Lili`uokalani Trust

Financial Statements and Supplemental Schedule
December 31, 2012 and 2011
Together with Independent Auditor's Report

KMHLLP

A Hawaii Limited Liability Partnership

Independent Auditor's Report

To the Trustees of
Lili`uokalani Trust:

Report on the Financial Statements

We have audited the accompanying financial statements of Lili'uokalani Trust (the Trust) which comprise the statements of financial position as of December 31, 2012 and 2011, and the related statements of activities, functional expenses and cash flows for the years then ended and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these 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 financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these 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 financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the 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 financial statements.

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

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Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Trust as of December 31, 2012 and 2011, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matter

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying supplementary information is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audits of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the 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 financial statements as a whole.

KMH LLP

KMH LLP

Honolulu, Hawaii
June 24, 2013

Lili`uokalani Trust

Statements of Financial Position
December 31, 2012 and 2011

Assets

	2012	2011
Current Assets:		
Cash and cash equivalents	$ 3,804,027	$ 4,543,063
Accounts receivable, net	2,624,979	2,968,781
Prepaid expenses and other assets	1,310,879	907,884
Total current assets	7,739,885	8,419,728
Property and Equipment, Net	25,040,163	20,020,272
Investments:		
Marketable securities	53,370,146	48,854,226
Other	108,923,242	96,899,612
Deferred Rent Receivable	20,049,395	19,397,156
Total assets	$ 215,122,831	$ 193,590,994

Liabilities and Net Assets

	2012	2011
Current Liabilities:		
Accounts payable and other accrued liabilities	$ 1,744,024	$ 1,068,100
Accrued vacation	938,197	860,925
Deferred revenue	461,000	360,000
Notes payable	191,096	1,848,012
Total current liabilities	3,334,317	4,137,037
Accrued Postretirement Benefits	1,439,993	1,249,894
Deferred Revenue, Less Current Portion	2,158,097	2,172,492
Notes Payable, Less Current Portion	7,031,909	2,271,672
Total liabilities	13,964,316	9,831,095
Commitments and Contingencies		
Net Assets:		
Unrestricted:		
Board designated for set aside liabilities	-	2,699,568
Undesignated	201,111,671	181,009,748
	201,111,671	183,709,316
Temporarily restricted	46,844	50,583
Total net assets	201,158,515	183,759,899
Total liabilities and net assets	$ 215,122,831	$ 193,590,994

See accompanying notes to financial statements.

Lili`uokalani Trust

Statements of Activities

For the Years Ended December 31, 2012 and 2011

	2012			2011		
	Unrestricted	Temporarily Restricted	Total	Unrestricted	Temporarily Restricted	Total
Revenues, Gains, and Other Suppport:						
Rent	$ 23,218,904	$ -	$ 23,218,904	$ 21,963,931	$ -	$ 21,963,931
Real property and general excise tax reimbursements	5,216,458	-	5,216,458	5,240,492	-	5,240,492
Donations	518,611	-	518,611	20,482	-	20,482
Net realized gains on sales and exchange of real estate	11,874,216	-	11,874,216	-	-	-
Net realized and unrealized gains (losses) on investments	4,488,153	-	4,488,153	(3,503,797)	-	(3,503,797)
Income from investments	2,165,789	-	2,165,789	1,540,381	-	1,540,381
Other	52,076	-	52,076	7,039	-	7,039
	47,534,207	-	47,534,207	25,268,528	-	25,268,528
Net assets released from restrictions	3,739	(3,739)	-	4,806	(4,806)	-
Total revenues, gains and other support	47,537,946	(3,739)	47,534,207	25,273,334	(4,806)	25,268,528
Expenses:						
Program services	15,643,071	-	15,643,071	17,440,884	-	17,440,884
Program support services	3,721,445	-	3,721,445	3,885,909	-	3,885,909
Endowment management services	10,651,747	-	10,651,747	11,604,682	-	11,604,682
Total expenses	30,016,263	-	30,016,263	32,931,475	-	32,931,475
Total revenues, gains and other support over expenses	17,521,683	(3,739)	17,517,944	(7,658,141)	(4,806)	(7,662,947)
Pension-related changes other than net periodic pension costs	(119,328)	-	(119,328)	3,313,683	-	3,313,683
Increase (decrease) in net assets	17,402,355	(3,739)	17,398,616	(4,344,458)	(4,806)	(4,349,264)
Net Assets at Beginning of Year	183,709,316	50,583	183,759,899	188,053,774	55,389	188,109,163
Net Assets at End of Year	$ 201,111,671	$ 46,844	$ 201,158,515	$ 183,709,316	$ 50,583	$ 183,759,899

See accompanying notes to financial statements.

