPQ)

Ontario Teachers Pension Plan (OTPP)

Public Sector Pension Investment Board (PSP)*

BC Municipal Pension Plan BCMPP*

Alberta Investment Management Corporation (AIMCO)

Ontario Municipal Employee's Retirement Savings Plan (OMERS)

The numbers we pulled were from the top five reported executives from each pension plan. We acknowledge that each of the plans cited here uses somewhat different methods to determine and report executive compensation. However, we believe that they are still comparable, especially when looked at over a ten-year time frame.

The eighth pension plan in this group is the Health Care of Ontario Pension Plan (HOOPP). We were unable to get compensation information for HOOPP because that plan does not publicly report executive compensation.

² The numbers are for a ten-year period from January 1, 2011 until December 31, 2020. Those Pension Plans with an asteriks "*" beside them report on a fiscal basis with a year end of March 31st. The ten-year period for those pension plans is April 1, 2010 until March 31, 2020. Unless otherwise specified, the data in this document has been compiled from publicly available annual reporting of the respective plans. With the exception of CDPQ, returns are as reported in these documents, and are net. CDPQ results were reported gross of some expenses, and have been reduced by 0.2% to best approximate a net return. Longer-term periods are annualized, and are as reported by the respective plans.



How is Compensation Determined

Generally, executive compensation is determined by a number of factors. First, the size of the plan has an impact. Executives who are responsible for larger sums of money are, in general expected to make more than executives who are responsible for smaller sums.

Second, performance is taken into account. Executives who meet or exceed investment and other performance goals are generally remunerated at a higher rate than those who do not.

Finally, looking at the rates for compensation in similar positions will give us a sense of what is needed in order to attract skilled talent.

OMERS pays its executives in four envelopes: base salary, short term incentive plan, long term incentive plan and benefits. The base salary is a fixed amount. The short-term and long-term incentive plans are based on achieving certain performance goals. Long term incentives are held back for three years before being paid out. While it is not completely clear from publicly available data what is and is not included in the package to determine short and long-term incentives, investment returns are certainly a large part of the performance goals.

