Accuity LLP
CERTIFIED PUBLIC ACCOUNTANTS

Kamehameha Schools and Subsidiaries

Consolidated Financial Statements and Supplementary Schedules

June 30, 2017 and 2016

Kamehameha Schools and Subsidiaries
Index
June 30, 2017 and 2016

Accuity LLP
CERTIFIED PUBLIC ACCOUNTANTS

Report of Independent Auditors

To the Audit Committee
Kamehameha Schools and Subsidiaries

Report on the Consolidated Financial Statements
We have audited the accompanying consolidated financial statements of Kamehameha Schools and Subsidiaries (the "Organization"), which comprise the consolidated balance sheets as of June 30, 2017 and 2016, and the related consolidated statements of activities and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements
Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility
Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Organization as of June 30, 2017 and 2016, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

an independent member of
BAKER TILLY
INTERNATIONAL

999 Bishop Street, Suite 1900
Honolulu, Hawaii 96813
Telephone: 808 531 3400 Facsimile: 808 531 3433

Report on Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The supplementary information included in Schedules 1 and 2 is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information for the years ended June 30, 2017, 2016, 2015, 2014 and 2013 is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Accuity LLP

Honolulu, Hawaii
September 28, 2017

Kamehameha Schools and Subsidiaries
Consolidated Balance Sheets
June 30, 2017 and 2016
(All dollars in thousands)

	2017	2016
Assets		
Current assets		
Cash and cash equivalents	$ 56,937	$ 124,293
Short-term investments	29,997	-
Receivables, net	7,664	6,225
Other	2,393	2,680
Total current assets	96,991	133,198
Trust investments		
Financial investments, net	7,966,142	7,317,987
Interest receivables	7,189	7,022
Real estate investments, net	255,832	248,779
	8,229,163	7,573,788
Other investments	39,471	37,482
Property and equipment, net	663,392	682,061
Accrued pension asset	552	-
Deferred charges and other	120,717	117,125
Total assets	$ 9,150,286	$ 8,543,654
Liabilities and Net Assets		
Current liabilities		
Accounts payable and accrued expenses	$ 48,628	$ 42,245
Current portion of notes payable	14,786	9,786
Deferred income and other	27,779	26,231
Total current liabilities	91,193	78,262
Notes payable	244,905	159,690
Accrued postretirement benefits	68,420	65,107
Accrued pension liability	-	134,170
Deferred income and other	182,203	187,689
Total liabilities	586,721	624,918
Commitments and contingencies		
Net assets – unrestricted	8,563,565	7,918,736
Total liabilities and net assets	$ 9,150,286	$ 8,543,654

The accompanying notes are an integral part of the consolidated financial statements.

Kamehameha Schools and Subsidiaries
Consolidated Statements of Activities
Years Ended June 30, 2017 and 2016
(All dollars in thousands)

	2017	2016
Revenues, gains (losses), and other support		
Tuition and fees	$ 38,169	$ 36,725
Less: Financial aid	(27,802)	(26,324)
Net tuition and fees	10,367	10,401
Investment gains (losses), net	883,272	(185,917)
Rental	228,490	209,178
Net gains on property sales	25,578	34,089
Other	6,326	3,966
Total revenues, gains (losses) and other support	1,154,033	71,717
Expenses		
Educational programs	302,239	285,424
Management and general		
Rental	117,290	109,308
Other	121,053	106,182
Total expenses	540,582	500,914
Change in net assets before retirement plan related changes other than net periodic cost	613,451	(429,197)
Retirement plan related changes other than net periodic cost	31,378	(71,051)
Change in net assets	644,829	(500,248)
Net assets		
Beginning of year	7,918,736	8,418,984
End of year	$ 8,563,565	$ 7,918,736

The accompanying notes are an integral part of the consolidated financial statements.

Kamehameha Schools and Subsidiaries
Consolidated Statements of Cash Flows
Years Ended June 30, 2017 and 2016
(All dollars in thousands)

	2017	2016
Cash flows from operating activities		
Change in net assets	$ 644,829	$ (500,248)
Adjustments to reconcile change in net assets to net cash used in operating activities		
Depreciation and amortization	56,405	52,665
Net realized and unrealized (gains) losses on investments	(815,357)	245,610
Net gains on property transactions	(25,578)	(34,089)
Retirement plan related changes other than net periodic cost	(31,378)	71,051
Contribution to pension plan	(103,396)	-
Changes in operating assets and liabilities		
Receivables, net	(1,439)	393
Deferred charges and other	(5,013)	(4,289)
Accounts payable, accrued expenses and other liabilities	5,812	(1,606)
Net cash used in operating activities	(275,115)	(170,513)
Cash flows from investing activities		
Proceeds from sales of investments	3,396,302	4,535,588
Purchases of investments	(3,261,252)	(4,205,738)
Proceeds from real estate transactions	25,608	34,294
Purchases of real estate	(20,847)	(49,210)
Proceeds from sales of property and equipment	9	4
Purchases of property and equipment	(22,275)	(28,375)
Net cash provided by investing activities	117,545	286,563
Cash flows from financing activities		
Proceeds from borrowings	125,000	-
Repayment of borrowings	(34,786)	(24,286)
Net cash provided by (used in) financing activities	90,214	(24,286)
Net increase (decrease) in cash and cash equivalents	(67,356)	91,764
Cash and cash equivalents		
Beginning of year	124,293	32,529
End of year	$ 56,937	$ 124,293
Supplemental disclosure of cash flow information		
Income taxes paid (received)	$ (53)	$ 1,362
Interest paid	6,649	7,109

The accompanying notes are an integral part of the consolidated financial statements.

1. Summary of Significant Accounting Policies

Description of the Organization

Kamehameha Schools (the "Schools") is a charitable trust established under Hawaii law and operates under the terms of the Will of Bernice Pauahi Bishop, deceased. The Schools are governed by a Board of Trustees (the "Trustees") and subject to the jurisdiction of the First Circuit Court of the State of Hawaii (the "Court"). The primary assets of the Schools are lands and properties located in the State of Hawaii (the "State") and debt and equity investments.

The Schools provide a variety of educational services, including early education, campus-based programs, and other extension, enrichment and summer school programs. Early education programs are conducted in various facilities throughout the State. The campus-based programs include campuses on the islands of Oahu, Maui and Hawaii which serve students from kindergarten through grade 12. The Schools are also engaged in summer programs, educational partnerships and other outreach programs. In addition, the Schools provide a significant amount of scholarships for post-secondary education.

Principles of Consolidation

The consolidated financial statements of Kamehameha Schools and Subsidiaries (the "Organization") include the accounts of the Schools, Bishop Holdings Corporation and its Subsidiaries ("BHC"), Ke Ali'i Pauahi Foundation ("KAPF"), P&C Insurance Company, LLC ("P&C"), Kaloko'eli Properties LLC ("KPL"), and Bishop Financial Limited.

The consolidated financial statements of BHC include the accounts of:

- Pauahi Management Corporation and its wholly-owned subsidiaries – KBH, Inc. and Lake Manassas Limited Liability Company.
- Kamehameha Investment Corporation ("KIC") and its wholly-owned subsidiary, Keauhou Community Services, Inc.

BHC is a taxable holding corporation with subsidiaries primarily involved in property investment.

KAPF is a charitable organization whose exclusive purpose is to actively engage in fundraising, scholarship and development activities for the Schools.

P&C provides property and liability coverage for the Schools and its affiliates.