Lili`uokalani Trust

Statements of Functional Expenses
For the Years Ended December 31, 2012 and 2011

	2012					2011				
		Support Services					Support Services			
	Program Services	Program Support	Endowment Management	Total	Total Expenses	Program Services	Program Support	Endowment Management	Total	Total Expenses
Salaries	$ 7,141,090	$ 1,752,191	$ 438,526	$ 2,190,717	$ 9,331,807	$ 7,171,260	$ 1,567,535	$ 915,135	$ 2,482,670	$ 9,653,930
Taxes	-	22,634	6,609,644	6,632,278	6,632,278	-	25,314	6,676,009	6,701,323	6,701,323
Financial Assistance	3,730,315	(730)	-	(730)	3,729,585	3,615,897	-	-	-	3,615,897
Loss on Pension Settlement	-	-	-	-	-	2,371,249	547,329	312,887	860,216	3,231,465
Employee Benefits and Payroll Taxes	1,763,511	382,083	122,705	504,788	2,268,299	1,536,226	347,681	136,277	483,958	2,020,184
Professional Services:										
Legal	-	19,131	225,630	244,761	244,761	-	11,199	310,521	321,720	321,720
Accounting	-	91,195	15,222	106,417	106,417	-	95,697	33,759	129,456	129,456
Other	4,910	330,648	526,367	857,015	861,925	54,713	188,870	397,891	586,761	641,474
Repairs and Maintenance	684,076	94,146	3,464	97,610	781,686	522,998	103,671	8,279	111,950	634,948
Insurance	387,437	64,945	95,484	160,429	547,866	369,778	63,853	91,882	155,735	525,513
Trustees' Fees	-	262,250	262,250	524,500	524,500	-	243,250	243,250	486,500	486,500
Utilities	339,516	123,976	14,769	138,745	478,261	303,728	122,720	14,397	137,117	440,845
Occupancy Expense	167,114	109,118	156,164	265,282	432,396	199,687	109,686	157,911	267,597	467,284
Travel and Meals	202,937	46,762	140,535	187,297	390,234	194,286	47,149	100,176	147,325	341,611
Other Expenses	70,497	103,261	170,808	274,069	344,566	31,553	160,020	101,568	261,588	293,141
Supplies	174,869	135,628	22,441	158,069	332,938	174,544	137,037	21,844	158,881	333,425
General Real Estate Expenses	-	-	207,890	207,890	207,890	-	-	247,962	247,962	247,962
Telephone	130,622	16,090	7,564	23,654	154,276	126,922	16,209	7,144	23,353	150,275
Education	65,382	73,116	-	73,116	138,498	70,979	7,509	-	7,509	78,488
Bad Debt Expense	-	-	131,179	131,179	131,179	-	-	134,906	134,906	134,906
Equipment Rental	60,625	22,522	9,630	32,152	92,777	58,212	30,334	9,697	40,031	98,243
Real Estate Management Fees	-	-	49,394	49,394	49,394	-	-	49,375	49,375	49,375
Grants Paid	43,500	3,500	-	3,500	47,000	55,000	-	-	-	55,000
Dues	3,507	13,847	14,435	28,282	31,789	3,736	11,868	10,677	22,545	26,281
Leasing Commission	-	-	28,425	28,425	28,425	-	-	189,416	189,416	189,416
Publications	1,408	2,280	1,954	4,234	5,642	1,106	2,798	2,705	5,503	6,609
Total expenses before depreciation and amortization	14,971,316	3,668,593	9,254,480	12,923,073	27,894,389	16,861,874	3,839,729	10,173,668	14,013,397	30,875,271
Depreciation and Amortization	671,755	52,852	1,397,267	1,450,119	2,121,874	579,010	46,180	1,431,014	1,477,194	2,056,204
Total	$ 15,643,071	$ 3,721,445	$ 10,651,747	$ 14,373,192	$ 30,016,263	$ 17,440,884	$ 3,885,909	$ 11,604,682	$ 15,490,591	$ 32,931,475

See accompanying notes to the financial statements.

Lili`uokalani Trust

Statements of Cash Flows
For the Years Ended December 31, 2012 and 2011

	2012	2011
Cash Flows from Operating Activities:		
Cash received from customers	$ 28,213,530	$ 25,341,525
Cash paid to suppliers for goods and services	(17,512,279)	(21,736,765)
Cash paid to employees for services	(9,331,807)	(9,653,930)
Net investment income received	2,165,789	1,540,381
Other cash (disbursements) receipts	(58,644)	3,341,204
Net cash provided by (used in) operating activities	3,476,589	(1,167,585)
Cash Flows from Investing Activities:		
Proceeds from the sales or maturities of marketable securities	6,785,115	16,144,803
Purchases of marketable securities	(6,314,358)	(16,396,485)
Proceeds from the sales or maturities of limited partnership interests	3,800,204	13,424,035
Purchases of limited partnership interests	(12,943,472)	(6,490,131)
Proceeds from the sales of real estate	10,184,403	-
Purchases of real estate	(5,014,916)	(2,015,508)
Purchases of property and equipment	(3,815,922)	(3,412,608)
Net cash (used in) provided by investing activities	(7,318,946)	1,254,106
Cash Flows from Financing Activities:		
Proceeds under line of credit	3,776,000	1,783,300
Proceeds from note payable	5,000,000	-
Repayment of line of credit	(5,559,300)	-
Repayment of notes payable	(113,379)	(61,413)
Net cash provided by financing activities	3,103,321	1,721,887
Net (decrease) increase in cash	(739,036)	1,808,408
Cash and Cash Equivalents at Beginning of Year	4,543,063	2,734,655
Cash and Cash Equivalents at End of Year	$ 3,804,027	$ 4,543,063

See accompanying notes to financial statements.

