

Lili‘uokalani Trust

Financial Statements and Supplemental Schedule
December 31, 2016 and 2015
Together with Independent Auditor’s Report



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, 2016 and 2015, 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 from 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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Lili'uokalani Trust as of December 31, 2016 and 2015, 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 audit of the 2016 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
August 30, 2017

Lili'uokalani Trust

Statements of Financial Position
December 31, 2016 and 2015

Assets

	<u>2016</u>	<u>2015</u>
Current Assets:		
Cash and cash equivalents	\$ 2,480,461	\$ 2,901,623
Accounts receivable, net	2,351,115	1,726,758
Investment receivable	1,223,157	4,104,007
Prepaid expenses and other assets	<u>604,080</u>	<u>870,745</u>
Total current assets	6,658,813	9,603,133
Property and Equipment, Net	36,201,663	31,058,399
Investments:		
Marketable securities	66,645,328	79,864,505
Other	156,807,264	144,353,137
Deferred Rent Receivable	<u>21,098,938</u>	<u>20,448,224</u>
Total assets	<u>\$ 287,412,006</u>	<u>\$ 285,327,398</u>

Liabilities and Net Assets

Current Liabilities:		
Accounts payable and other accrued liabilities	\$ 1,786,145	\$ 1,471,174
Accrued vacation	936,006	974,991
Deferred revenue	637,000	1,074,000
Notes payable	<u>327,637</u>	<u>319,798</u>
Total current liabilities	3,686,788	3,839,963
Accrued Postretirement Benefits	1,258,915	1,383,030
Deferred Revenue, Less Current Portion	14,496,595	13,388,966
Notes Payable, Less Current Portion	<u>11,493,819</u>	<u>11,821,815</u>
Total liabilities	<u>30,936,117</u>	<u>30,433,774</u>
Commitments and Contingencies		
Net Assets - Unrestricted	<u>256,475,889</u>	<u>254,893,624</u>
Total net assets	<u>256,475,889</u>	<u>254,893,624</u>
Total liabilities and net assets	<u>\$ 287,412,006</u>	<u>\$ 285,327,398</u>

See accompanying notes to financial statements.

Lili'uokalani Trust

Statements of Activities

For the Years Ended December 31, 2016 and 2015

	2016			2015		
	Unrestricted	Temporarily Restricted	Total	Unrestricted	Temporarily Restricted	Total
Revenues, Gains, and Other Support:						
Rent	\$ 26,650,614	\$ -	\$ 26,650,614	\$ 26,022,617	\$ -	\$ 26,022,617
Real property and general excise tax reimbursements	7,002,960	-	7,002,960	6,419,141	-	6,419,141
Donations	10,585	-	10,585	9,077	-	9,077
Net realized gains on sales and exchange of real estate	-	-	-	9,613,280	-	9,613,280
Net realized and unrealized gains on investments	3,658,256	-	3,658,256	391,533	-	391,533
Income from investments	2,934,773	-	2,934,773	3,565,674	-	3,565,674
Other	39,440	-	39,440	38,585	-	38,585
	<u>40,296,628</u>	<u>-</u>	<u>40,296,628</u>	<u>46,059,907</u>	<u>-</u>	<u>46,059,907</u>
Net assets released from restrictions	-	-	-	6,752	(6,752)	-
Total revenues, gains and other support	<u>40,296,628</u>	<u>-</u>	<u>40,296,628</u>	<u>46,066,659</u>	<u>(6,752)</u>	<u>46,059,907</u>
Expenses:						
Program services	18,737,895	-	18,737,895	16,978,579	-	16,978,579
Program support services	4,642,580	-	4,642,580	5,145,488	-	5,145,488
Endowment management services	15,520,635	-	15,520,635	14,850,689	-	14,850,689
Total expenses	<u>38,901,110</u>	<u>-</u>	<u>38,901,110</u>	<u>36,974,756</u>	<u>-</u>	<u>36,974,756</u>
Total revenues, gains and other support over expenses	1,395,518	-	1,395,518	9,091,903	(6,752)	9,085,151
Pension-Related Changes Other Than Net Periodic Pension Costs	186,747	-	186,747	399,816	-	399,816
Increase (decrease) in net assets	1,582,265	-	1,582,265	9,491,719	(6,752)	9,484,967
Net Assets at Beginning of Year	254,893,624	-	254,893,624	245,401,905	6,752	245,408,657
Net Assets at End of Year	<u>\$ 256,475,889</u>	<u>\$ -</u>	<u>\$ 256,475,889</u>	<u>\$ 254,893,624</u>	<u>\$ -</u>	<u>\$ 254,893,624</u>

See accompanying notes to financial statements.

