



EXECUTIVE CHAMBERS  
HONOLULU

NEIL ABERCROMBIE  
GOVERNOR

February 28, 2013

The Honorable Donna Mercado Kim, President  
and Members of the Senate  
Twenty-Seventh State Legislature  
State Capitol, Room 409  
Honolulu, Hawaii 96813

The Honorable Joseph Souki, Speaker  
and Members of the House of Representatives  
Twenty-Seventh State Legislature  
State Capitol, Room 431  
Honolulu, Hawaii 96813

Dear President Mercado Kim, Speaker Souki, and Members of the Legislature:

For your information and consideration, I am transmitting two (2) copies of the **Employees' Retirement System's report on Act 192** regarding its direct holdings in Sudan scrutinized companies. In accordance with Section 93-16, Hawaii Revised Statutes, I am also informing you that the report may be viewed electronically at **<http://budget.hawaii.gov/budget/reports-to-the-legislature/>**.

Sincerely,

/s/

NEIL ABERCROMBIE  
Governor, State of Hawaii

EMPLOYEES' RETIREMENT SYSTEM  
OF THE STATE OF HAWAII  
DIRECT HOLDINGS IN SUDAN SCRUTINIZED COMPANIES  
2012

Act 192, Session Laws of Hawaii 2007, expresses the State's desire to not participate in ownership of companies that provide significant practical support for genocide activities being conducted by the Sudanese government in the Darfur region.

The Board of Trustees of the Employees' Retirement System recognizes the intent of Act 192 and will abide by its requirements. The Board, however, must also apply a decision framework to act for the exclusive benefit of ERS Plan participants. In this respect, the Board recognized that divestment activities could potentially increase the portfolio's idiosyncratic investment risk. Divestment guidelines and procedures, codified in the ERS' *Sudan Investment Policy* ("Policy"), were therefore developed to minimize the impact of the Sudan divestment policy upon the investment results of the ERS portfolio. The Sudan divestment policy is intended to also avoid:

- Discriminating against companies whose Sudan-related business activities are supported by the U.S. government;
- Discriminating against companies whose Sudan-related business activities do not support genocide activities;
- Unnecessarily harming U.S. companies and jobs; and
- Compromising the Board of Trustees' duties to the beneficiaries of the ERS.

The ERS was required to make its best efforts to identify all of its direct holdings in scrutinized companies within 180 days after July 1, 2007. Those efforts were to include:

- Reviewing publicly available information regarding companies with business operations in Sudan provided by nonprofit organizations and other appropriate parties;
- Contacting ERS' asset managers with investments in scrutinized companies; and
- Contacting other institutional investors that have divested from or engaged with companies that have business operations in Sudan.

Each year thereafter, Act 192 requires the ERS to provide to the legislature a publicly-available report that includes activity under section 4, to include: 1) A summary or correspondence with companies engaged by the public fund; 2) All investments sold, redeemed, divested, or withdrawn; 3) All prohibited investments; and, 4) Any progress made. The ERS respectfully reports all pertinent activity in 2012 related to Sudan Scrutinized Companies as outline in Act 192:

I Summary of correspondence with companies engaged by public fund:

The ERS relied on the *Sudan Company Report* prepared by the Conflict Risk Network (CRN) to determine “scrutinized companies,” that certain business activities in Sudan may determine their status as a “highest offender.” Highest offenders are subject to possible divestment in accordance with the Policy.

Before taking any action against the company, the ERS Board considers any additional information they may provide. The ERS will send a letter to the scrutinized company to inform them of their Sudan-related activities, and encourage them to cease their scrutinized active business operations within 90 days. If the company continues to have scrutinized active business operations after ninety days following the first engagement by ERS, the Board will consider divestment or other corrective actions to the extent possible with due consideration from among other things, return on investment, diversification, and the ERS’ other legal obligations. Failure to respond to the ERS letter may lead to divestment action.

Three highest offender security positions (Caterpillar Inc., Reliance Industries Limited, and China Petroleum and Chemical Corporation) were held in the ERS portfolio at some point in 2012. The Caterpillar and Reliance positions were acquired prior to the beginning of 2012 and therefore subject to eventual divestment by Board action; these positions were no longer being held by any investment managers by the end of 2012 in accordance with the divestment period as prescribed by the Policy. The China Petroleum and Chemical Corporation position was traded into the ERS portfolio in error and removed from the portfolio shortly after discovery and notification to the investment manager. Accordingly, the letters sent to any highest offender companies during the 2012 calendar year were to Caterpillar and Reliance.

Caterpillar Inc. (US) (“CAT”) was classified as *scrutinized* company on the CRN report of February 29, 2012. The ERS sent an engagement letter to CAT on March 28, 2012 and on June 4, 2012; there was no response received from CAT. After ERS staff consulted with CRN on September 12, 2012, the Board of Trustees approved a divestment from CAT on October 11, 2012. The ERS investment managers completed divestment of CAT by the end of November 2012.

Reliance Industries Limited (“Reliance”) was classified as *scrutinized* company on the CRN report of February 29, 2012. The ERS sent an engagement letter to Reliance on April 3, 2012 and on June 4, 2012; there was no response received from Reliance. Subsequent to ERS

investment managers being informed of the scrutinized status of Reliance, the positions were sold off at the manager's discretion. The ERS investment managers no longer hold Reliance.