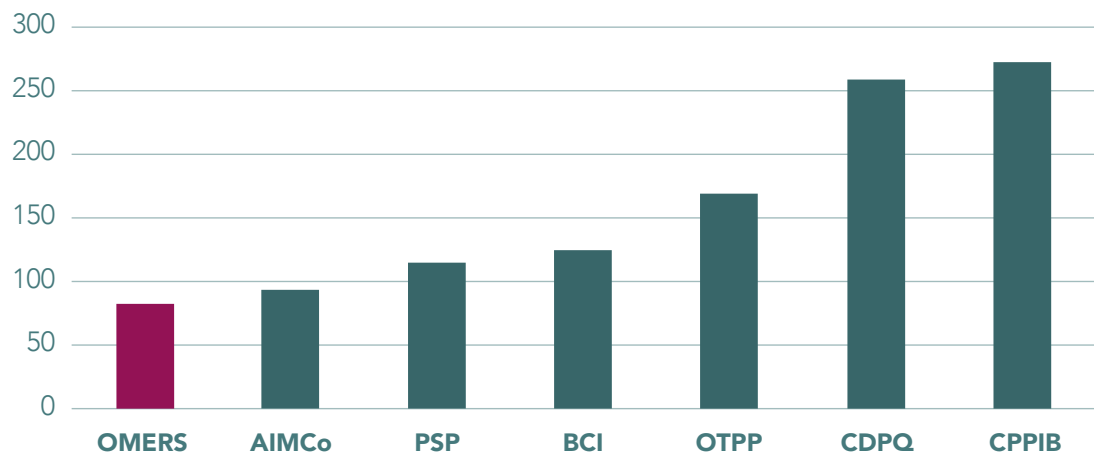
Findings

1. The size of OMERS does not explain the high earnings.

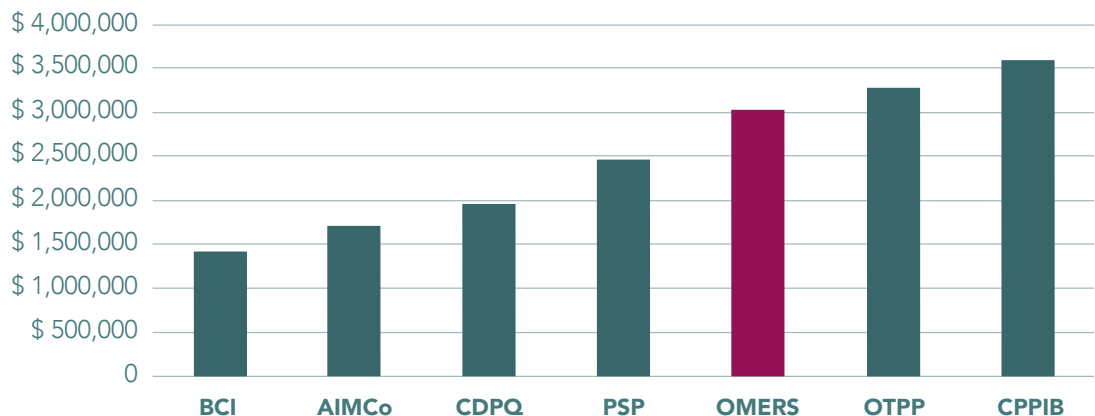
Despite being one of the smaller plans in the group, OMERS pays some of the highest absolute rates for executive compensation.

In terms of assets under management, OMERS is the smallest of the plans compared. Despite its smaller size, OMERS is the third highest in terms of absolute average compensation over the past ten years.

Average Assets Under Management 2011-2020 (\$B)

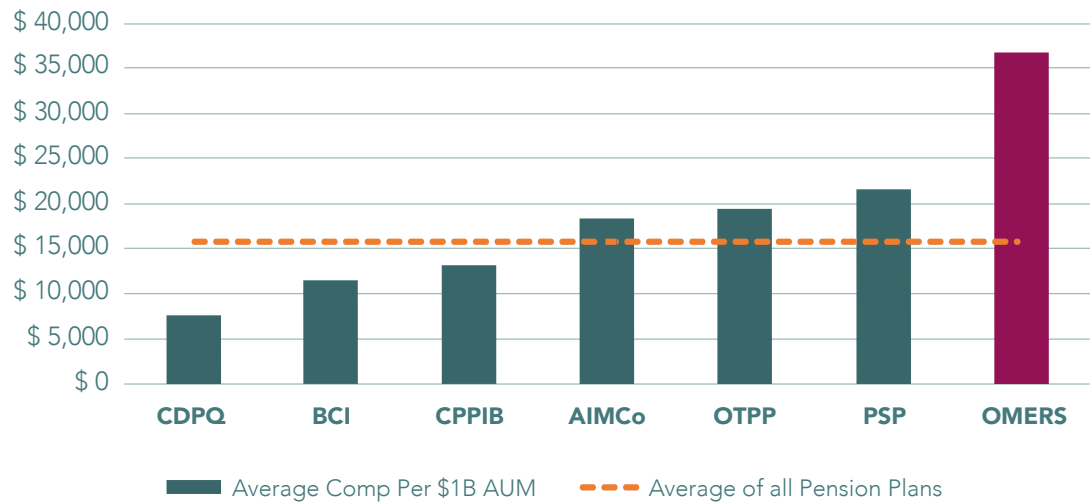


Average Executive Compensation (2011-2020)



If we look at the amount of executive compensation per billion dollars worth of assets under management, OMERS is by far the most expensive as the table below shows.

Average Executive Compensation per \$1B of Assets Under Management (2011-2020)



OMERS paid significantly more in executive compensation for each one billion dollars of assets under management (AUM) than any of the other six pension plans. For each billion dollars of assets under management, OMERS gave their top executives over 70% more in compensation than the next highest cost pension plan (the Public Sector Pension Investment Board - PSP)

Further, if we were to take the average level of compensation per billion dollars of assets under management of all the pension plans combined, OMERS executive compensation was **235%** higher – more than twice the average for all seven plans.

2. OMERS performance does not explain the higher earnings

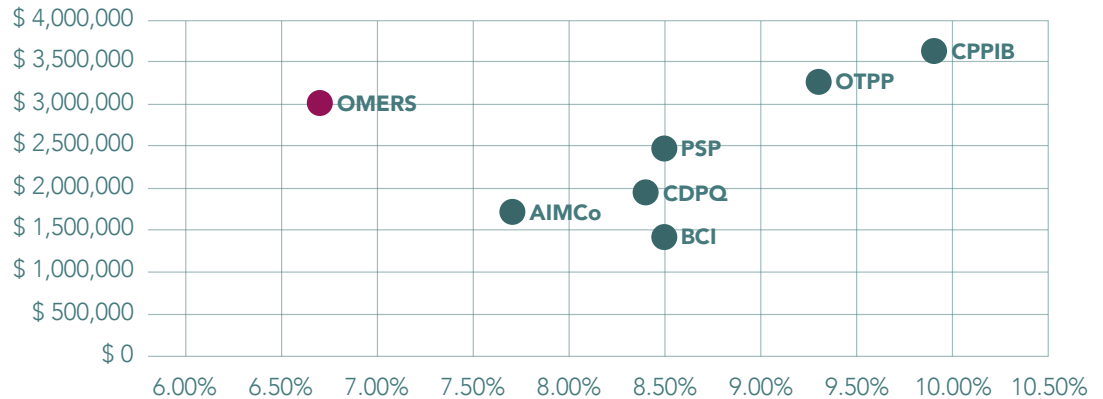
OMERS has argued that compensation for its executives must be competitive with that provided in the market. In their 2017 annual report, OMERS stated that “the compensation programs are designed to attract, engage and retain high-performing people and help ensure they are motivated to pursue OMERS investment goal of earning returns that meet or exceed the Plan’s long term requirements.”³