Lili'uokalani Trust

Statements of Functional Expenses
For the Years Ended December 31, 2016 and 2015

	2016					2015				
	Program Services	Support Services			Total Expenses	Program Services	Support Services			Total Expenses
		Program Support	Endowment Management	Total			Program Support	Endowment Management	Total	
Salaries	\$ 8,711,652	\$ 2,050,475	\$ 1,398,469	\$ 3,448,944	\$ 12,160,596	\$ 7,715,993	\$ 2,180,950	\$ 970,315	\$ 3,151,265	\$ 10,867,258
Taxes	23,924	40,530	8,582,319	8,622,849	8,646,773	-	42,309	8,223,970	8,266,279	8,266,279
Financial Assistance	3,244,389	184	38	222	3,244,611	3,818,287	227	-	227	3,818,514
Employee Benefits and Payroll Taxes	2,002,229	456,526	311,360	767,886	2,770,115	2,155,493	509,887	221,924	731,811	2,887,304
Professional Services	312,826	811,072	1,228,563	2,039,635	2,352,461	11,577	784,087	1,499,780	2,283,867	2,295,444
Travel and Meals	323,202	195,399	138,845	334,244	657,446	150,167	279,619	180,802	460,421	610,588
Insurance	505,278	5,251	142,648	147,899	653,177	448,501	76,781	129,711	206,492	654,993
Repairs and Maintenance	610,998	19,586	17,661	37,247	648,245	498,070	114,741	15,725	130,466	628,536
Occupancy Expense	192,447	185,302	202,256	387,558	580,005	156,253	115,648	168,289	283,937	440,190
Trustees' Fees	-	282,375	282,375	564,750	564,750	-	260,750	260,750	521,500	521,500
Utilities	447,924	18,821	14,367	33,188	481,112	352,657	134,200	18,225	152,425	505,082
General Real Estate Expenses	-	14,058	392,856	406,914	406,914	-	-	377,959	377,959	377,959
Supplies	175,520	57,687	107,430	165,117	340,637	217,659	131,302	47,800	179,102	396,761
Telephone	248,071	6,609	56,991	63,600	311,671	221,936	38,166	21,827	59,993	281,929
Equipment Rental	115,984	69,576	42,215	111,791	227,775	95,449	19,818	16,726	36,544	131,993
Education	56,089	65,134	16,014	81,148	137,237	47,088	71,342	-	71,342	118,430
Real Estate Management Fees	-	-	105,624	105,624	105,624	-	-	105,624	105,624	105,624
Dues	20,426	12,672	25,409	38,081	58,507	5,209	21,410	13,396	34,806	40,015
Leasing Commission	-	-	45,440	45,440	45,440	-	-	46,657	46,657	46,657
Bad Debt Expense	-	-	44,425	44,425	44,425	-	-	54,407	54,407	54,407
Publications	6,113	5,238	10,105	15,343	21,456	2,039	768	2,005	2,773	4,812
Other Expenses	184,826	152,940	720,872	873,812	1,058,638	63,591	170,138	166,630	336,768	400,359
Total expenses before impairment, depreciation and amortization	17,181,898	4,449,435	13,886,282	18,335,717	35,517,615	15,959,969	4,952,143	12,542,522	17,494,665	33,454,634
Loss on Impairment of Property and Equipment	-	-	-	-	-	-	-	466,527	466,527	466,527
Depreciation and Amortization	1,555,997	193,145	1,634,353	1,827,498	3,383,495	1,018,610	193,345	1,841,640	2,034,985	3,053,595
Total	\$ 18,737,895	\$ 4,642,580	\$ 15,520,635	\$ 20,163,215	\$ 38,901,110	\$ 16,978,579	\$ 5,145,488	\$ 14,850,689	\$ 19,996,177	\$ 36,974,756

See accompanying notes to the financial statements.