Lili`uokalani Trust

Statements of Cash Flows
For the Years Ended December 31, 2012 and 2011

	2012	2011
Reconciliation of Cash Flows from Operating Activities:		
Increase (decrease) in net assets	$ 17,398,616	$ (4,349,264)
Adjustments to reconcile increase (decrease) in net assets to net cash provided by (used in) operating activities:		
Net realized gains on sales and exchange of real estate	(11,874,216)	-
Contributed property	(510,000)	-
Net realized and unrealized (gains) losses on investments	(4,488,153)	3,503,797
Depreciation and amortization	2,121,874	2,056,204
Decrease (increase) in accounts receivable	343,802	(818,725)
Decrease in prepaids expenses and other assets	107,005	743,944
Increase in deferred rent receivable	(652,239)	(687,165)
Increase in accounts payable and other accrued liabilities	675,924	131,122
Increase in accrued vacation	77,272	20,394
Increase (decrease) in deferred revenue	86,605	(357,008)
Decrease in accrued pension benefits	-	(1,436,957)
Increase in accrued postretirement benefits	190,099	26,073
Net cash provided by (used in) operating activities	$ 3,476,589	$ (1,167,585)

See accompanying notes to financial statements.

1. Summary of Operations and Significant Accounting Policies

a. Operations

Lili`uokalani Trust (the Trust) was created in 1909 by the late Queen Lili`uokalani, Hawaii's last reigning monarch. The Trust is dedicated to providing support and services to orphan and destitute children, with preference given to those of Hawaiian ancestry. Income of the Trust is derived principally from rental income received from long-term leases on owned real estate, sales of certain real property located in the state of Hawaii and investment income realized from its investment portfolios.

b. Basis of Presentation

The Trust's net assets and activities are classified based on the existence or absence of donor-imposed restrictions as follows:

- **Unrestricted Net Assets** – Net assets not subject to donor-imposed stipulations. The portion of unrestricted net assets that the board of trustees has designated for a specific purpose is presented separately from the undesignated net assets in the accompanying statements of financial position. The board of trustees retains full control over such designated funds and may use them for any purpose.

- **Temporarily Restricted Net Assets** – Net assets subject to donor-imposed stipulations that may or will be met either by actions of the Trust and/or the passage of time.

- **Permanently Restricted Net Assets** – Net assets subject to donor-imposed stipulations that must be maintained permanently by the Trust. The donors of these assets generally permit the use of the income earned on related investments for general or specific purposes. The Trust has no permanently restricted net assets.

c. Management Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (US 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 financial statements and the reported amounts of revenues and expenses during the reporting period. Significant items subject to such estimates and assumptions include the carrying amount of receivables, real property, investments, and accrued postretirement benefits. Actual results could differ from those estimates.

1. Summary of Operations and Significant Accounting Policies (continued)

d. Income Taxes

The Trust has been recognized by the Internal Revenue Service as exempt from Federal income tax under Section 501(c)(3) of the Internal Revenue Code (Code) and is classified as a private operating foundation under Section 4942. As an exempt private operating foundation, the Trust is not subject to the excise tax on net investment income for private foundations. To maintain its private operating foundation status, the Code requires the distribution, for charitable purposes, of at least 85 percent of the lesser of adjusted net income or the minimum investment return (i.e., five percent of the aggregate fair market value of investment assets less cash deemed to be held for charitable purposes). The distribution must not be less than 2/3 of minimum investment return.

In each of the years 2012 and 2011, the Trust has expended sufficient amounts for charitable purposes or utilized distribution carryovers from prior years to not incur a tax for failure to distribute income that is imposed by the aforementioned section of the Code.

e. Cash and Cash Equivalents

The Trust primarily maintains its cash in bank deposit accounts and had approximately $758,000 and $756,000 in excess of federally insured limits at December 31, 2012 and 2011, respectively. The Trust has not experienced losses in these accounts and management believes there is no significant credit risk related to cash.

The Trust considers cash on hand, deposit accounts and financial instruments with original maturities of three months or less at the date of purchase to be cash and cash equivalents.

f. Accounts Receivable

Accounts receivable consist of amounts due from investment managers and percentage rent due from lessees. Management determines the allowance for doubtful accounts by identifying troubled accounts and using historical experience applied to an aging of accounts. Accounts receivable are written off when deemed uncollectible and recoveries of previously written off receivables are recorded when received. For the years ended December 31, 2012 and 2011, management's estimated allowance was approximately $220,000 and $230,000, respectively.