However, OMERS has underperformed every other pension plan in its peer group over the past ten years⁴. The higher compensation rates paid by OMERS have not translated into higher returns.

³ OMERS 2017 Annual Report, page 89

⁴ Not Just One Tough Year” CUPE Ontario, May 2021

Average Executive Compensation vs 10-Year Annualized Return (2011-2020)



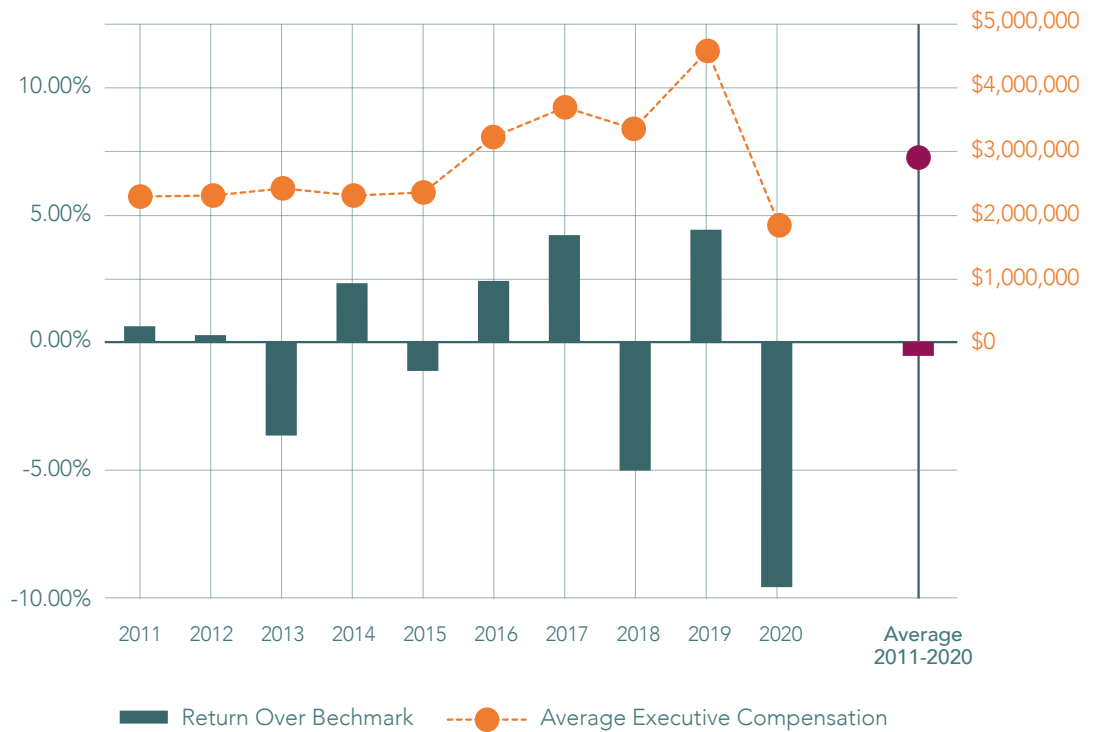
It also begs the question of OMERS performance bonuses. How is it that OMERS executives make so much more for so much less? For every one percent return on investment, OMERS, on average, has paid almost sixty-eight percent more than the average of the other six plans over the ten-year period.

Despite their claim that compensation is based on performance, the data shows that OMERS compensation over the past ten years has increased at a far greater rate than performance.

In 2016, for example, compensation spiked. The combined overall compensation costs for the top five OMERS executives increased from \$12.8 million in 2015 to \$18.1 million the next year. That was a 41% increase in compensation over one year. While income and returns dropped in 2015, they did not drop so low and 2016 returns were not so high as to justify the magnitude of the salary increase. Between 2011 to 2015, total executive compensation did not exceed \$13.4 million in any given year. The 2016 annual report does not provide any explanation for this massive jump in compensation, but a new salary benchmark was apparently set.