Lili'uokalani Trust

Statements of Cash Flows

For the Years Ended December 31, 2016 and 2015

	<u>2016</u>	<u>2015</u>
Cash Flows from Operating Activities:		
Cash received from customers	\$ 37,153,139	\$ 31,997,980
Cash paid to suppliers for goods and services	(22,938,483)	(23,599,815)
Cash paid to employees for services	(12,160,596)	(10,767,316)
Net investment income received	2,934,773	3,565,674
Other cash receipts	236,773	447,479
Net cash provided by operating activities	<u>5,225,606</u>	<u>1,644,002</u>
Cash Flows from Investing Activities:		
Proceeds from the sales or maturities of marketable securities and other	47,741,476	37,117,555
Purchase of marketable securities and other	(32,935,728)	(34,718,957)
Proceeds from the sales or maturities of limited partnership interests	15,548,953	15,511,715
Purchases of limited partnership interests	(26,373,748)	(25,862,811)
Proceeds from the sales of real estate	-	9,721,831
Purchases of real estate	(3,128,940)	(2,323,324)
Purchases of property and equipment	(6,178,624)	(6,835,503)
Net cash used in investing activities	<u>(5,326,611)</u>	<u>(7,389,494)</u>
Cash Flows from Financing Activities:		
Repayment of notes payable	(320,157)	(203,144)
Proceeds from note payable	-	5,500,000
Net cash (used in) provided by financing activities	<u>(320,157)</u>	<u>5,296,856</u>
Net decrease in cash	(421,162)	(448,636)
Cash and Cash Equivalents at Beginning of Year	<u>2,901,623</u>	<u>3,350,259</u>
Cash and Cash Equivalents at End of Year	<u>\$ 2,480,461</u>	<u>\$ 2,901,623</u>

See accompanying notes to financial statements.

Lili'uokalani Trust

Statements of Cash Flows

For the Years Ended December 31, 2016 and 2015

	<u>2016</u>	<u>2015</u>
Reconciliation of Cash Flows from Operating Activities:		
Increase in net assets	\$ 1,582,265	\$ 9,484,967
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Net realized gains on sales and exchange of real estate	-	(9,613,280)
Net realized and unrealized gains on investments	(3,658,256)	(391,533)
Loss on impairment of property and equipment	-	466,527
Depreciation and amortization	3,383,495	3,053,595
Increase in accounts receivable	(624,356)	(144,273)
Decrease in investment receivable	4,104,007	-
Decrease (increase) in prepaid expenses and other assets	266,665	(132,033)
Increase in deferred rent receivable	(650,714)	(157,143)
Increase (decrease) in accounts payable and other accrued liabilities	314,971	(529,510)
(Decrease) increase in accrued vacation	(38,985)	35,696
Increase (decrease) in deferred revenue	670,629	(142,361)
Decrease in accrued postretirement benefits	(124,115)	(286,650)
Net cash provided by operating activities	<u>\$ 5,225,606</u>	<u>\$ 1,644,002</u>

See accompanying notes to financial statements.

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

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. The Trust has no temporarily restricted net assets.
- **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, investments, and accrued postretirement benefits. Actual results could differ from those estimates.

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

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 2016 and 2015, 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 \$2,673,000 and \$3,092,000 in excess of federally insured limits at December 31, 2016 and 2015, 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 consists of amounts due primarily from 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, 2016 and 2015, management's estimated allowance was approximately \$155,000 and \$133,000, respectively.

g. Investment Receivable

Investment receivable consists of amounts redeemed, but not yet received from investment managers on December 31.

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

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

h. 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.

i. 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 20-40 years
Land improvements	30-40 years

j. Investments

Investments include marketable securities, non-controlling interests in for-profit limited partnerships, and real estate. Investments in marketable securities consist of mutual funds, equity securities and U.S. treasuries 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.

k. 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.

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

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

l. 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.

m. Employee Benefit Plans

The Trust accounts for its postretirement benefit plan 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.

n. 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.

o. 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.