KPL is a wholly-owned limited liability company whose exclusive purpose is to engage in the planning, designing, financing and construction of low-cost housing for sale or rental.

In addition, under accounting principles generally accepted in the United States of America ("GAAP"), certain investments may be considered as entities for consolidation should they meet specified criteria. Bishop Financial Limited met these criteria as it has a specific purpose and is managed by an independent investment management firm.

All significant intercompany transactions and accounts have been eliminated in consolidation.

Basis of Financial Statement Presentation
The Organization's consolidated financial statements have been prepared on the accrual basis of accounting, and are presented in conformity with GAAP. Net assets, revenues, gains and other support, and expenses are classified based on the existence or absence of donor-imposed restrictions. KAPF's combined temporarily and permanently restricted net assets amounted to approximately $20.3 million and $17.8 million at June 30, 2017 and 2016, respectively. The Schools have no board or donor designated funds. As the restricted net assets of KAPF are not significant, all net assets of the Organization and changes therein are classified and reported as unrestricted net assets.

Use of Estimates
The preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates.

Concentrations of Risk
Financial instruments that potentially subject the Organization to significant concentrations of credit risk consist principally of cash and cash equivalents and investments. While the majority of cash and cash equivalent accounts exceed available depository insurance limits, management does not anticipate non-performance by their financial institutions and regularly reviews the viability of these institutions. The Organization also attempts to limit its risk in investments by maintaining a diversified investment portfolio. In addition to credit risk, trust and other investments are exposed to interest rate, market and geographic risk.

Fair Value Measurements
For financial and nonfinancial assets and liabilities reported at fair value, the Organization defines fair value as the price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market in an orderly transaction between market participants. The Organization measures fair value using assumptions developed based on market data obtained from independent external sources and the reporting entity's own assumption. The hierarchy is broken down into levels based on the reliability of the inputs as follows:

- **Level 1** – Valuations based on quoted prices in active markets for identical assets or liabilities that the Organization has the ability to access. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these products does not entail a significant degree of judgment.

- **Level 2** – Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, directly or indirectly.

- **Level 3** – Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

Further, fair value measurements should consider adjustments for risk, such as the risk inherent in a valuation technique or its inputs.

Fair value estimates are made at a specific point in time based on relevant market information about the financial instruments. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore, cannot be determined with precision. Changes in assumptions could significantly affect these estimates. Transfers between levels are recognized on the actual date of the event or change in circumstances that caused the transfer.

Cash and Cash Equivalents
Cash and cash equivalents include unrestricted demand deposits and all highly liquid deposits with an original maturity of three months or less. Cash and cash equivalents are held in financial institutions located in the State and other states. Cash balances are maintained in excess of depository institution insurance limits. The carrying amounts of cash equivalents approximate fair value because of the short maturity of these instruments.

Short-Term Investments
Short-term investments include liquid fixed income securities with maturities greater than three months and less than one year. The carrying amounts approximate fair value because of the short maturity of these investments.

Investments
The noncurrent section titled Trust Investments represents financial, real estate and interest receivables subject to the Organization’s investment policies described below. Other investments represent investments held at the Organization’s various subsidiaries and deferred compensation plan investments that are not subject to the same investment policies. Property, plant and equipment represents assets used for educational and administrative purposes, as well as assets related to the Organization’s agricultural and conservation land.

The Organization is subject to a spending policy that was approved by Court Order dated March 13, 2000. The investment policies seek to meet or exceed an investment objective of an annualized real return of 5.0% (CPI + 5 percentage points), net of fees and direct expenses, over most rolling ten-year periods, as well as over longer periods. In meeting this objective, the Organization allocates assets in a prudent manner, balancing risks and potential rewards while maintaining adequate levels of liquidity.

The Organization’s long-term educational spending rate of 4% is meant to provide a net real total return to the investment balance of 1% on a long-term basis.

All investments, investment settlements and interest receivables are classified as noncurrent assets in the consolidated balance sheets regardless of maturity or liquidity. In any given year, investments may need to be liquidated to support annual educational spending, but on a long-term basis, the Organization’s investment and spending objectives are designed to support the educational programs in perpetuity. Refer to Schedules of Trust Spending and Schedule of Total Return for the relevant policies and historical information of the Organization.

Investments in debt and equity securities with readily determinable market values are measured at fair value based on quoted market prices. Investments in real estate are reported at the lower of cost or fair value. Investments also include limited partnerships, hedge funds, commingled funds and other investments that do not have a readily determinable fair value. These investments utilize a wide range of investment strategies and are reported at fair value based on the most current information provided by external investment managers and other industry standard methodologies.

The carrying value of interest receivables approximates fair value because of the short maturity of these instruments.

Unrealized gains and losses for marketable debt and equity securities and other investments are included in the consolidated statements of activities. Management fees vary depending on investment structure, and as such, are presented net of investment gains and losses.

The Organization may use derivative instruments for risk hedging and value-added strategies. Derivative financial instruments primarily include currency forward contracts and financial futures and are recorded at fair value with the resulting gain or loss included in the consolidated statements of activities.

Receivables
The carrying value of tenant and other receivables approximates fair value because of the short maturity of these instruments.

Property and Equipment
Property and equipment are carried at cost, less accumulated depreciation and amortization. The Organization provides for depreciation and amortization on property and equipment using the straight-line method over the estimated useful lives of the assets as follows:

	Years
Land improvements	30
Buildings and improvements	30
Equipment	5 to 10

The Organization reviews its long-lived assets, such as property and equipment, for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. An impairment loss exists for an asset held for use when the cash flows expected to be generated by an asset are less than the carrying amount. Measurement of the impairment loss is based on the fair value of the asset. No impairment losses were recorded for the years ended June 30, 2017 or 2016.

Revenue Recognition
Tuition and fees revenue is recognized in the period for which the education programs or student related services were provided. Financial aid that covers a portion of tuition and other costs are reflected as a reduction of tuition and fees.

Profits on sales of real estate are recognized in full when title has passed, minimum down payment criterion is met, the terms of any note received are such as to satisfy continuing investment requirements and collectability of the note is reasonably assured, the risks and rewards of ownership have been transferred to the buyer, and there is no substantial continuing involvement with the property. If any of the aforementioned criteria are not met, the profit is deferred and recognized under either the installment, cost recovery, deposit or percentage-of-completion methods and are recorded to “Deferred income and other” on the consolidated balance sheets.

Lease rental income is recognized on a straight-line basis over the fixed term of the respective leases. The deferred rent revenue is included in “Deferred income and other” on the consolidated balance sheets. Differences between revenue recognized and amounts due under respective lease agreements are recorded as increases or decreases, as applicable, to deferred rent receivable included in “Deferred charges and other” on the consolidated balance sheets.

The Organization recognizes non-real estate revenue in the period in which services are rendered.

The Schools present taxes collected from customers and remitted to government agencies on a gross basis in its consolidated statements of activities. For the years ended June 30, 2017 and 2016, the Schools collected and remitted $46.7 million and $46.1 million in taxes, respectively.

Income Taxes
In a ruling dated February 9, 1939, and reaffirmed in 1969, 1986 and 2000, the Internal Revenue Service ("IRS") determined that the Schools are exempt from federal income taxes under Internal Revenue Code ("IRC") Section 501(c)(3) as they are organized and operated for educational purposes within the meaning of IRC Section 170(b)(1)(A)(ii). KAPF is also exempt from federal income taxes under IRC Section 501(c)(3) and qualifies as a supporting organization as described in IRC Section 509(a)(3). To the extent that the Schools and KAPF receive unrelated business income, such earnings are subject to unrelated business income tax.