1. Summary of Operations and Significant Accounting Policies (continued)

g. Prepaid Expenses and Other Assets

Prepaid expenses and other assets consist primarily of deferred leasing commissions and escrow deposits. Deferred leasing commissions are amortized on a straight-line basis over the term of the related leases.

h. Property and Equipment

Property and equipment are recorded at cost, except that land acquired in the original deed of trust is recorded at the appraisal value at date of grant. All Trust property and equipment is considered exempt. Exempt property represents property used for program services. Maintenance and repairs are expensed as incurred and expenditures for renewals or betterments are capitalized.

Depreciation is calculated using the straight-line method over the estimated useful lives of the assets.

Furniture, fixtures and equipment	3 to 7 years
Buildings and improvements	Shorter of lease term or 20 years
Land improvements	30 years

i. Investments

Investments include marketable securities, non-controlling interests in for-profit limited partnerships, and real estate. Investments in marketable securities consist of mutual funds and equity securities and are stated at fair value based on quoted market prices. Investments in real estate and for-profit limited partnerships are classified as other investments and are reported at the lower of cost or fair value.

Included in investments are cash equivalents of $967,698 and $1,126,732 at December 31, 2012 and 2011, respectively, which the Trust has elected not to classify as cash equivalents in the statements of financial position.

1. Summary of Operations and Significant Accounting Policies (continued)

j. Deferred Rent Receivable

The Trust, as lessor, has lease agreements that provide for scheduled rent increases over the terms of the leases. Rental income is recognized on a straight-line basis over the term of the lease. The difference between rental income per the lease agreements and amounts recognized on a straight-line basis is recorded as deferred rent receivable on the accompanying statements of financial position.

k. Deferred Revenue

Deferred revenue consists of rents received in advance of the due date and lease extension premiums. Lease extension premiums are amortized on a straight-line basis over the life of the related leases.

l. Employee Benefit Plans

The Trust accounts for its defined benefit and postretirement benefit plans in accordance with Accounting Standards Codification (ASC) 715, *Employers Accounting for Pensions*. ASC 715 prescribes standards of financial accounting and reporting for an employer that offers pension benefits to its employees. ASC 715 requires employers to (a) recognize the overfunded or underfunded status of a single-employer defined benefit postretirement plan as an asset or liability in its statement of financial position and to recognize changes in that funded status in unrestricted net assets in the year in which the changes occur, and (b) measure the funded status of a plan as of the date of its year-end statement of financial position.

m. Donations

The Trust reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statements of activities as net assets released from restrictions.

1. Summary of Operations and Significant Accounting Policies (continued)

n. Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed Of

Long-lived assets (individual assets or asset groups) are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If future net cash flows are less than the carrying value of an asset, an impairment loss is recognized to the extent the asset's carrying value exceeds its fair value. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

o. Reclassifications

Certain reclassifications were made to prior year's financial statements to conform to the 2012 presentation. Such reclassifications had no impact on the previously reported change in net assets.

p. Recent Accounting Pronouncement

In October 2012, the Financial Accounting Standards Board issued ASC Update 2012-05, *Statement of Cash Flows (Topic 230) – Not-for-Profit (NFP): Classification of the Sale Proceeds of Donated Financial Assets in the Statement of Cash Flows*. This guidance requires a NFP to classify cash receipts from the sale of donated financial assets consistently with cash donations received in the statement of cash flows if those cash receipts were from the sale of donated financial assets that upon receipt were directed without any NFP-imposed limitations for sale and were converted nearly immediately into cash. Accordingly, the cash receipts from the sale of those financial assets should be classified as cash inflows from operating activities, unless the donor restricted the use of the contributed resources to long-term purposes, in which case those cash receipts should be classified as cash flows from financing activities. Otherwise, cash receipts from the sale of donated financial assets should be classified as cash flows from investing activities by the NFP. This guidance is effective prospectively for fiscal years, and interim periods within those years, beginning after June 15, 2013. Management does not believe that the adoption of this guidance will have a significant effect on the Trust's financial position or results of operations.

q. Subsequent Events

The Trust has evaluated subsequent events through June 24, 2013, the date the financial statements were issued.

2. Investments

a. Marketable Securities

Investments stated at fair value at December 31, 2012 and 2011 were as follows:

	Fair Value	Cost	Unrealized Gains/(Losses)
2012:			
Cash equivalents	$ 967,698	$ 967,698	$ -
Mutual funds	43,998,325	40,920,547	3,077,778
Equity securities	8,404,123	6,924,694	1,479,429
	$ 53,370,146	$ 48,812,939	$ 4,557,207
2011:			
Cash equivalents	$ 1,126,732	$ 1,126,732	$ -
Mutual funds	40,744,056	42,364,722	(1,620,666)
Equity securities	6,983,438	6,491,923	491,515
	$ 48,854,226	$ 49,983,377	$ (1,129,151)

b. Other Investments

The Trust's other investments consist of investments in for-profit limited partnerships and real estate held for use, sale and development. As allowed under ASC 958-325-35, the Trust accounts for its other investments at the lower of cost or fair value. Under this method, the same measurement attribute is used for all other investments and declines in the value of those investments are recognized if their aggregate market value is less than their carrying amount; recoveries of aggregate market value in subsequent periods are recorded in those periods subject only to the limitation that the carrying amount does not exceed the original cost.