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

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

p. Recent Accounting Pronouncement

In January 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-01, *Financial Instruments – Overall: Recognition and Measurement of Financial Assets and Financial Liabilities*. This ASU requires equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. This ASU will be effective beginning after December 15, 2018. Management is currently assessing the impact of this ASU on its financial position and results of operations and has not yet determined if the adoption of this ASU will have a material effect on its financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*. This ASU replaces the existing lease guidance in U.S. GAAP with new guidance applicable to both lessees and lessors and requires lessees to recognize right-of-use assets and lease liabilities for all leases other than those that meet the definition of short-term leases at the commencement date of the lease. A right-of-use asset is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. A lease liability is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis. The standard also requires additional quantitative and qualitative disclosures regarding the amount, timing and uncertainty of cash flows arising from leases. This ASU will be effective beginning after December 15, 2019. Management is currently assessing the impact of this ASU on its financial position and results of operations and has not yet determined if the adoption of this ASU will have a material effect on its financial statements.

In August 2016, the FASB issued ASU No. 2016-14, *Not-for-Profit Entities: Presentation of Financial Statements of Not-for-Profit Entities*. This ASU changes presentation and disclosure requirements for not-for profit entities to provide more relevant information about their resources (and the changes in those resources) to donors, grantors, creditors, and other users. These include qualitative and quantitative requirements in net asset classes, investment return, expenses, liquidity and availability of resources and presentation of operating cash flow. This ASU will be effective beginning after December 15, 2018. Management is currently assessing the impact of this ASU on its financial position and results of operations and has not yet determined if the adoption of this ASU will have a material effect on its financial statements.

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

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

q. Subsequent Events

The Trust has evaluated subsequent events through August 30, 2017, the date the financial statements were available to be issued, and it was determined that all subsequent events had been properly accounted for.

2. Investments

a. Marketable Securities

Marketable securities stated at fair value at December 31, 2016 and 2015 were as follows:

	<u>Fair Value</u>	<u>Cost</u>	<u>Net Unrealized Gains/(Losses)</u>
2016:			
Mutual funds	\$ 47,596,719	\$ 46,436,567	\$ 1,160,152
U.S. treasuries	10,031,998	10,243,219	(211,221)
Equity securities	8,929,658	6,371,236	2,558,422
Other	86,953	86,953	-
	<u>\$ 66,645,328</u>	<u>\$ 63,137,975</u>	<u>\$ 3,507,353</u>
2015:			
Mutual funds	\$ 57,642,652	\$ 59,103,787	\$ (1,461,135)
U.S. treasuries	13,506,309	13,641,079	(134,770)
Equity securities	8,633,587	6,016,239	2,617,348
Other	81,957	81,957	-
	<u>\$ 79,864,505</u>	<u>\$ 78,843,062</u>	<u>\$ 1,021,443</u>

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

2. Investments (continued)

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.

At December 31, 2016 and 2015, the cost and fair value of other investments were as follows:

	Cost	Fair Value (Unaudited)	Fair Value Over/(Under) Cost (Unaudited)
2016:			
Investment in real estate	\$ 42,649,704	\$ 552,896,805	\$ 510,247,101
Investment in for-profit limited partnerships	114,157,560	129,658,406	15,500,846
Total	<u>\$ 156,807,264</u>	<u>\$ 682,555,211</u>	<u>\$ 525,747,947</u>
2015:			
Investment in real estate	\$ 41,868,474	\$ 551,060,501	\$ 509,192,027
Investment in for-profit limited partnerships	102,484,663	109,930,454	7,445,791
Total	<u>\$ 144,353,137</u>	<u>\$ 660,990,955</u>	<u>\$ 516,637,818</u>

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, 2016 and 2015, the Trust had outstanding funding commitments of approximately \$11,798,000 and \$8,461,000, respectively.

