KAMEHAMEHA SCHOOLS AND SUBSIDIARIES

Consolidated Financial Statements and Supplemental Schedules

June 30, 2006 and 2005

(With Independent Auditors' Report Thereon)

KAMEHAMEHA SCHOOLS
AND SUBSIDIARIES

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Independent Auditors' Report

The Board of Trustees
Kamehameha Schools:

We have audited the accompanying consolidated balance sheets of Kamehameha Schools and subsidiaries as of June 30, 2006 and 2005, and the related consolidated statements of activities and cash flows for the years then ended. These consolidated financial statements are the responsibility of Kamehameha Schools' management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of Kamehameha Schools and subsidiaries' internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Kamehameha Schools and subsidiaries as of June 30, 2006 and 2005, and the changes in their net assets and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Our audits for the years ended June 30, 2006 and 2005 were made for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The supplementary information included in schedules 1 and 2 for the years ended June 30, 2006 and 2005 is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information has been subjected to the auditing procedures applied in the audits of the consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the consolidated financial statements taken as a whole for the years ended June 30, 2006 and 2005.

As described in note 1(e), Kamehameha Schools changed its method for accounting for certain investments that do not have readily determinable fair values and adopted a policy of reporting these investments at fair value in accordance with the *AICPA Audit and Accounting Guide, Not-for-Profit Organizations* as of July 1, 2005. The cumulative effect of this change in accounting principle as of July 1, 2005 and the fair value of these investments at June 30, 2006 have been estimated by management in the absence of readily determinable fair values. Management's estimates are based on information provided by the fund managers or the general partners.

KPMG LLP, a U.S. limited liability partnership, is the U.S.
member firm of KPMG International, a Swiss cooperative.

We have also previously audited, in accordance with auditing standards generally accepted in the United States of America, the consolidated balance sheets of Kamehameha Schools and subsidiaries as of June 30, 2004, 2003, 2002, 2001, and 2000 and the related consolidated statements of activities and cash flows for the years then ended (none of which is presented herein), and we expressed unqualified opinions on those consolidated financial statements. The supplementary information included in schedules 1 and 2 of Kamehameha Schools and subsidiaries' 2004, 2003, 2002, 2001, and 2000 consolidated financial statements was subjected to auditing procedures applied in the audits of those consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the consolidated financial statements from which it has been derived.

KPMG LLP

October 24, 2006

KAMEHAMEHA SCHOOLS
AND SUBSIDIARIES

Consolidated Balance Sheets

June 30, 2006 and 2005

(In thousands)

Assets		**2006**	**2005**
Cash and cash equivalents	$	50,498	64,956
Investments (notes 2 and 11)		5,675,829	4,860,735
Collateral received for loaned securities (note 2)		466,038	386,352
Receivables, net (note 3)		18,581	19,769
Property and equipment, net (note 4)		750,437	725,272
Real estate held for development and sale (note 5)		29,089	34,148
Deferred charges and other		80,017	51,723
Total assets	$	7,070,489	6,142,955
Liabilities and Net Assets			
Notes payable (note 6)	$	243,020	244,880
Obligation to repay securities lending collateral (note 2)		466,038	386,352
Accounts payable and accrued expenses		71,064	60,119
Income taxes payable (note 7)		13,734	31,794
Accrued pension liability (note 8)		47,832	48,684
Accrued postretirement benefits (note 8)		23,465	22,223
Deferred compensation payable (note 9)		9,276	9,489
Deferred income and other		17,754	19,781
Total liabilities		892,183	823,322
Net assets – unrestricted		6,178,306	5,319,633
Commitments and contingencies (notes 2, 6, 7, 8, 9, and 12)			
Total liabilities and net assets	$	7,070,489	6,142,955

See accompanying notes to consolidated financial statements.

KAMEHAMEHA SCHOOLS
AND SUBSIDIARIES

Consolidated Statements of Activities

Years ended June 30, 2006 and 2005

(In thousands)

		2006	2005
Revenues, gains, and other support:			
Tuition and fees	$	20,917	16,835
Less financial aid		(9,198)	(7,438)
Net tuition and fees		11,719	9,397
Net realized and unrealized gains on investments (note 2)		559,685	482,069
Rental (note 12)		159,392	142,114
Investment income, net (note 2)		112,916	80,702
Net gain on property sales (note 10)		183,273	120,330
Other		2,545	2,569
Total revenues, gains, and other support		1,029,530	837,181
Expenses:			
Educational programs		190,592	176,366
Management and general:			
Rental		66,194	63,273
Other (notes 6, 7, and 12)		50,854	73,003
Total expenses		307,640	312,642
Change in net assets before cumulative effect of a change in accounting principle		721,890	524,539
Cumulative effect on prior years (to June 30, 2005) of changing to fair value accounting for investments (note 1)		136,783	—
Change in net assets		858,673	524,539
Net assets at beginning of year		5,319,633	4,795,094
Net assets at end of year	$	6,178,306	5,319,633
Pro forma amounts assuming fair value accounting for investments is applied retroactively:			
Change in net assets	$	721,890	546,797

See accompanying notes to consolidated financial statements.