2. Investments (continued)

b. Other Investments (continued)

At December 31, 2012 and 2011, the cost and fair value of other investments was as follows:

	Cost	Fair Value (Unaudited)	Fair Value Over/(Under) Cost (Unaudited)
2012:			
Investment in real estate	$ 35,746,349	$ 403,013,547	$ 367,267,198
Investment in for-profit limited partnerships	73,176,893	86,184,219	13,007,324
Total	$ 108,923,242	$ 489,197,766	$ 380,274,522
2011:			
Investment in real estate	$ 32,367,467	$ 411,739,745	$ 379,372,278
Investment in for-profit limited partnerships	64,532,145	70,295,712	5,763,567
Total	$ 96,899,612	$ 482,035,457	$ 385,135,845

The Trust has formal commitments with various limited partnerships to acquire interests in the partnerships up to agreed upon amounts. The Trust, at the discretion of the limited partnerships, may be called upon to fully fund their commitments. At December 31, 2012 and 2011, the Trust had outstanding funding commitments of approximately $10,900,000 in both years.

2. Investments (continued)

b. Other Investments (continued)

Investment in real estate at December 31, 2012 and 2011 consisted of the following:

	Held for Use	Held for Sale	Held for Development	Total
2012:				
Land	$ 1,001,525	$ 691,772	$ 224,120	$ 1,917,417
Building and improvements	42,366,601	-	-	42,366,601
	43,368,126	691,772	224,120	44,284,018
Accumulated depreciation and amortization	(16,407,897)	-	-	(16,407,897)
	26,960,229	691,772	224,120	27,876,121
Construction in progress (see Note 9)	-	-	7,870,228	7,870,228
Investment in real estate, net	$ 26,960,229	$ 691,772	$ 8,094,348	$ 35,746,349
2011:				
Land	$ 1,001,525	$ 830,929	$ 224,120	$ 2,056,574
Building and improvements	39,930,309	-	-	39,930,309
	40,931,834	830,929	224,120	41,986,883
Accumulated depreciation and amortization	(15,245,403)	-	-	(15,245,403)
	25,686,431	830,929	224,120	26,741,480
Construction in progress (see Note 9)	-	-	5,625,987	5,625,987
Investment in real estate, net	$ 25,686,431	$ 830,929	$ 5,850,107	$ 32,367,467

Real estate held for use primarily represents property that the Trust leases to third parties under non-cancelable leases.

Real estate held for sale consists of the Trusts' interest in the land under certain four condominium properties.

2. Investments (continued)

b. Other Investments (continued)

In 2007, the Trust entered into an agreement with Kawaiahao Church (Church) to acquire the Church's minority leased fee interest in the land underlying a condominium building for an initial purchase price of $3,290,000. The initial purchase price was allocated to the cost basis of each apartment unit. Any contingent payments relating to future sales of apartment units made to the Church will be accounted for as an adjustment to the cost basis of each unit in the year such unit is sold.

The purchase agreement also contains additional payments contingent on the future sales of apartment units. This contingent additional payment requirement expired on August 11, 2012. Under the agreement, the Trust was required to pay to the Church 8.2 percent of the gross sales price, as defined, of each apartment unit sold and closed by the Trust within five years of the Trust's purchase of the Church's interest. The agreement allowed the 8.2 percent share per apartment unit payment to the Church to be reduced by the Trust for the allocated amount of the initial purchase price to each unit.

For the year ended December 31, 2012, the Trust received proceeds of approximately $3,492,000 and recognized a gain of approximately $3,283,000 related to sales of the land underlying the condominium. Through August 10, 2012, the Trust made contingent payments to the church of $84,000 and no further contingent payments are required. There were no sales of real estate during 2011.

Real estate held for development includes land acquisition costs, initial planning costs and capitalized interest related to various parcels of land in Kona.

3. Property and Equipment

Property and equipment at December 31, 2012 and 2011 consisted of the following:

	2012	2011
Land	$ 3,587,975	$ 3,587,975
Building and improvements	33,123,051	24,322,485
Furniture, fixtures and equipment	3,578,707	3,285,837
	40,289,733	31,196,297
Accumulated depreciation and amortization	(15,407,760)	(14,500,150)
	24,881,973	16,696,147
Construction in progress (see Note 9)	158,190	3,324,125
Property and equipment, net	$ 25,040,163	$ 20,020,272

For the years ended December 31, 2012 and 2011, the Trust capitalized approximately $201,000 and $112,000 of interest costs, respectively.

4. Fair Value Measurements

US GAAP establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under US GAAP are described below:

Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Trust has the ability to access.

Level 2: Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

4. Fair Value Measurements (continued)

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The Trust's investments are recorded at fair value as follows:

Mutual funds are stated at fair value using quoted market prices. Shares of mutual funds are valued at the net asset value of shares held by the Trust at the reporting date on a recurring basis.