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

2. Investments (continued)

b. Other Investments (continued)

Investment in real estate at December 31, 2016 and 2015 consisted of the following:

	Use	Held for Sale	Development	Total
2016:				
Land	\$ 1,001,525	\$ 532,720	\$ 224,120	\$ 1,758,365
Building and improvements	45,121,334	-	-	45,121,334
	46,122,859	532,720	224,120	46,879,699
Accumulated depreciation and amortization	(21,904,247)	-	-	(21,904,247)
	24,218,612	532,720	224,120	24,975,452
Construction in progress (see Note 8)	-	-	17,674,252	17,674,252
Investment in real estate, net	<u>\$ 24,218,612</u>	<u>\$ 532,720</u>	<u>\$ 17,898,372</u>	<u>\$ 42,649,704</u>
2015:				
Land	\$ 1,001,525	\$ 532,720	\$ 224,120	\$ 1,758,365
Building and improvements	45,050,062	-	-	45,050,062
	46,051,587	532,720	224,120	46,808,427
Accumulated depreciation and amortization	(20,353,837)	-	-	(20,353,837)
	25,697,750	532,720	224,120	26,454,590
Construction in progress (see Note 8)	-	-	15,413,884	15,413,884
Investment in real estate, net	<u>\$ 25,697,750</u>	<u>\$ 532,720</u>	<u>\$ 15,638,004</u>	<u>\$ 41,868,474</u>

Real estate held for use primarily represents property that the Trust leases to third parties under long-term non-cancelable leases (see Note 7).

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

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

2. Investments (continued)

b. Other Investments (continued)

For the year ended December 31, 2015, the Trust received proceeds of approximately \$9,722,000 and recognized a gain of approximately \$9,613,000, related to the sale of its interest in the land under certain condominiums. In 2016, the Trust did not sell any of its interests in the land under the condominiums.

Real estate held for development includes land acquisition costs, initial planning costs and capitalized interest related to various parcels of land in Kona. For the years ended December 31, 2016 and 2015, the Trust capitalized approximately \$390,000 and \$237,000 of interest costs, respectively.

3. Property and Equipment

Property and equipment at December 31, 2016 and 2015 consisted of the following:

	2016	2015
Land	\$ 8,693,589	\$ 8,693,589
Building and improvements	40,541,785	35,892,784
Furniture, fixtures and equipment	6,086,848	5,558,237
	55,322,222	50,144,610
Accumulated depreciation and amortization	(21,581,966)	(19,748,881)
	33,740,256	30,395,729
Construction in progress (see Note 8)	2,461,407	662,670
Property and equipment, net	\$ 36,201,663	\$ 31,058,399

For the years ended December 31, 2016 and 2015, the Trust capitalized approximately \$18,000 and \$3,000 of interest costs, respectively.

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

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.

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.

U.S. treasuries 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, 2016 and 2015.

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

4. Fair Value Measurements (continued)

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.

The following table sets forth the Trust's investments by type of fund based on Level 1 inputs as of December 31, 2016 and 2015:

	2016	2015
Mutual funds:		
Foreign large blend	\$ 13,096,063	\$ 10,617,130
Large blend	10,229,777	13,319,619
Foreign small/mid value	7,064,700	6,870,925
Diversified emerging markets	5,433,094	4,533,569
Money market funds	4,866,405	11,240,015
Large growth	4,836,734	7,828,285
Precious metals	2,069,946	-
Natural resources	-	1,859,040
Equity resources	-	1,374,069
Total mutual funds	<u>47,596,719</u>	<u>57,642,652</u>
Equity securities:		
Consumer goods	5,720,699	5,943,157
Financial	1,770,626	1,536,905
Services	837,187	798,711
Industrial goods	286,881	192,578
Consumer entertainment	198,519	162,236
Other	115,746	-
Total equity securities	<u>8,929,658</u>	<u>8,633,587</u>
U.S. treasuries	10,031,998	13,506,309
Other	86,953	81,957
Total investments at fair value	<u>\$ 66,645,328</u>	<u>\$ 79,864,505</u>

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

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, 2016 and 2015, the carrying amount of notes payable was approximately \$11,821,000 and \$12,142,000, 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. 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 matched 100 percent of employee contributions up to the first 4 percent of included compensation, plus 50 percent of employee contributions up to the next 2 percent of included compensation.