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, operating losses and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The amount recognized for deferred tax assets is reduced, if necessary, to the amount more likely than not to be realized. Income taxes are calculated by each subsidiary as if it filed separate income tax returns.

P&C is exempt from Hawaii income taxes, however is subject to tax on direct written premiums. For federal income tax purposes, P&C is treated as a disregarded entity.

KPL is exempt from Hawaii income taxes. For federal income tax purposes, KPL is treated as a disregarded entity.

The Organization evaluates uncertain tax positions utilizing a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. At June 30, 2017 and 2016, management believes there were no significant uncertain tax positions.

Pension and Postretirement Obligations
The Organization records the difference between the benefit obligation and fair value of plan assets on the consolidated balance sheets. In addition, the Organization recognizes, as part of unrestricted net assets, the gains and losses due to differences between actuarial assumptions and actual experience and any effects on prior service due to plan amendments that arise during the period which are not yet recognized as net periodic benefit costs.

Fair Value of Financial Investments and Pension Plan Assets
The fair value of the Organization's financial investments and pension plan assets was determined as follows:

- **Common and preferred stocks, short-term investments and cash equivalents, and mutual funds** – The fair value of these investments is estimated using quoted or observable prices in an active market or exchange and is generally categorized in Level 1 or Level 2.

- **U.S. government obligations** – The fair value of these investments is generally based on quoted prices in active markets and is generally categorized in Level 1.

- **International government bonds, corporate debt securities, and other debt securities** – The fair value of these investments is estimated using a market approach with both observable prices in an active market and unobservable inputs such as extrapolated data and proprietary pricing models and is generally categorized in Level 2.

- **Commingled funds, hedge funds, private equity funds, collective investment funds and loans** – These investments are generally reported at fair value using a market approach based on information provided by the respective external investment managers at the most recent valuation date and adjusted for cash flows from the valuation date to fiscal year end, if applicable. Because these investments are not readily marketable, their estimated value is subject to uncertainty and therefore may differ from the value that would have been used had a ready market for such investment existed. For investments in investment companies, the Organization estimates the fair value of an investment using the net asset value of the investment without further adjustment unless the Organization determines that the net asset value is deemed to be not reflective of fair value. These funds are generally categorized in Level 3.

The Organization's investment policy guides its asset allocation, which allows for the use of derivatives and other strategies which are achieved, in part, through limited partnership and commingled funds. When executed through a limited partnership, these investments pose no off-balance sheet risk to the Organization due to the limited liability structure of the investments.

Commitments and Contingencies
Liabilities for loss contingencies, including environmental remediation costs, arising from claims, assessments, litigation, fines and penalties, and other sources, are recorded when it is probable that a liability has been incurred and the amount of the assessment and/or remediation can be reasonably estimated.

Reclassification
Certain amounts in the 2016 consolidated financial statements have been reclassified to conform to the 2017 presentation. Such reclassifications have no impact on the 2016 change in net assets as previously reported.

Subsequent Events
The Organization has reviewed all events that have occurred from July 1, 2017 through September 28, 2017, the date that the consolidated financial statements were available for issuance, for proper accounting and disclosure in the consolidated financial statements.

2. Financial Investments

The Organization's financial investments reported at fair value on a recurring basis have been categorized based on the fair value hierarchy in Note 1 at June 30, 2017 and 2016 as follows (in thousands):

	2017	2016
Trust financial investments, net	$ 7,966,142	$ 7,317,987
Amounts receivable for securities sold	(191,523)	(107,221)
Amounts payable for securities purchased	10,809	17,118
Trust financial investments	7,785,428	7,227,884
Other investments	39,471	37,482
Total investments	$ 7,824,899	$ 7,265,366

	Level 1	Level 2	Level 3	Total
2017				
Common and preferred stocks	$ 374,290	$ -	$ -	$ 374,290
Fixed income				
U.S. government obligations	408,454	-	-	408,454
International government bonds	-	189,998	-	189,998
Other debt securities	-	331,726	-	331,726
Short-term investments and cash equivalents	124,199	62,746	-	186,945
Mutual funds	55,470	-	-	55,470
Hedge funds	-	-	3,091,850	3,091,850
Private equity funds	-	-	2,263,267	2,263,267
Commingled funds	-	-	813,602	813,602
Loans	-	-	109,297	109,297
Total investments	$ 962,413	$ 584,470	$ 6,278,016	$ 7,824,899
2016				
Common and preferred stocks	$ 498,012	$ -	$ -	$ 498,012
Fixed income				
U.S. government obligations	328,474	-	-	328,474
International government bonds	-	177,152	-	177,152
Other debt securities	-	286,237	-	286,237
Short-term investments and cash equivalents	7,248	6,218	-	13,466
Mutual funds	112,520	-	-	112,520
Hedge funds	-	-	3,143,708	3,143,708
Private equity funds	-	-	1,905,712	1,905,712
Commingled funds	-	-	658,974	658,974
Loans	-	-	141,111	141,111
Total investments	$ 946,254	$ 469,607	$ 5,849,505	$ 7,265,366

Net realized and unrealized gains/(losses) on Level 3 investments were included in the consolidated statements of activities. Changes in Level 3 investments measured at fair value on a recurring basis for the years ended June 30, 2017 and 2016 were as follows (in thousands):

	Hedge Funds	Private Equity Funds	Commingled Funds	Loans	Total
As of July 1, 2015	$ 3,790,016	$ 1,618,660	$ 667,322	$ 151,685	$ 6,227,683
Net realized and unrealized gains/(losses) on investments	(170,813)	31,080	(29,624)	70	(169,287)
Purchases	313,358	535,979	172,830	45,857	1,068,024
Sales	(788,853)	(280,007)	(151,554)	(56,501)	(1,276,915)
As of June 30, 2016	3,143,708	1,905,712	658,974	141,111	5,849,505
Net realized and unrealized gains on investments	389,709	222,106	156,252	923	768,990
Purchases	305,665	469,902	153,728	41,133	970,428
Sales	(747,232)	(334,453)	(155,352)	(73,870)	(1,310,907)
As of June 30, 2017	$ 3,091,850	$ 2,263,267	$ 813,602	$ 109,297	$ 6,278,016
Change in unrealized gains/(losses) relating to investments held at June 30, 2016	$ 72,718	$ (68,918)	$ (9,619)	$ 972	$ (4,847)
Change in unrealized gains relating to investments held at June 30, 2017	$ 421,927	$ 81,074	$ 154,570	$ 1,151	$ 658,722

The Organization's investments may be subject to restrictions that (i) limit the Organization's ability to redeem/withdraw capital from such investments during a specified period of time subsequent to the Organization's investment of capital in such investments and/or (ii) the amount of capital that investors in such investments, including the Organization, may redeem/withdraw as of a given redemption/withdrawal date. Capital available for redemption/withdrawal may also be subject to redemption/withdrawal charges and may or may not include capital attributable to the Organization's participation in illiquid investments and/or designated investments held by investments from which the Organization makes redemptions/withdrawals. These investments generally limit redemptions to monthly, quarterly, semi-annually, annually or longer, at fair value, and require between 30 and 90 days' prior written notice.