The China Petroleum and Chemical Corporation position was traded into the ERS portfolio in error and removed from the portfolio shortly after discovery and notification to the investment manager. Accordingly, no letters were sent to officials at the firm.

## II All Investment Sold, Redeemed, Divested or Withdrawn

<u>Action</u>	<u>Company Divested</u>	<u>Market Value</u> <sup>1</sup>
Sold: October 24, 2012	China Petroleum and Chemical Corporation <sup>2</sup>	\$2,519,124.65
Sold: November 2, 2012	Caterpillar Inc.	\$1,395,838.40
Sold: November 5, 2012	Caterpillar Inc.	\$1,151,362.46

<sup>1</sup> Market Value in US Dollars at time of divestment

<sup>2</sup> Security was traded into the ERS portfolio in error on July 3, 2012.

## III All Prohibited Investments

Companies held in the 2012 calendar year  
 Caterpillar Inc. (US)  
 Reliance Industries Limited  
 China Petroleum & Chemical Corporation

## IV Any Progress Made

<u>Company</u>	<u>Status</u>
Caterpillar Inc. (US)	Two investment managers holding CAT on the date that the Board voted for divestment. Each was notified of Board divestment action in October 2012. Both managers sold the holdings by early November 2012.
China Petroleum & Chemical Corporation	Reversal of inadvertent purchase of this security on October 24, 2012.

EMPLOYEES' RETIREMENT SYSTEM  
OF THE STATE OF HAWAII  
DIRECT HOLDINGS IN SUDAN SCRUTINIZED COMPANIES  
2011

Act 192, Session Laws of Hawaii 2007, expresses the State's desire to not participate in ownership of companies that provide significant practical support for genocide activities being conducted by the Sudanese government in the Darfur region.

The Board of Trustees of the Employees' Retirement System (ERS) recognizes the intent of Act 192 and will abide by its requirements. The Board of Trustees, however, must also apply a decision framework to act for the exclusive benefit of ERS Plan participants. In this respect, the Board of Trustees recognized that divestment activities could potentially increase the portfolio's idiosyncratic investment risk. Divestment guidelines and procedures, codified in the ERS' *Sudan Investment Policy* ("Policy") were, therefore, developed to minimize the impact of the Sudan divestment policy upon the investment results of the ERS portfolio. The Sudan divestment policy is intended to also avoid:

- Discriminating against companies whose Sudan-related business activities are supported by the U.S. government;
- Discriminating against companies whose Sudan-related business activities do not support genocide activities;
- Unnecessarily harming U.S. companies and jobs; and
- Compromising the Board of Trustees' duties to the beneficiaries of the ERS.

The ERS was required to make its best efforts to identify all of its direct holdings in scrutinized companies within 180 days after July 1, 2007. Those efforts were to include:

- Reviewing publicly available information regarding companies with business operations in Sudan provided by nonprofit organizations and other appropriate parties;
- Contacting ERS' asset managers with investments in scrutinized companies; and
- Contacting other institutional investors that have divested from or engaged with companies that have business operations in Sudan.

Each year, thereafter, Act 192 requires the ERS to provide to the legislature a publicly-available report that includes activity under Section 4, to include: 1) A summary or correspondence with companies engaged by the public fund; 2) All investments sold, redeemed, divested, or withdrawn; 3) All prohibited investments; and, 4) Any progress made. The ERS respectfully reports all pertinent activities in 2011 related to Sudan Scrutinized Companies as outlined in Act 192:

I. Summary of Correspondence With Companies Engaged by Public Fund

The ERS relied on the *Sudan Company Report* prepared by the Conflict Risk Network (formerly known as the Genocide Intervention Network) to determine “scrutinized companies,” whose business activities in Sudan may determine their status as a “highest offender.” Highest offenders are subject to possible divestment in accordance with the Policy.

Before taking any action against the company, the Board of Trustees considers any additional information available. The ERS will send a letter to the scrutinized company to inform them of their Sudan-related activities, and encourage them to cease their scrutinized active business operations within 90 days. If the company continues to have scrutinized active business operations after 90 days following the first engagement by ERS, the Board of Trustees will consider divestment or other corrective actions to the extent possible with due consideration from among other things, return on investment, diversification, and the ERS’ other legal obligations. Failure to respond to the ERS letter may lead to divestment action.

The Conflict Risk Network added PTT Public Company Ltd. (“PPT”) to its scrutinized company list on November 30, 2009. The ERS verified its first exposure to PTT Public Company, Ltd. (“PTT”) stock on May 22, 2009. Engagement letters were sent to PPT on December 2, 2009 and February 2, 2010; however, the company was non-responsive. The Board of Trustees approved to divest this position on June 14, 2010. There were no letters sent to any scrutinized companies during the 2011 calendar year since there were no new company names subject to the Policy.

II. All Investment Sold, Redeemed, Divested or Withdrawn

<u>Action</u>	<u>Company Divested</u>	<u>Market Value</u> <sup>1</sup>
Sold: March 31, 2011	PTT Public Company Ltd.	\$2,949,924.54

<sup>1</sup> Market Value in US Dollars at time of divestment

III. All Prohibited Investments

Companies held in the 2011 calendar year  
PTT Public Company, Ltd.

IV. Any Progress Made

There were no “scrutinized companies” held in the ERS investment portfolio as of December 31, 2011; therefore, there is nothing to report with respect to this section.