Equity securities are stated at fair value using quoted market prices.

The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

There have been no changes in the methodologies used at December 31, 2012 and 2011.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Trust believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

4. Fair Value Measurements (continued)

The following table sets forth the Trust's investments by type of fund based on Level 1 inputs as of December 31, 2012:

Mutual funds:	
Diversified emerging markets	$ 9,508,848
Intermediate-term bond	7,277,520
Money market funds	6,171,386
Foreign large growth	4,386,537
World bond	4,349,272
Foreign large value	4,241,779
Large growth	3,918,574
Foreign small/mid value	2,887,660
Small growth	1,256,749
Total mutual funds	43,998,325
Equity securities:	
Consumer goods	3,043,090
Services	1,523,728
Financial	1,101,416
Basic materials	1,044,141
Technology	754,708
Healthcare	608,095
Conglomerates	115,445
Consumer entertainment	90,698
Industrial goods	84,852
Utilities	37,950
Total equity securities	8,404,123
Cash equivalents	967,698
Total investments at fair value	$ 53,370,146

4. Fair Value Measurements (continued)

The following table sets forth the Trust's investments by type of fund based on Level 1 inputs as of December 31, 2011:

Mutual funds:	
Money market funds	$ 7,879,138
Diversified emerging markets	7,501,181
Intermediate-term bond	6,594,448
Foreign large value	5,427,154
World bond	4,048,976
Large growth	3,283,352
Foreign small/mid value	2,613,351
Foreign large growth	2,280,490
Small growth	1,115,966
Total mutual funds	40,744,056
Equity securities:	
Consumer goods	2,447,447
Services	1,192,653
Basic materials	983,625
Technology	790,150
Financial	710,789
Healthcare	571,890
Conglomerates	104,737
Industrial goods	67,869
Consumer entertainment	59,488
Utilities	54,790
Total equity securities	6,983,438
Cash equivalents	1,126,732
Total investments at fair value	$ 48,854,226

4. Fair Value Measurements (continued)

The Trust's other financial instruments include cash and cash equivalents, receivables, prepaid expense and other assets, accounts payable and other accrued liabilities. The carrying amounts of these assets and liabilities approximate fair value because of the short-term nature of these instruments.

As of December 31, 2012 and 2011, the carrying amount of notes payable was approximately $7,223,000 and $4,120,000, respectively, which approximates fair value as the interest rate is commensurate with interest rates currently offered by lending institutions for loans of similar terms to companies with comparable credit risk.

5. Temporarily Restricted Net Assets

Temporarily restricted net assets at December 31, 2012 and 2011 consisted of the following:

	2012	2011
Operations:		
U.S. Department of Education Summer Food Service Program	$ 568	$ 568
Other/Emergency Fund	46,276	50,015
Total	$ 46,844	$ 50,583

Net assets in the amount of approximately $3,700 and $4,800 were released from donor restrictions in 2012 and 2011, respectively, by incurring expenses satisfying the restricted purposes related to the applicable programs.

6. Designated Net Assets

In 2006, the Trustees designated $3,018,000 for the renovation of the Waianae Coast Children's Center. On March 19, 2007, the Trust received a private letter ruling from the Internal Revenue Service approving the designated amount as a qualifying distribution for the tax year ended December 31, 2006. The set aside is reduced as related expenditures are incurred. In 2009, the Trustees increased the amount designated for the renovation of the Waianae Coast Children's Center by $2,982,000. On November 10, 2009, the Trust received a private letter ruling from the Internal Revenue Service approving the designated amount as a qualifying distribution for the tax year ended December 31, 2009. In 2012 and 2011, the Trust recorded expenditures related to the renovation of the Waianae Coast Children's Center of approximately $2,700,000 and $2,747,000, respectively. As of December 31, 2012, the full amount of the set aside had been applied to expenditures incurred.

7. Employee Benefit Plans

a. 401(k) Plan

In 2005, the Trust established a defined contribution plan qualifying under Section 401(k) of the Internal Revenue Code, covering all regular employees who have six months of service and are age 21 or older. Employees may contribute up to 75 percent of included compensation, as defined in the defined contribution plan. The Trust matches 100 percent of employee contributions up to the first 3 percent of included compensation, plus 50 percent of employee contributions up to the next 2 percent of included compensation.

Expenses related to the Plan totaled approximately $358,000 and $349,000 for the years ended December 31, 2012 and 2011, respectively.

b. Defined Benefit Pension and Postretirement Benefit Plans

The Trust has a non-contributory defined benefit pension plan (the Plan) covering substantially all of its employees. The Plan's benefits are based on years of service and the employee's compensation during the last several years of employment. The Trust's funding policy is to contribute annually the amount consistent with the minimum funding standards as required by applicable federal regulations.

Effective December 31, 2004, the Plan was curtailed. Upon the effective date of the curtailment, accrual of benefits ceased and no individual is able to become an eligible participant of the Plan.

