

Kim Reynolds
GOVERNOR

Adam Gregg
LT. GOVERNOR



Donna M. Mueller
CHIEF EXECUTIVE OFFICER

September 27, 2018

Honorable W. Charles Smithson,
Secretary of the Senate
Honorable Carmine Boal,
Chief Clerk of the House
General Assembly of the State of Iowa
Des Moines, IA 50319

Dear Mr. Smithson and Ms. Boal:

Enclosed is the Iowa Public Employees' Retirement System's report for the fiscal year ended June 30, 2018, on divestment activities related to companies doing business in Iran. This annual report is required by Iowa Code section 12H.5.

The report describes IPERS' implementation of the Iran divestment program and provides information on IPERS divestment activities and costs. The report also includes the list of prohibited companies that was in effect as of June 30, 2018.

Sincerely,

A handwritten signature in black ink that reads "Donna M. Mueller". The signature is written in a cursive style.

Donna M. Mueller
Chief Executive Officer

Enclosure

**IOWA PUBLIC EMPLOYEES' RETIREMENT SYSTEM
ANNUAL REPORT
ON IRAN DIVESTMENT
For the Fiscal Year Ended June 30, 2018**

Iowa Code chapter 12H requires the Iowa Public Employees' Retirement System (IPERS) to scrutinize companies with business operations in Iran, and under certain circumstances, to restrict its purchases of, and/or divest of, holdings of any company determined to have active business operations in Iran. Chapter 12H specifies certain procedures to be followed in engaging companies doing business in Iran, and requires IPERS to annually report to the General Assembly on its activities concerning the Iran divestment law.

Implementation

IPERS develops its list of scrutinized companies using the research and findings of ISS-Ethix (ISS). ISS is a research firm that specializes in researching and monitoring the activities of companies against various types of environmental, social and governance screens. ISS uses the criteria established in Chapter 12H to screen various sources of publicly available information in order to provide IPERS with a list of scrutinized companies. ISS also assists IPERS in evaluating any follow-up responses from scrutinized companies.

IPERS sends a letter to each company believed to have active business operations in Iran and asks them to discontinue their operations in Iran. Companies are given the opportunity to provide evidence that contradicts ISS's findings. The letter also notifies the company that IPERS will prohibit further investment and/or divest of its holdings in the company's securities if the company does not meet the requirements of the law. If the company does not respond, or fails to provide convincing evidence within the time period established by law, then IPERS places the company on its prohibited companies list. The prohibited companies list is updated quarterly, and is provided to the public on IPERS' Web site at www.ipers.org.

IPERS' investment managers are prohibited from purchasing securities issued by companies on the prohibited companies list. Investment managers that have any existing direct holdings¹ of a prohibited company must sell (divest) the position within 18 months of the date the company was first notified. An investment manager has the discretion to decide when to sell its holdings within the 18-month period.

¹ It is important to note that chapter 12H makes a distinction between direct holdings and indirect holdings. *Direct holdings* are securities directly owned and held in IPERS' name. *Indirect holdings* refer to situations where IPERS may indirectly own an interest in a security because of its ownership of shares in a commingled investment vehicle, such as a mutual fund. The General Assembly recognized that it may not be possible to efficiently divest of prohibited companies held in a commingled fund, and exempted indirect holdings from many provisions of chapter 12H. IPERS is required to analyze the prudence of moving its indirect holdings to Iran-free commingled funds if such an option exists. See section on Indirect Holdings.

Chapter 12H requires IPERS to engage only those scrutinized companies in which it has direct holdings. However, IPERS has opted to send letters to all scrutinized companies, and will place a scrutinized company on the prohibited companies list if warranted, regardless of whether or not IPERS has any direct holdings in the company. This is done because IPERS prefers to engage a company and determine whether it is a prohibited company pursuant to the law's criteria before an investment manager purchases any securities of such company. IPERS' investment managers want to know if a company is prohibited before buying it - not afterwards.

Chapter 12H also requires IPERS to contact companies that have inactive business operations in Iran. However, the purpose of such letter is to encourage them to keep their business activities inactive until state-sponsored terrorism stops in Iran. IPERS uses information from ISS to determine which companies may have inactive business operations in the Iran. Currently, no companies have inactive business operations in Iran as defined in Chapter 12H.

Fiscal Year 2018 Engagement Activity

The following chart summarizes the numbers of companies contacted by IPERS in fiscal year 2018 pursuant to chapter 12H.

| Time Period | Number |
|--------------------|---------------|
| Sept. 30, 2017 | 0 |
| Dec. 31, 2017 | 9 |
| Mar. 31, 2018 | 0 |
| June 30, 2018 | 3 |

Letters were sent to twelve companies under scrutiny for active business operations. IPERS received responses from two of these companies. During fiscal year 2018, thirteen companies were added to the prohibited companies list, and ten companies were removed. The companies were removed because IPERS, with the assistance of ISS, concluded that they no longer met the criteria established in Chapter 12H. IPERS' prohibited companies list in effect as of June 30, 2018 is included as Appendix A to this report.

Chapter 12H also requires IPERS to send reminder letters to companies on the prohibited companies list and encourage them to transform their operations to inactive operations. This task was completed in September 2018 for the fifty-five companies on IPERS' prohibited companies list on August 17, 2018.