Investments in private equity and venture capital funds are generally nonredeemable and distributions, which are generally at the discretion of fund managers/general partners, are expected to be received through the liquidation of the underlying investments of the fund throughout the fund's life.

The Organization's loan investments typically range in duration from three to eight years.

Investment gains (losses) for the years ended June 30, 2017 and 2016 were as follows (in thousands):

	2017	2016
Interest and dividend income	$ 67,915	$ 59,693
Realized and unrealized gains (losses)	815,357	(245,610)
Investment gains (losses), net of investment fees	$ 883,272	$ (185,917)

3. Derivatives

The Organization utilizes a variety of derivative instruments as part of the overall investment strategy, including certain forward currency contracts and futures contracts. As described in Note 7, the Organization also utilizes interest rate swap agreements to manage interest rate risk associated with its variable debt facilities. Derivative instruments by their nature bear, to varying degrees, elements of market risk and credit risk that are not reflected in the amounts recorded in the consolidated financial statements. Market risk represents the potential for changes in the value of derivative instruments due to levels of volatility and liquidity or other events affecting the underlying asset, reference rate or index, including those embodied in interest and foreign exchange rate movements and fluctuations in commodity or security prices. Credit risk is the possibility that a loss may occur due to the failure of a counterparty to perform according to the terms of a contract. The Organization's risk of loss in the event of counterparty default is limited to the amounts recognized in the consolidated balance sheets, not the notional amounts of the instruments.

The Organization's forward currency contracts are traded Over-the-Counter ("OTC") and are primarily utilized to mitigate the impact of exchange rate fluctuations on the U.S. dollar value of international investment holdings. A forward currency contract is an agreement between two parties to buy and sell a currency at a set price on a future date. The value of a forward currency contract fluctuates with changes in forward currency exchange rates. Forward currency contracts are marked-to-market daily and the change in value is recorded by the Organization as an unrealized gain or loss. Realized gains or losses equal to the difference between the value of the contract at the time it was opened and the value at the time it was closed are recorded upon delivery or receipt of the currency or, if a forward currency contract is offset by entering into another forward currency contract with the same broker, upon settlement of the net gain or loss.

The Organization's futures contracts are traded on centralized exchanges and are used to manage market exposures and to implement certain investment strategies in a more effective and efficient manner than would be expected by other alternatives such as the purchase or sale of the underlying market securities. Upon entering into a futures contract, the Organization is required to deposit with its broker an amount of cash or liquid securities in accordance with the initial margin requirements of the broker or exchange. Gains and losses are realized when the contracts expire or are closed. Futures contracts are marked-to-market daily based on settlement prices established by the board of trade or exchange on which they are traded, and an appropriate payable or receivable for the change in value is recorded by the Organization.

The following table presents amounts for investment-related derivatives, including the exposure amount, the fair values at June 30, 2017 and 2016, and gains and losses for the years ended June 30, 2017 and 2016 (in thousands):

	Exposure Amounts	Derivative Assets	Derivative Liabilities	Net Gain / (Loss)
2017				
Forward currency contracts	$ 252	$ 2,041	$ (1,789)	$ 8,487
Futures contracts	(66,416)	902	-	(3,647)
		$ 2,943	$ (1,789)	$ 4,840
2016				
Forward currency contracts	$ (3,108)	$ 1,670	$ (4,778)	$ (11,169)
Futures contracts	(12,683)	-	(251)	(12,683)
		$ 1,670	$ (5,029)	$ (23,852)

4. Real Estate Investments

The Organization's real estate investments primarily consist of commercial, residential and agricultural properties located in the State of Hawaii. At June 30, 2017 and 2016, the cost of real estate investments was as follows (in thousands):

	2017	2016
Land	$ 63,273	$ 58,681
Buildings and improvements	347,045	309,389
Less: Accumulated depreciation	(176,233)	(166,447)
	234,085	201,623
Construction in progress	12,243	39,156
Investments in joint venture	9,504	8,000
Real estate, total at carrying value	$ 255,832	$ 248,779

The Organization entered into a joint venture under the equity method during 2016 and is included in real estate investments, net in the accompanying consolidated balance sheets.

Refer to the Notes to Schedule of Total Return for methods and assumptions used to estimate fair value.

5. Property and Equipment

Property and equipment, net, at June 30, 2017 and 2016 consisted of the following (in thousands):

	2017	2016
Educational property and equipment		
Land	$ 17,977	$ 16,201
Buildings, improvements and equipment	949,341	935,352
Less: Accumulated depreciation	(431,944)	(401,143)
	535,374	550,410
Non-educational property and equipment		
Land and land improvements	36,821	36,821
Buildings, improvements and equipment	150,211	144,730
Less: Accumulated depreciation and amortization	(80,052)	(71,327)
	106,980	110,224
Construction in progress	21,038	21,427
Property and equipment, net	$ 663,392	$ 682,061

Non-educational property and equipment are primarily comprised of assets related to conservation and agriculture lands as well as assets used for general administration.

6. Receivables

Receivables, net, at June 30, 2017 and 2016 were as follows (in thousands):

	2017	2016
Tenant and tuition	$ 5,814	$ 7,800
Trade	1,512	1,192
Other	3,473	3,626
	10,799	12,618
Less: Allowance for doubtful accounts	(3,135)	(6,393)
Receivables, net	$ 7,664	$ 6,225

7. Notes Payable

At June 30, 2017 and 2016, unsecured notes payable consisted of the following (in thousands except percentages):

	2017	2016
Senior promissory notes payable under a $250.0 million private shelf facility		
3.47%, payable through March 2042	$ 125,000	$ -
Senior promissory notes payable under a $450.0 million private shelf facility		
6.80%, payable through March 2027	9,524	10,476
4.88%, payable through June 2028	36,667	40,000
4.93%, payable through April 2029	26,000	29,000
3.85%, payable through January 2037	50,000	50,000
Term loan, variable		
2.00% and 1.41% at June 30, 2017 and 2016, respectively, payable through March 2022	12,500	15,000
1.37% at June 30, 2016	-	25,000
Total notes payable	259,691	169,476
Less: Current portion	(14,786)	(9,786)
Long-term notes payable	$ 244,905	$ 159,690

The fair value of notes payable is estimated using the current rates at which similar loans would be made by lenders to borrowers with similar credit ratings and similar remaining maturities. The fair value of the Schools' notes payable was $267.8 million and $178.0 million as of June 30, 2017 and 2016, respectively.

In March 2017, the Schools entered into a $250.0 million private shelf facility. Notes may be issued under this facility through March 2020, at interest rates determined at the time of issuance.

In November 2012, the Schools entered into a $450.0 million private shelf facility. Notes may be issued under this facility through November 2017, at interest rates determined at the time of issuance.

In March 2012, the Schools entered into a $25.0 million, 10-year term loan with variable interest rates. The Schools entered into an interest rate swap agreement to pay a fixed interest rate of 2.48% with the same financial institution. The swap may be settled monthly. The interest rate swap's fair value is measured using Level 2 inputs. The fair value estimates were determined by the financial institution, based on an income approach that considers quoted prices for economically equivalent swaps, projected yield curves and volatility risks that may require significant estimates and judgments. The fair value of the interest rate swap was $0.04 million and $(0.34) million as of June 30, 2017 and 2016, respectively, and was included in deferred charges and other assets. The change in fair value of the interest rate swap was included in other income.