7. Employee Benefit Plans (continued)

b. Defined Benefit Pension and Postretirement Benefit Plans (continued)

The Trust also provides postretirement health benefits to eligible employees based on age and years of service. The plan covers the cost of medical plan coverage subject to a set monthly maximum.

During 2008, the Trustees approved the termination of the defined benefit pension plan subject to management's evaluation of the cost/benefit of such action. In October 2009, the Trust officially terminated the defined benefit pension plan. In October 2011, the Trust settled its pension obligation by providing participants with annuities or lump sum payments as provided for under the pension plan.

The changes in the obligations and assets of the Trust's postretirement benefit plan and the changes in unrestricted net assets for 2012 and the funded status of this plan and amounts related to this plan reflected in the Trust's statements of financial position were as follows:

	Postretirement Benefits
Benefit obligation, December 31, 2011	$ 1,249,894
Service cost	42,524
Interest cost	64,708
Actuarial loss	117,593
Benefits paid	(34,726)
Benefit obligation, December 31, 2012	1,439,993
Fair value of plan assets, December 31, 2011	-
Employer contribution	34,726
Benefits paid	(34,726)
Fair value of plan assets, December 31, 2012	-
Accrued postretirement benefits	$ (1,439,993)
Change in net periodic benefit cost not yet recognized:	
As of December 31, 2011	$ 268,048
Current year	(119,328)
Current net periodic benefit cost not yet recognized	$ 148,720

7. Employee Benefit Plans (continued)

b. Defined Benefit Pension and Postretirement Benefit Plans (continued)

The changes in the obligations and assets of the Trust's defined benefit plans and the changes in unrestricted net assets for 2011 and the funded status of these plans and amounts related to these plans reflected in the Trust's statements of financial position were as follows:

	Pension Benefits	Postretirement Benefits
Benefit obligation, December 31, 2010	$ 10,662,921	$ 1,223,821
Service cost	-	54,782
Interest cost	44,429	69,739
Actuarial gain	(291,145)	(76,507)
Benefits paid	(10,416,205)	(21,941)
Benefit obligation, December 31, 2011	-	1,249,894
Fair value of plan assets, December 31, 2010	9,225,964	-
Actual return on plan assets	49,929	-
Employer contribution	1,169,383	21,941
Administrative expenses	(29,071)	-
Benefits paid	(10,416,205)	(21,941)
Fair value of plan assets, December 31, 2011	-	-
Accrued postretirement benefits	$ -	$ (1,249,894)
Change in net periodic benefit cost not yet recognized:		
As of December 31, 2010	$ (3,231,465)	$ 185,830
Current year	3,231,465	82,218
Current net periodic benefit cost not yet recognized	$ -	$ 268,048

The overall expected long-term rate of return on assets assumption is based on the expected returns of various asset classes weighted by the pension plan's asset allocation.

7. Employee Benefit Plans (continued)

b. Defined Benefit Pension and Postretirement Benefit Plans (continued)

The following estimated future postretirement benefit payments, which reflect expected future service are expected to be paid in the years indicated:

	Postretirement Benefit Plan
Years ending December 31,	
2013	$ 37,914
2014	44,777
2015	51,178
2016	58,616
2017	65,807
2018 – 2022	355,933

The Trust expects to contribute approximately $38,000 to its postretirement benefit plan in 2013.

The following assumptions were used in accounting for the plans at December 31:

	Postretirement Benefit Plan	
	2012	2011
Benefit obligation:		
Discount rate	4.25%	5.25%
Expected long-term rate of return on plan assets	n/a	n/a
Health care trend rates	8% - 5%	8.5% - 5%
Year of ultimate trend	2025	2019
Net periodic benefit cost (years ended):		
Discount rate	5.25%	5.75%
Expected long-term rate of return on plan assets	n/a	n/a
Health care trend rates	8.5% - 5%	9% - 5%
Year of ultimate trend	2019	2019

7. Employee Benefit Plans (continued)

b. Defined Benefit Pension and Postretirement Benefit Plans (continued)

The components of net periodic benefit cost were as follows:

	Pension Plan	Postretirement Benefit Plan	
	2011	2012	2011
Service cost	$ -	$ 42,524	$ 54,782
Interest cost	44,429	64,708	69,739
Expected return on plan assets	(46,130)	-	-
Amortization of net loss (gain)	22,554	(18,454)	(11,008)
Settlement loss	2,913,967	-	-
Amortization of unrecognized net transition obligation	-	16,719	16,719
Net periodic benefit cost	$ 2,934,820	$ 105,497	$ 130,232

The estimated transition obligation for the postretirement benefit plan that will be amortized from unrestricted net assets into net periodic pension benefit cost during 2013 is $16,719.

8. Notes Payable

In 2004, the Trust entered into a term loan agreement with a bank in the original amount of $1,300,000 to finance the purchase of its main office space and related improvements. Effective June 27, 2012, the Trust entered into a loan amendment agreement to extend and amend the terms of the loan. The loan interest rate decreased from 5.31 percent to 3.23 percent and required monthly principal and interest payments decreased from $7,836 to $5,178. The maturity date of the loan is extended to July 1, 2022. There was a balance of approximately $1,050,000 and $1,083,000 outstanding on the loan at December 31, 2012, and 2011, respectively.