Expenses related to the 401(k) plan totaled approximately \$504,900 and \$500,000 for the years ended December 31, 2016 and 2015, respectively.

b. 457(b) Plan

Effective September 2013, the Trust established a non-qualified deferred compensation plan called the Queen Lili'uokalani Trust 457(b) Plan, covering a select group of eligible employees and independent contractors of the Trust. Participants can defer a portion of their compensation up to the IRS limit and have the funds invested tax deferred.

Expenses related to the 457(b) plan totaled approximately \$3,700 and \$3,300 for the years ended December 31, 2016 and 2015, respectively.

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

5. Employee Benefit Plans (continued)

c. Postretirement Benefit Plan (continued)

The Trust 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.

The changes in the obligations and assets of the Trust's postretirement benefit plan and the changes in unrestricted net assets for 2016 and 2015 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:

	<u>2016</u>	<u>2015</u>
Benefit obligation, beginning of year	\$ 1,383,030	\$ 1,669,680
Service cost	52,299	67,300
Interest cost	60,368	68,476
Plan amendments	-	(289,010)
Actuarial (gain) loss	(215,155)	(94,090)
Benefits paid	<u>(21,627)</u>	<u>(39,326)</u>
Benefit obligation, end of year	<u>1,258,915</u>	<u>1,383,030</u>
Fair value of plan assets, beginning of year		
Employer contribution	21,627	39,326
Benefits paid	<u>(21,627)</u>	<u>(39,326)</u>
Fair value of plan assets, end of year	<u>-</u>	<u>-</u>
Accrued postretirement benefit liability	<u>\$ (1,258,915)</u>	<u>\$ (1,383,030)</u>
Change in net periodic benefit cost not yet recognized:		
Beginning of year	\$ 483,084	\$ 83,268
Current year	<u>186,747</u>	<u>399,816</u>
Current net periodic benefit cost not yet recognized	<u>\$ 669,831</u>	<u>\$ 483,084</u>

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

5. Employee Benefit Plans (continued)

c. Postretirement Benefit Plan (continued)

The components of net periodic benefit cost were as follows:

	2016	2015
Service cost	\$ 52,299	\$ 67,300
Interest cost	60,368	68,476
Amortization of unrecognized net transition obligation	(28,408)	16,716
Net periodic benefit cost	<u>\$ 84,259</u>	<u>\$ 152,492</u>

The prior service costs that will be amortized into net periodic benefit cost in 2017 are approximately \$45,000.

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

	2016	2015
Benefit obligation:		
Discount rate	4.12%	4.44%
Expected long-term rate of return on plan assets	n/a	n/a
Health care trend rates	7% - 5%	7.25% - 5%
Year of ultimate trend	2025	2025
Net periodic benefit cost (years ended):		
Discount rate	4.44%	4.15%
Expected long-term rate of return on plan assets	n/a	n/a
Health care trend rates	7.25% - 5%	7.5% - 5%
Year of ultimate trend	2025	2025

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

5. Employee Benefit Plans (continued)

c. Postretirement Benefit Plan (continued)

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

Years ending December 31,	
2017	\$ 42,074
2018	52,691
2019	54,364
2020	64,843
2021	68,365
2022 – 2026	426,419

The Trust expects to contribute approximately \$42,000 to its postretirement benefit plan in 2016.

Assumed health care cost trend rates could have a significant effect on the amounts reported for the post-retirement medical plan. A one percentage point change in assumed health care cost trend rates would have the following effects:

	<u>1% increase</u>	<u>1% decrease</u>
Post-retirement benefit obligation	\$ 45,976	\$ (39,926)
Total service and interest cost	7,354	(6,098)

6. Notes Payable

In 2004, the Trust entered into a commercial 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. In 2012, the Trust amended the loan agreement to extend and amend the terms of the loan. The loan interest rate decreased from 5.31 percent to 3.23 percent and the required monthly principal and interest payments decreased from \$7,836 to \$5,178. The maturity date of the loan was extended to July 1, 2022. There was a balance of approximately \$929,000 and \$961,000 outstanding on the loan at December 31, 2016, and 2015, respectively.

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

6. Notes Payable (continued)

In 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, which was completed in 2012. 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 \$4,385,000 and \$4,532,000 outstanding on the loan at December 31, 2016, and 2015, respectively.