The Schools have a revolving credit facility with two commercial banks that expire in 2020. The revolving credit facility provides for a commitment of $65.0 million. Amounts drawn under the facility bear interest based on the bank's prime interest rate or London Interbank Offered Rate ("LIBOR") plus a spread. At June 30, 2017 and 2016, there were no outstanding balances.

All note and credit agreements contain certain restrictions and require the maintenance of a minimum endowment value and liquidity ratio.

Annual maturities of notes payable are as follows (in thousands):

Year ending June 30,	
2018	$ 14,786
2019	14,786
2020	14,786
2021	14,786
2022	13,786
Thereafter	186,761
	$ 259,691

Interest expense incurred was $7.9 million and $7.0 million for the years ended June 30, 2017 and 2016, respectively.

8. Income Taxes

Total income tax expense (benefit) amounted to approximately $1.6 million and $(1.8) million for the years ended June 30, 2017 and 2016, respectively. These amounts are included in other management and general expenses in the accompanying consolidated statements of activities.

The components of deferred tax assets and liabilities as of June 30, 2017 and 2016 were as follows (in thousands):

	2017	2016
Deferred tax assets		
Charitable contribution carryforwards	$ 55,142	$ 53,400
Net operating loss carryforwards	28,775	29,908
Passive activity loss carryforwards	38,666	29,786
Difference in basis of investments and real estate	4,799	4,874
Other	4,826	4,405
	132,208	122,373
Less: Valuation allowance	(132,208)	(121,019)
Net deferred taxes	$ -	$ 1,354

The change in valuation allowance was an increase of $11.2 million and a decrease of $0.3 million for the years ended June 30, 2017 and 2016, respectively.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portions or all of the deferred tax assets will be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods which the deferred tax assets are deductible, management believes it is more likely than not that it will not realize these deductible differences and has provided a valuation allowance of $132.2 million and $121.0 million for the years ended June 30, 2017 and 2016, respectively. The amount of deferred tax assets considered realizable, however, could be increased in the near term if estimates of future taxable income during the carryforward period are increased. The Organization has passive activity losses of $85.9 million available to carryforward indefinitely for federal and state tax purposes, charitable contribution carryforwards of $122.8 million and $121.4 million for federal and state tax purposes, respectively, expiring at various dates beginning in fiscal year 2017 through 2022, and net operating loss carryforwards of $73.8 million expiring at various dates beginning in fiscal year 2026 through 2037.

As of June 30, 2017 and 2016, there were no significant pending federal or state income tax audits. The federal statute of limitations remains open for the Organization for the years ended June 30, 2014 through 2017. State statute of limitations for various states remains open for the years ended June 30, 2009 through 2017.

9. Pension and Other Postretirement Benefits

The Organization has a defined benefit pension plan (the “Pension Plan”) which covers substantially all employees after satisfying age and length of service requirements. The Pension Plan was frozen as of June 30, 2014.

In addition to the Organization’s Pension Plan, the Schools sponsor a defined benefit health care plan that provides postretirement medical benefits to eligible full-time employees who meet minimum age and service requirements.

The following table reconciles the changes to the benefit obligations and plan assets for the years ended June 30, 2017 and 2016 to the funded status of the plans and amounts recognized in the consolidated financial statements as of June 30, 2017 and 2016 (in thousands):

	Pension Benefits		Postretirement Benefits	
	2017	**2016**	**2017**	**2016**
Change in benefit obligation				
Benefit obligation at beginning of year	$ 401,762	$ 365,733	$ 65,107	$ 53,699
Service cost	-	-	2,664	2,176
Interest cost	15,429	16,741	2,753	2,618
Benefits paid	(17,167)	(15,696)	(1,542)	(1,458)
Actuarial (gains) losses	(6,849)	34,984	(562)	8,072
Benefit obligation at end of year	393,175	401,762	68,420	65,107
Change in fair value of plan assets				
Fair value of plan assets at beginning of year	267,592	293,027	-	-
Actual return on plan assets	39,906	(9,739)	-	-
Employer contributions	103,396	-	1,542	1,458
Benefits paid	(17,167)	(15,696)	(1,542)	(1,458)
Fair value of plan assets at end of year	393,727	267,592	-	-
Funded status and recognized asset (liability)	$ 552	$ (134,170)	$ (68,420)	$ (65,107)

The accumulated benefit obligation for the Pension Plan was $393.2 million and $401.8 million at June 30, 2017 and 2016, respectively.

The net periodic benefit cost (income) consisted of the following for the years ended June 30, 2017 and 2016 (in thousands):

	Pension Benefits		Postretirement Benefits	
	2017	**2016**	**2017**	**2016**
Service cost	$ -	$ -	$ 2,664	$ 2,176
Interest cost	15,429	16,741	2,753	2,618
Expected return on plan assets	(18,494)	(19,219)	-	-
Amortization of actuarial losses	1,624	505	931	459
Net periodic benefit cost (income)	$ (1,441)	$ (1,973)	$ 6,348	$ 5,253

Actuarial (gains) losses and amounts amortized into net periodic benefit cost (income) for the years ended June 30, 2017 and 2016 were as follows (in thousands):

	Pension Benefits		Postretirement Benefits	
	2017	**2016**	**2017**	**2016**
Actuarial (gains) losses arising during the year	$ (28,261)	$ 63,943	$ (562)	$ 8,071
Net actuarial losses reclassified as a component of net periodic benefit cost	(1,624)	(505)	(931)	(458)
Change in amounts not yet recognized as net periodic benefit cost	$ (29,885)	$ 63,438	$ (1,493)	$ 7,613

The actuarial losses that have not yet been recognized as components of net periodic benefit cost at June 30, 2017 and 2016 were as follows (in thousands):

	Pension Benefits		Postretirement Benefits	
	2017	2016	2017	2016
Amounts not yet recognized as periodic benefit cost	$ 83,124	$ 113,009	$ 17,658	$ 19,151

There are no estimated prior service costs expected to be amortized into net periodic benefit cost in 2018 for the pension and postretirement plans. The estimated actuarial losses expected to be amortized into net periodic benefit cost in 2018 are $1,353,000 and $755,000 for the pension and postretirement plans, respectively.

	Pension Benefits		Postretirement Benefits	
	2017	2016	2017	2016
Weighted average assumptions				
Benefit obligation				
Discount rate	4.00%	3.90%	4.26%	4.25%
Net periodic benefit cost				
Discount rate	3.90%	4.63%	4.25%	4.91%
Expected return on plan assets	7.50%	7.50%	N/A	N/A

The expected return on plan assets is based on the target asset allocation at the beginning of the fiscal year and is determined using forward-looking assumptions in the context of historical returns. The expected return on plan assets assumption is evaluated on an annual basis. The change in asset allocation during fiscal year 2017 will result in a lower expected return assumption in future years.