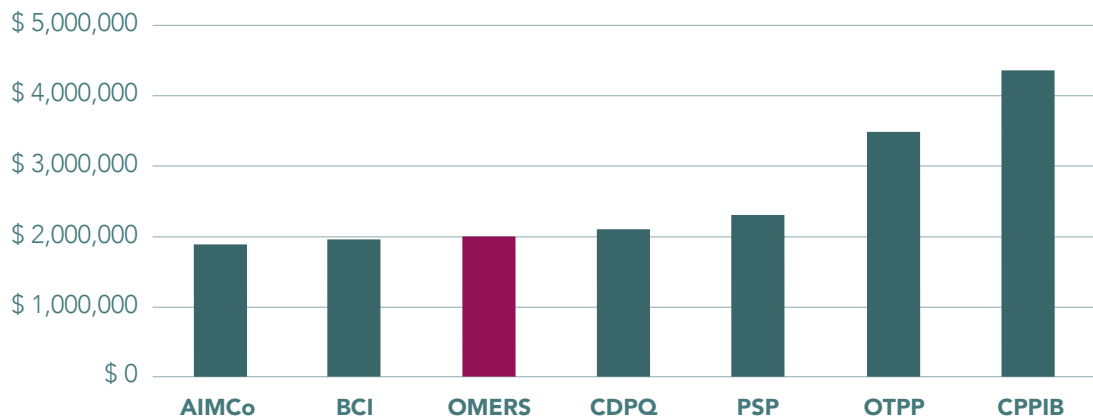
The table below charts the average income increases paid to OMERS top five executives as compared with the amount that OMERS exceeded or failed to reach the plan's established investment benchmarks. Only during the catastrophic 2020 calendar year did the top five OMERS executives see a marked decline in compensation.

OMERS CEO Average Annual Income Correlated with OMERS Investment Performance



Despite the fact that OMERS showed a **net loss** of almost three billion dollars in 2020 and despite the fact that total executive compensation reduced significantly, the compensation for OMERS executives was still in the middle of the pack when compared to their peers, all of which, unlike OMERS, had excellent investment returns in 2020.

Average Executive Compensation 2020



3. Internally Established Performance Benchmarks versus Universal Benchmarks

It is important to note that OMERS investment benchmarks are set differently than in the other plans cited above. OMERS uses “absolute return” pre-set benchmarks for all their asset classes. Although all plans use this method for asset classes such as private equity, infrastructure and real estate, OMERS is the only one to do so for public equity markets. This means that stock market performances as measured by indices like the TSX, S&P or MSCI at the end of the year are not incorporated into OMERS benchmarks or their measure of their executive performance. OMERS is unique in using this method for setting their public markets benchmarks.

Also notable is that OMERS benchmarks are among the lowest of the plans compared here⁵. Although there are other factors at play, meeting these benchmarks would, presumably, be easier than meeting the higher benchmarks set by the other plans. Despite this, OMERS executives failed over ten years to meet even these lower benchmarks.

It is also worth noting that at the same time as we see exorbitant compensation and low investment returns, we also see OMERS is actively pursuing a reduced discount rate. These planned discount rate reductions appear to be unrelated to any change in asset mix but are usually characterized as a “buffer” against future down markets. However, given the interplay between anticipated investment returns and plan liabilities, a reduced discount rate inevitably puts downward pressure on future benefit levels, which is of great concern to CUPE plan members in OMERS.



Conclusions

The high executive compensation at OMERS, especially in light of its documented pattern of investment underperformance as compared to other large defined benefit pension plans and funds is deeply troubling for CUPE plan members. This is especially the case as OMERS has increasingly made governance changes, particularly at its Sponsors Board, that lessen the plan's transparency and accountability to its plan members.

For CUPE Ontario members looking at this and the previous report "Not Just One Tough Year", it appears that over the past decade, OMERS has rewarded its executives' lacklustre investment performance with exceedingly high executive compensation.

The risks in OMERS are not borne by OMERS executives. Risks are borne by the plan members in the form of potentially lower future benefits, and by the employers and active plan members in the form of potentially higher contribution rates. Investment costs and investment performance are part of this equation. It therefore is incumbent on OMERS to clearly explain the reason for such a stark divergence from other plans in terms of performance and executive compensation. This pattern of investment underperformance and excessive compensation cannot continue if the plan is to fulfill its obligations – a strong, defined benefit pension plan that ensures income security in retirement – to its hard working, active plan members serving on the front lines of Ontario's municipalities, school boards and child welfare agencies.

Accordingly, CUPE Ontario reiterates our call for OMERS to cooperate fully with an independent and transparent third-party review of its investment performance and operations.