Fiscal Year 2018 Divestment Activity

IPERS had equity holding in two securities at June 30, 2017. IPERS managers had until April 20, 2018 and January 21, 2018 to sell these securities of Hyundai Mobis and Siemens AG, respectively. Those two securities were sold in the fourth quarter of 2018. A new manager inadvertently purchased 252,000 shares of a prohibited security, China Railway Group Ltd., on July 27, 2017 and August 4, 2017. That position was sold on November 20, 2017 and IPERS was fully compensated for the trading loss of \$17,417.00. Another company, Korea Gas Corporation, went on IPERS' prohibited list for Iran on February 13, 2018. It was already held directly by one manager, who completely sold out of that position in the second quarter of 2018. IPERS ended fiscal year 2018 with no direct holdings of prohibited equity securities.

IPERS had direct fixed income holdings in two securities at June 30, 2017. By the end of the fourth quarter of 2018 those position were gone. One manager inadvertently added to one of those two positions in the third quarter, but sold those securities on November 9, 2018. A small gain of \$4,968.56 was recorded on the transactions. Royal Dutch Shell PLC went on the prohibited list on July 13, 2017. Several of our existing managers held bonds in that company then. At the close of fiscal year 2018, IPERS' only prohibited fixed income holdings were 425,000 par of the Royal Dutch Shell PLC bonds, but all holdings in that company's bonds had been sold by July 31, 2018.

Indirect Holdings

As noted earlier, chapter 12H makes a distinction between direct and indirect holdings. IPERS held twenty-seven indirect holdings in the stock of companies listed on the prohibited companies list on June 30, 2018. They were valued at \$49,432,406.51. IPERS indirectly held no bonds of companies listed on the prohibited companies list at June 30, 2018. In total, IPERS had \$49,432,406.51 worth of indirect holdings as of June 30, 2018, which comprised approximately 0.15% of the total IPERS fund.

While indirect holdings are generally exempt from most of the provisions of the law, IPERS is required by law to evaluate the prudence and potential costs associated with moving its indirect investments to funds that will comply with chapter 12H, if any such vehicles exist. Based on potential trading costs & fees, IPERS does not believe it is prudent to take such action given the relatively small indirect exposures to prohibited companies.

Fiscal Year 2018 Program Costs

IPERS incurred third party costs of \$1,667.00 for research services in fiscal year 2018, and did not incur any staff overtime costs to implement the program.

For More Information

Updates of IPERS' Iran prohibited list and holdings can be found on IPERS' Web site at <https://www.ipers.org/about-us/investments/iran-investment-restrictions> quarterly throughout the year. IPERS staff can be reached by e-mail at investments@ipers.org or by telephone at 515-281-0030.

Exhibit A

Iowa Public Employees' Retirement System's Iran Prohibited Companies List

May 11, 2018

Divestment Date *

| | |
|--|------------------|
| » Aban Offshore Ltd. | |
| » Alstom SA | |
| » Arabian Pipes Co | |
| » Capital Product Partners LP | October 13, 2018 |
| » Chadormalu Mineral & Ind. Co. | |
| » China Camc Engineering Co. Ltd | |
| » China Nonferrous Metal Industry's Foreign Eng. And Const. Co. Ltd. | |
| » China Oilfield Services | |
| » China Petroleum & Chemical Corp | |
| » China Railway Group Ltd | |
| » Chiyoda Corporation | |
| » Daelim Industrial | |
| » Daewoo Engineering & Construction | |
| » Danieli & C - Officine Meccaniche Spa | |
| » DNO ASA | July 18, 2018 |
| » F.L.Smidth & Co. AS | |
| » Gazprom OAO | |
| » Gruppo Waste Italia SpA | |
| » Hyundai Engineering & Construction | |
| » Hyundai Mobis | |
| » Hyundai Motor | |
| » Indian Oil Corporation Ltd. | |
| » Inpex Corporation | |
| » Inter Rao Ues JSC | |
| » Japan Drilling Co., Ltd. | |
| » Japan Petroleum Exploration Co., Ltd. | |
| » Korea Electric Power | |
| » Korea Gas Corporation | May 13, 2019 |
| » Lukoil Oil Co. | |
| » Maire Tecnimont S.p.A. | |
| » Man SE | May 13, 2019 |
| » Marubeni Corporation | |
| » Mitsubishi Materials Corporation | |
| » Motor Sich | |
| » Oil & Natural Gas Corporation Ltd. | |
| » Oil India Ltd | |
| » OMV AG | |
| » Outotec Oyj | May 13, 2019 |
| » PetroChina Co. Ltd. | |
| » PJSC Tatneft | July 18, 2018 |
| » Polskie Gornictwo Naftowe i Gazownictwo SA | |
| » Porsche Automobil Holding SE | May 13, 2019 |
| » Posco | |
| » Posco Daewoo Corp | October 13, 2018 |
| » Power Construction Corporation of China, Ltd. | |
| » Poyry PLC | |
| » Royal Dutch Shell Plc | October 13, 2018 |
| » Shipping Corporation of India Ltd. | |
| » Siemens AG | |
| » Sojitz Corp. | May 13, 2019 |
| » Total S.A. | May 13, 2019 |
| » United Aircraft Corporation | |
| » Volkswagen AG | May 13, 2019 |
| » Zio Podolsk Machinery Plant | |

» Denotes companies with active business operations. There are no companies with inactive business operations. Note: not all of these companies are held by IPERS.

* Denotes deadline for divesting of security.