The assumed healthcare cost trend rates at June 30, 2017 and 2016 were as follows:

	2017	2016
Healthcare cost trend rate assumed for the next year	7.90%	8.90%
Rate to which the cost trend rate is assumed to decline (ultimate trend rate)	4.50%	4.50%
Year that the rate reaches the ultimate trend rate	2026	2025

The fair value of the Organization's Pension Plan assets at June 30, 2017 and 2016 by asset category were as follows (in thousands):

	Fair Value Measurements at Reporting Date Using			
	Level 1	**Level 2**	**Level 3**	**Total**
2017				
Cash and cash management funds	$ 4,978	$ 14,166	$ -	$ 19,144
Fixed income				
U.S. government obligations	62,496	-	-	62,496
Corporate debt	-	294,034	-	294,034
Other debt securities	-	25,733	-	25,733
Total investments	$ 67,474	$ 333,933	$ -	401,407
Amounts receivable for securities sold				5,160
Interest receivable				3,709
Amounts payable for securities purchased				(16,549)
Total plan assets				$ 393,727
2016				
Cash and cash management funds	$ 1,505	$ -	$ -	$ 1,505
Mutual fund	60,927	-	-	60,927
Collective investment funds	-	3,312	128,791	132,103
Hedge funds and other	-	-	73,057	73,057
Total plan assets	$ 62,432	$ 3,312	$ 201,848	$ 267,592

The Organization has an investment strategy to reduce return-seeking assets and increase long duration fixed income allocations over time with the intention of reducing volatility of funded status and pension costs. During fiscal year 2017, the Organization contributed $103.4 million to the Pension Plan, which changed the asset allocation target to 100% fixed income and cash equivalents. Prior to the contribution, the target allocation to return-seeking assets was 70% and the target allocation to fixed income and cash equivalents was 30%.

A third party investment manager is engaged by the Organization to manage a custom long bond portfolio, which invests primarily in fixed income securities to match the duration of future pension payments. The assets are subject to investment grade, credit exposure and interest rate exposure restrictions. At June 30, 2017, the Pension Plan assets primarily included corporate and government debt instruments.

At June 30, 2016, fixed income securities were held by the collective investment and hedge funds which primarily included corporate bonds of companies from diversified industries and U.S. Treasuries. Return-seeking assets, some of which were included in common and collective funds, primarily included investments in large capital and small capital companies located in the U.S., as well as international equity securities in developed and emerging markets. Return-seeking assets also included hedge fund investments in absolute return/hedge funds that followed several different strategies and inflation-hedging assets such as real estate investment trusts, energy and commodities. The Organization engaged third party investment managers who invested in mutual funds, collective investment funds, hedge funds and other funds to achieve the previous target allocations.

The following table sets forth a summary of the changes in the fair value of the Pension Plan's Level 3 investments for the years ended June 30, 2017 and 2016 (in thousands):

	Collective Investment Funds	Hedge Funds and Other	Total
As of July 1, 2015	$ 122,679	$ 82,047	$ 204,726
Actual return on plan assets			
Relating to assets still held at the reporting date	2,510	(9,484)	(6,974)
Relating to assets sold during the period	132	494	626
Purchases	4,218	1,500	5,718
Sales	(748)	(1,500)	(2,248)
As of June 30, 2016	128,791	73,057	201,848
Actual return on plan assets			
Relating to assets still held at the reporting date	(15,762)	(19,382)	(35,144)
Relating to assets sold during the period	18,554	26,620	45,174
Purchases	77,908	23,159	101,067
Sales	(209,491)	(103,454)	(312,945)
As of June 30, 2017	$ -	$ -	$ -

The following benefit payments are expected to be paid from the respective plans (in thousands):

	Pension Benefits	Postretirement Benefits
Year ending June 30,		
2018	$ 17,824	$ 1,599
2019	18,634	1,734
2020	19,270	1,844
2021	19,871	2,001
2022	20,435	2,160
2023–2027	107,837	13,149
	$ 203,871	$ 22,487

The expected benefits are based on the same assumptions used to measure the benefit obligation at June 30 and include estimated future employee service for the postretirement plan.

The Organization is not required to make any contributions to its Pension Plan in 2018. The Organization expects to contribute $1.6 million to its postretirement medical plan in 2018.

The Organization has employee savings plans under Sections 403(b) and 401(k) of the IRC. The plans cover substantially all the Organization's employees after satisfying service requirements. Participating employees may defer up to 50% (subject to certain limitations) of their pretax earnings to the Section 401(k) plan.

The Organization makes employer matching and non-elective employer contributions to the 401(k) plan. Contributions to the 401(k) plan for the years ended June 30, 2017 and 2016 amounted to approximately $15.0 million and $14.0 million, respectively.

10. Natural Classification of Expenses

Operating expenses incurred for the years ended June 30, 2017 and 2016 were as follows (in thousands):

	2017	2016
Human resources and employee benefits	$ 214,673	$ 206,872
Taxes and recoveries	72,996	66,519
Professional fees and services	56,685	47,553
Depreciation and amortization	56,405	52,665
Scholarships	30,833	29,812
Collaborations	27,363	20,468
Rentals and utilities	16,568	15,896
Supplies	15,586	15,808
Interest	7,979	7,092
Other expenses	41,494	38,229
Total expenses	$ 540,582	$ 500,914

11. Commitments and Contingencies

Rental Income
The majority of land and buildings are generally leased under long-term lease arrangements. At June 30, 2017, future rental income from these leases based on present effective minimum rentals is summarized as follows (in thousands):

Year ending June 30,	
2018	$ 122,347
2019	115,246
2020	110,143
2021	104,274
2022	94,868
Thereafter	2,046,921
	$ 2,593,799

Percentage rental income, based on stipulated percentages of gross lessees' sales, amounted to approximately $17.2 million and $16.5 million for the years ended June 30, 2017 and 2016, respectively.

Capital Commitments
At June 30, 2017 and 2016, the Schools were committed under agreements with certain partnerships and corporations to invest an additional $1.4 billion and $1.3 billion, respectively.

At June 30, 2017 and 2016, open construction, renovation, major repair and other contracts amounted to $165 million and $172 million, respectively.

Litigation

There are various claims and complaints against the Organization that are incidental to its operations. Management, after consideration with legal counsel, is of the opinion that the ultimate resolution of these matters should not have a material adverse effect on the consolidated financial statements.

Trustee Matters

In accordance with Court approval, the Trustees are compensated with an annual retainer payable monthly and a meeting fee for each meeting attended which is subject to annual maximum meeting limitations. For the years ended June 30, 2017 and 2016, total Trustee compensation amounted to $702,000 and $541,000, respectively.

Supplementary Schedules

Kamehameha Schools and Subsidiaries
Schedules of Trust Spending
Years Ended June 30, 2017, 2016, 2015, 2014 and 2013
(All dollars in thousands) **Schedule 1**

	2017	2016	2015	2014	2013
Trust spending, net					
Campus-based programs					
Campus education	$ -	$ 3,461	$ 5,770	$ 7,440	$ 7,436
Kapalama	93,418	93,156	96,405	90,236	93,849
Hawaii	38,483	37,883	37,221	35,981	34,012
Maui	32,425	32,363	32,281	31,789	32,275
Preschools	32,893	31,855	29,381	28,961	29,340
Outreach programs					
Community education and engagement (includes funding for Hoʻokakoʻo, a not-for-profit organization, of $1,750, $1,752, $1,161, $1,083 and $50 for the years ended June 30, 2017, 2016, 2015, 2014 and 2013, respectively)	39,326	38,045	31,527	36,201	37,158
Collaborations	25,639	20,484	18,342	20,300	17,425
Scholarships	30,134	29,220	27,403	26,913	25,832
Innovations	1,432	-	-	-	-
Educational support services	23,349	15,639	11,693	12,030	11,993
Interest on debt	7,716	7,018	7,419	7,913	8,423
Other program expenditures	3,963	3,558	3,812	4,714	569
Base spending	328,778	312,682	301,254	302,478	298,312
Less: Tuition, fees and other educational income, net	(10,653)	(10,882)	(11,599)	(12,486)	(12,030)
Base distributions	318,125	301,800	289,655	289,992	286,282
Equipment	1,335	1,652	1,506	2,616	2,634
Information technology investment plan	5,518	4,042	5,880	10,123	14,920
Major repairs	7,167	6,767	7,225	6,391	9,055
Capital projects	20,786	15,843	20,512	57,414	40,348
Debt financing of capital projects	9,786	9,786	10,786	10,786	(14,839)
In-kind transactions	-	1,711	821	788	8,489
Total trust spending before reserve activity	362,717	341,601	336,385	378,110	346,889
Reserve activity – operating, net	-	-	-	-	(31,594)
Total trust spending	$ 362,717	$ 341,601	$ 336,385	$ 378,110	$ 315,295
Average fair value of endowment	$ 10,210,432	$ 9,807,128	$ 9,142,326	$ 8,514,061	$ 8,425,932
Trust spending rate before debt financing and reserve activity	3.5%	3.4%	3.6%	4.3%	4.3%
Trust spending rate	3.6%	3.5%	3.7%	4.4%	3.7%