In 2013, the Trust entered into a commercial term loan agreement with the aforementioned bank in the amount of \$1,210,000 to retire the remaining balance on an original 2008 loan used to finance the purchase of the Wili Pa Loop property and related improvements for the Maui Children's Center. The loan matures on November 8, 2023, bears interest at 4.10 percent and requires the Trust to make monthly principal and interest payments of \$6,455. At December 31, 2016 and 2015, the loans had outstanding balances of approximately \$1,118,000 and \$1,149,000, respectively.

On December 4, 2015, the Trust entered into a \$5,500,000 commercial term loan agreement with the aforementioned bank to finance the acquisition of its Kapolei Children's Center. The loan matures on December 8, 2025, bears interest at 3.45 percent and requires the Trust to make monthly principal and interest payments of \$24,544. There was a balance of approximately \$5,390,000 and \$5,500,000 outstanding on the loan at December 31, 2016 and 2015, respectively.

The Trust also has a line of credit with the aforementioned bank in the amount of \$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 0.75 percent or the bank's base rate minus a margin of 0.75 percent with a minimum interest rate not less than 1.75 percent, and expires in October 2017. As of December 31, 2016 and 2015, there were no outstanding draws on the line of credit.

All loans, including any outstanding line of credit draws, are secured by approximately \$25 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 agreements. The Trust was in compliance with these requirements as of December 31, 2016.

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

6. Notes Payable (continued)

The approximate annual principal payments on notes payable at December 31, 2016 were as follows:

For the years ending	
December 31,	
2017	\$ 328,000
2018	339,000
2019	350,000
2020	362,000
2021	375,000
Thereafter	<u>10,067,000</u>
	<u>\$ 11,821,000</u>

7. 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 long-term non-cancelable operating leases as of December 31, 2016 were approximately as follows:

For the years ending	
December 31,	
2017	\$ 21,437,000
2018	21,021,000
2019	21,035,000
2020	20,840,000
2021	20,731,000
Thereafter	<u>882,703,000</u>
Total	<u>\$ 987,767,000</u>

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, 2016 and 2015, amounted to approximately \$3,401,000 and \$3,429,000, respectively.

Lili'uokalani Trust

Notes to Financial Statements
December 31, 2016 and 2015

8. Commitments

The Trust entered into contracts with various third parties related to its development projects and construction in progress. At December 31, 2016, these contracts totaled approximately \$9,947,000, of which the Trust had incurred approximately \$7,444,000 as of December 31, 2016.

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. As of December 31, 2016, no claim was requested related to the promissory note.

Supplementary Information

Lili'uokalani Trust

Supplemental Schedule of Land
December 31, 2016

	<u>Cost Basis</u>	<u>Appraisal Basis (Unaudited)</u>
Investment Land:		
Oahu:		
Waikiki	\$ 1,124,245	\$ 360,231,274
Other Oahu	247,791	13,157,200
Hawaii:		
Kona:		
Developed	49,331	84,584,450
Undeveloped	224,120	61,822,250
Leased for agriculture	112,877	2,450,800
Other Hawaii	1	5,392,800
Total investment land	<u>1,758,365</u>	<u>527,638,774</u>
Land Used for Tax Exempt Purposes --		
Children's Centers:		
Hilo	302,816	580,000
Kona	1	377,300
Kaneohe	703,316	670,000
Kapalama	217,160	2,880,000
Kauai	966,857	780,000
Kapolei*	5,105,614	5,105,614
Maui	883,190	930,000
Punaluu	1	3,638,400
Waianae	514,634	630,000
Total land used for tax exempt purposes	<u>8,693,589</u>	<u>15,591,314</u>
Total land	<u>\$ 10,451,954</u>	<u>\$ 543,230,088</u>

Note: The supplemental "appraisal basis" value of land is stated primarily at the estimated market value on January 1, 2015 as appraised by John Child & Company, in its report dated November 12, 2015. 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.

*The Kapolei Children Center was not included in the appraisal described in the note above as the purchase was made in December 2015. As such, the "appraisal basis" value is based on the purchase price.

See accompanying independent auditor's report.