In June 18, 2012, the Trust entered into a $5,000,000 commercial term loan agreement with the aforementioned bank to fund the construction of its Waianae Coast Children's Center (see note 6). The loan matures on July 1, 2022, bears interest at 3.23 percent and requires the Trust to make monthly principal and interest payments of $24,314. There was a balance of approximately $4,947,000 outstanding on the loan at December 31, 2012.

8. Notes Payable (continued)

Both term loans are secured by approximately $11.6 million of marketable securities, and also require the Trust to maintain certain financial covenants related to its loan to value ratio, as defined in the loan agreement. The Trust was in compliance with these requirements as of December 31, 2012.

The Trust also has a line of credit with the aforementioned bank. In connection with the $5,000,000 commercial term loan, the Trust reduced its line of credit from $5,000,000 to $2,500,000. The line of credit bears interest at a variable interest rate and is subject to the Trust's choice of the bank's one-, three- or six-month London Inter-Bank Offer Rates (LIBOR) plus 0.875 percent or the bank's base rate minus a margin of .75 percent with a minimum interest rate not less than 1.75 percent, and expires in October 2013. As of December 31, 2012, there were no outstanding draws on the line of credit. As of December 31, 2011 there were outstanding draws of approximately $1,783,000 on the line of credit bearing interest at 1.75 percent.

On February 19, 2008, the Trust entered into a promissory note with a bank in the original amount of $1,350,000 to finance the purchase of the Wili Pa Loop property and related improvements for the Maui Children's Center. The maturity date of the loan is February 22, 2017. The note bears interest in three 36 month interest rate periods at the ends of which, the rate will be adjusted to match the current market commercial rate for similar loans at that date until repayment of the loan. The note bore an interest rate of 4.10 percent during the years ended December 31, 2012 and 2011. There was a balance of approximately $1,226,000 and $1,253,000 outstanding on the note at December 31, 2012 and 2011, respectively.

The approximate annual principal payments on notes payable at December 31, 2012 were as follows:

For the years ending December 31,	
2013	$ 191,000
2014	198,000
2015	204,000
2016	211,000
2017	1,290,000
Thereafter	5,129,005
	$ 7,223,005

8. Leases As Lessor

Land held by the Trust as investment property is leased or available for lease under operating lease arrangements which expire through 2082.

Future minimum rental revenues under non-cancelable operating leases as of December 31, 2012 were approximately as follows:

For the years ending December 31,	
2013	$ 19,558,000
2014	19,609,000
2015	19,447,000
2016	19,621,000
2017	23,750,000
Thereafter	644,905,000
Total	$ 746,890,000

The Trust receives percentage rentals (based on lessees' gross receipts, as defined) on certain of its properties. Percentage rent revenues earned for the years ended December 31, 2012 and 2011, amounted to approximately $2,536,000 and $1,798,000, respectively.

9. Commitments

The Trust entered into contracts with various third parties related to its development projects and construction in progress. At December 31, 2012, these contracts totaled approximately $12,973,000, of which the Trust had incurred approximately $10,932,000 as of December 31, 2012.

In October 2012, the Trust executed a promissory note agreement in the amount of $1,490,235 with a government agency to secure the Trust's commitment to fund its estimated share of costs under a water resource development agreement. The promissory note requires the Trust to pay the full amount of the promissory note within forty five days of receiving supporting evidence of the cost incurred. The note does not bear interest and is secured by approximately $2,600,000 of marketable securities, as defined in the agreement.

Supplementary Information

Lili'uokalani Trust

Supplemental Schedule of Land
December 31, 2012

	Cost Basis	Appraisal Basis (Unaudited)
Investment Land:		
Oahu:		
Waikiki	$ 1,283,297	$ 212,762,100
Other Oahu	247,791	9,135,600
Hawaii:		
Kona:		
Developed	49,331	78,573,800
Undeveloped	224,120	80,128,400
Leased for agriculture	112,877	2,257,200
Other Hawaii	1	5,095,300
Total investment land	1,917,417	387,952,400
Land Used for Tax Exempt Purposes --		
Children's Centers:		
Hilo	302,816	550,000
Kona	1	459,500
Kaneohe	703,316	620,000
Kapalama	217,160	2,110,000
Kauai	966,858	770,000
Maui	883,190	930,000
Punaluu	1	3,100,400
Waianae	514,634	650,000
Total land used for tax exempt purposes	3,587,976	9,189,900
Total land	$ 5,505,393	$ 397,142,300

Note: The supplemental "appraisal basis" value of land is stated primarily at the estimated market value on January 1, 2010 as appraised by John Child & Company, in its report dated November 15, 2010. For land sales that were not given a separate tax map key in the appraisal, their appraisal value has been removed in proportion to their cost basis. Land purchases subsequent to the appraisal have been included in the appraisal basis at cost.

See accompanying independent auditor's report.