See accompanying Report of Independent Auditors and notes to Schedules of Trust Spending.

1. Background and Purpose

The Schools' spending policy governs annual trust spending from the Endowment to support its educational purpose in perpetuity. The spending policy targets annual trust spending at 4% of the average fair value of the Endowment plus the net income, if any, generated from the Schools' agriculture and conservation lands. The spending policy also provides for actual trust spending to vary annually at a range of 2.5% to 6.0%.

For the years ended June 30, 2017, 2016, 2015, 2014 and 2013, the schedules were prepared on a modified accrual basis of accounting and presented total distributions made from the Endowment to fund educational programs (trust spending) by major program and activity. The schedules also presented trust spending rates for five fiscal years through June 30, 2017.

2. Trust Spending and Trust Spending Rate

Trust spending represents the amounts spent during the fiscal year on educational programs by major program and activity. The campus-based and outreach program costs represent direct and indirect costs of providing these programs. The Educational Support Services programs represent the costs of administering scholarships, financial aid, admissions, ancestry verification and other supporting functions for educational programs. Other program expenditures represent the direct and indirect costs of providing Ke Aliʻi Pauahi Foundation with scholarships and financial aid programs and certain educational services that benefit the various campus-based and outreach programs. Indirect costs, which represent the portion of the finance, operations and legal services and other ancillary costs that support the Schools' educational programs and purpose are allocated to education based on various methods depending on the type of cost including headcount, square footage and proportion in relation to the other estimates based on management's best judgment. Information technology investment plan includes information technology projects that are directly attributable to education as well as an allocation of information technology projects that are attributable to the entire organization. Major repairs, capital projects, interest on debt, net borrowing of debt and repayment of principal, and in-kind transactions are directly and indirectly attributable to education. Reserve activity represents the funding of an operating reserve, as approved by the Court, to ensure assets are readily available for unanticipated educational program expenses or the use of the operating reserve to fund educational program expenses. Reserve activity may also include returning funds to the Endowment if there are sufficient operating reserves.

For the purposes of this schedule, trust spending on educational programs includes major repairs and capital projects, an allocation of indirect costs, borrowing of debt, repayment of principal and the reserve activity. These items are not included in educational program expenses on the consolidated statements of activities. The trust spending rates are determined by dividing the total trust spending before debt financing and reserve activity and the total trust spending by the average fair value of the Endowment.

3. Endowment and Average Fair Value of the Endowment

The Endowment consists of all trust investment assets as described in Note 1 of the consolidated financial statements. The average fair value of the Endowment is based on the average of the prior 20-quarter-end fair values. Accordingly, the trust spending rates for the years ended June 30, 2017, 2016, 2015, 2014 and 2013 are based on the estimated average fair values over the last five fiscal years utilizing the respective quarter-end values. For information on fair values, see Note 2 in the notes of the Schedule of Total Return.

Kamehameha Schools and Subsidiaries
Schedule of Total Return
June 30, 2017 — Schedule 2

	Value at June 30, 2017 (In Thousands)	One-Year Total Return %	Five-Year Total Return %	Ten-Year Total Return %	Since July 1, 1999 Total Return %
Hawaii Real Estate	$ 3,550,769	12.2	11.6	10.6	11.4
Hawaii Real Estate Composite Index		7.0	10.5	6.4	7.2
Developed Markets (Economic Value)	1,756,848	23.6	13.9	6.2	7.9
Developed Markets Composite Index		18.2	11.6	4.2	4.6
Emerging Markets	614,686	21.8	7.5	3.8	N/A
Emerging Markets Composite Index		23.7	4.0	1.9	N/A
Private Equity	1,231,421	11.3	14.1	10.3	8.4
Private Equity Composite Index		10.8	11.2	8.3	10.7
Absolute Return	2,590,190	8.1	5.6	3.3	N/A
Absolute Return Composite Index		6.3	3.8	0.9	N/A
Marketable Real Assets (Economic Value)	357,965	-2.5	-2.9	1.1	N/A
Marketable Real Assets Composite Index		-4.7	-2.1	0.4	N/A
Illiquid Real Assets	554,588	19.4	0.5	6.8	17.5
Illiquid Real Assets Composite Index		24.5	0.6	4.8	6.4
Real Estate (Mainland)	250	NM	NM	NM	NM
Real Estate (Mainland) benchmark		NM	NM	NM	NM
U.S. Fixed Income	207,045	-2.4	1.3	4.6	5.2
Fixed Income Composite Index		-2.3	1.5	4.7	5.2
Global Fixed Income	280,802	6.6	2.7	N/A	N/A
Citigroup World Government		-4.1	-0.2	N/A	N/A
Cash Equivalents	405,702	0.3	-0.1	0.3	1.8
Three-month U.S. Treasury Bill		0.5	0.2	0.6	1.9
Total endowment, net of fees and direct expenses	$ 11,550,266	12.1	8.4	6.3	8.6
Endowment Fund Composite Benchmark		9.1	7.0	4.0	5.6
Total Endowment Fund Long-Term Objective (CPI+5%)		6.6	6.3	6.6	7.2

See accompanying Report of Independent Auditors and notes to Schedule of Total Return.

1. Background and Purpose

The Schools' investment policy establishes long-term and intermediate-term investment objectives, asset allocation targets, and performance measurement guidelines for the Endowment. The long-term investment return objective of the Endowment Fund is to meet or exceed an annualized real return of 5.0% (CPI + 5 percentage points), net of fees and direct expenses, over most rolling 10-year periods, as well as over longer periods. During 2015, the investment objective was revised to include only fees and direct expenses but not allocated support costs, consistent with industry practice.

The purpose of this schedule is to report the Schools' total return results for the Endowment (by asset class) as compared to long-term benchmark indices approved in the investment policy. The Schools' Endowment asset classes include:

Hawaii Real Estate
The Hawaii real estate assets can be divided into traditional land holdings, improved commercial properties, real estate held for development and sale, and purchase money mortgages. The traditional land holdings are typically leased to third parties under long-term ground leases while the improved commercial properties are actively managed by various third-party managers to generate space rents. Improved commercial properties are comprised of shopping centers, office buildings, and warehouse facilities.

Developed Markets
Developed markets is comprised primarily of marketable equity securities and derivative instruments of companies in the U.S. and developed markets outside of the U.S. Investments in this asset class are held directly or through commingled vehicles.

At June 30, 2017, the Schools held no S&P 500 short futures position to achieve asset allocation targets.

Emerging Markets
Emerging markets is comprised primarily of marketable equity securities and derivative instruments of companies in emerging markets. Investments in this asset class are held directly or through commingled vehicles.

Private Equity
Private equity investments are high risk, high potential return investments in illiquid privately placed equity or equity-related securities of nonpublic companies, companies or parts of companies that are being taken private, or public entities. The Schools' private equity and venture capital portfolio currently consists of limited partnership interests in pooled funds.

Absolute Return
Absolute return strategies endeavor to produce positive returns independent of the equity and fixed income markets though the underlying instruments are primarily equity and fixed income securities and derivatives thereof. The portfolio includes equity long-short, relative value, credit, diversified income and global macro strategies, and its exposure is global.

Marketable Real Assets
Real assets provide exposure to energy, commodities and other real assets globally. Marketable real assets are comprised primarily of marketable equity securities, derivatives and other liquid positions.

Illiquid Real Assets
Real assets provide exposure to energy, commodities and other real assets globally. Illiquid real assets are comprised primarily of illiquid investments in privately held companies and assets.

Real Estate (Mainland)
Mainland real estate assets consist of pooled and direct investments in residential, office, retail, timberland and a variety of other property types.

U.S. Fixed Income
Fixed income is comprised of investments in debt securities issued by a corporation, government or government agency. This asset class also includes, to a lesser degree, money market instruments, which include U.S. Treasury bills, bank certificates of deposit, repurchase agreements, commercial paper, bankers' acceptances, and derivative instruments. As of June 30, 2010, fixed income is comprised of investments in debt securities issued primarily by U.S. government and money market funds.

Global Fixed Income
Global fixed income is comprised primarily of debt securities issued by the U.S. government and governments of other developed countries. It also includes debt securities of other issuers such as corporations and the governments of emerging markets countries.

Cash Equivalents and Synthetic Cash
Cash equivalents are comprised of short-term investments in debt securities issued by a corporation, government or government agency, and money market instruments. Synthetic cash represents the funds that would have been available if the long domestic equity was liquidated instead of holding the short futures position.

At June 30, 2017, there was no synthetic cash.

2. Fair Value and Economic Value

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in the principal and most advantageous market in an orderly transaction between market participants. Unless otherwise indicated, values presented are fair values.

Economic value is defined as fair value plus notional exposure.

The following methods and assumptions were used to estimate the fair and economic value, as applicable, of each asset class:

Hawaii Real Estate
All of the commercial properties are currently externally appraised. Prior to June 2015, the commercial properties were appraised internally and an annual external review was obtained for valuation reasonableness. Prior to June 2008, commercial properties were externally appraised every three years. Most commercial properties are appraised using the discounted cash flow methodology.

All of the multifamily residential properties are currently externally appraised. The single-family residential properties are primarily internally appraised. Prior to June 2015, the residential properties were appraised internally and an annual external review was obtained for valuation reasonableness. Most residential properties are currently estimated using the discounted cash flow methodology.

The fair value of all real property interests is reduced by the fair value of any associated debt.

Developed Markets
The market values of marketable equity securities and derivatives for positions held directly are based on quoted market prices. For positions held through commingled vehicles, the market values are based on quoted prices of the underlying assets. As of June 30, 2017, market value was $1,757 million.

Emerging Markets
The market values of marketable equity securities and derivatives for positions held directly are based on quoted market prices. For positions held through commingled vehicles, the market values are based on quoted prices of the underlying assets.

Private Equity
Different techniques and many factors were considered in deriving the fair value of these investments. Several investments have been valued based on the underlying asset value and are based on a number of different factors including, among others, original cost, third-party financing transactions, discounted cash flows, and comparable industry multiples.

Absolute Return
Different techniques and many factors were considered in deriving the fair value of these investments. These investments have been valued based on the underlying asset value.

Marketable and Illiquid Real Assets
Different techniques have been utilized and factors considered in deriving the fair value of these investments. Marketable instruments are based on quoted market prices. Hedge funds, direct investments and limited partnership interests have been valued based on underlying asset values. As of June 30, 2017, Marketable Real Assets fair value was $358 million.

Real Estate (Mainland)
Different techniques were considered in deriving the fair value including net operating income divided by a capitalization rate, estimated cash flows discounted at a rate commensurate with risks involved, market comparables, independent appraisals, and carrying value of operating assets reduced by liabilities.

The fair value is reduced by the carrying value of any debt associated with such properties.

U.S. Fixed Income, Global Fixed Income and Cash Equivalents and Synthetic Cash
The market values of marketable debt securities, and cash equivalents are primarily based on quoted market prices. As of June 30, 2017, market value of cash equivalents was $406 million.

3. Total Return

Total return is calculated using the time weighted rate of return methodology. Total returns for periods greater than one year are annualized.

Total return for asset classes with derivative positions incorporates the associated gain or loss of such derivative and is based on the economic value.

Total return excludes certain indirect expenses, which represents twenty basis points for all periods presented.

“N/A” indicates that an asset class was not active for the respective time period.

“NM” indicates total return is not meaningful.

4. Benchmark Indices

The benchmark indices are set forth in the Schools' investment policy. Amendments to the benchmark indices are incorporated when effective and include revised benchmarks, asset class target weights, and blended benchmark allocation methodologies. Blended portfolio benchmarks are generally weighted based upon the asset class targets set forth in the Schools' approved investment but may be based upon actual weights. The following are comprised of the respective benchmarks:

- **Hawaii Real Estate Composite Index**
  CPI + 5% from July 1999 to December 2006; NCREIF from January 2007.

- **Developed Markets Composite Index**
  75% Russell 3000, 25% MSCI EAFE Net from July 1999 to December 2003; 67% Russell 3000, 33% MSCI EAFE Net from January 2004 to December 2006; 50% Russell 3000, 50% MSCI EAFE Net from January 2007 to February 2013; MSCI World Net from March 2013.

- **Emerging Markets Composite Index**
  MSCI Emerging Markets Free Index from July 1999 to December 2006; MSCI Emerging markets net from January 2007.

- **Private Equity Composite Index**
  CPI + 10% from July 1999 to June 2004; CPI + 8.75% from July 2004 to December 2006; Cambridge Associates vintage-year weighted custom benchmark from January 2007.

- **Absolute Return Composite Index**
  CPI + 8% from July 1999 to June 2004; CPI + 5% from July 2004 to December 2006; HFRI Fund of Funds Index from January 2007.

- **Marketable Real Assets Composite Index**
  40% Wilshire 5000 Energy Index, 40% Barclays Inflation-Indexed Bond Index (U.S. dollar hedged) and 20% Bloomberg Commodity Index to January 2010; 67% Wilshire 5000 Energy Index, 33% Bloomberg Commodity Index from February 2010, Wilshire 5000 Energy Index from February 2016.

- **Illiquid Real Assets Composite Index**
  CPI + 5% from July 1999 to December 2006; Cambridge Associates vintage-year weighted custom benchmark from January 2007.

- **Real Estate (Mainland) Benchmark**
  Per policy, there is no benchmark as this asset class is being liquidated.

- **U.S. Fixed Income Composite Index**
  Lehman Aggregate Index from July 1999 to December 2006; U.S. Treasury 6.5 Duration Bond Index from January 2007.

- **Global Fixed Income Index**
  Citigroup World Government Bond Index from January 2008.