KAMEHAMEHA SCHOOLS
AND SUBSIDIARIES

Consolidated Statements of Cash Flows

Years ended June 30, 2006 and 2005

(In thousands)

	2006	2005
Cash flows from operating activities:		
Change in net assets	$ 858,673	524,539
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Depreciation and amortization	36,606	34,462
Earnings in investee companies	—	(8,411)
Net realized and unrealized gains on investments	(559,685)	(482,069)
Net gain on property sales	(183,273)	(120,330)
Cumulative effect of change in accounting principle	(136,783)	—
Changes in operating assets and liabilities:		
Decrease (increase) in receivables, net	1,188	(686)
Increase in real estate held for development and sale	(1,476)	(3,200)
Increase in deferred charges and other	(28,294)	(6,435)
Increase (decrease) in accounts payable, accrued expenses, and other liabilities	9,095	(11,569)
Increase (decrease) in income taxes payable	(18,060)	7,092
Other	(2,693)	(962)
Net cash used in operating activities	(24,702)	(67,569)
Cash flows from investing activities:		
Proceeds from property sales	200,381	140,047
Proceeds from sales of investments	13,160,336	9,959,738
Purchases of investments	(13,276,269)	(9,959,393)
Purchases of property and equipment	(72,344)	(49,194)
Net cash provided by investing activities	12,104	91,198
Cash flows from financing activities:		
Proceeds from borrowings	10,000	—
Repayment of borrowings	(11,860)	(11,835)
Net cash used in financing activities	(1,860)	(11,835)
Net increase (decrease) in cash and cash equivalents	(14,458)	11,794
Cash and cash equivalents at beginning of year	64,956	53,162
Cash and cash equivalents at end of year	$ 50,498	64,956
Supplemental disclosure of cash flow information:		
Income taxes paid	$ 4,687	1,430
Interest paid	13,394	13,918
Supplemental disclosure of noncash investing activities:		
Transfer of property and equipment, net to real estate held for development and sale	$ 630	5,548

See accompanying notes to consolidated financial statements.

(1) Summary of Significant Accounting Policies and Practices

(a) Description of the Organization

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

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

(b) Principles of Consolidation

The consolidated financial statements include the accounts of the Schools, Bishop Holdings Corporation (BHC), Ke Ali'i Pauahi Foundation (KAPF), and Newport Kohala, LLC.

The consolidated financial statements of BHC include the accounts of:

- Pauahi Management Corporation (PMC) and its wholly owned subsidiaries – KDP, Limited; KBH, Inc.; VCI, Inc.; Lake Manassas Limited Liability Company; RTJ Limited Liability Company; and Paradise Petroleum, Inc. dba Ali'i Petroleum
- P&C Insurance Company, Inc.
- Kamehameha Investment Corporation and its wholly owned subsidiaries – Keauhou Community Services, Inc.; Paki, Inc.; Keauhou Resort Development Corporation and its investment in Keauhou Kona Resort Company.

BHC is a taxable holding corporation with subsidiaries primarily involved in property investment and management. The subsidiaries develop and sell real estate, maintain investments in equity and debt instruments, and own and operate a golf course. A subsidiary also owned and operated a hotel until it was sold in September 2004.

P&C Insurance Company, Inc., a wholly owned subsidiary of BHC, is a captive insurance company that provides property and liability coverage for the Schools and its affiliates.

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

In addition to the above, under U.S. generally accepted accounting principles, certain investments may be considered as entities for consolidation should they meet specified criteria. As of June 30, 2006 and 2005, Newport Kohala, LLC met these criteria. Newport Kohala, LLC is a single-member limited liability company formed exclusively to execute the Schools' absolute return investment strategies and is managed by an independent investment management firm.

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

(c) Basis of Financial Statement Presentation

The Schools' consolidated financial statements have been prepared on the accrual basis of accounting, and are presented in conformity with U.S. generally accepted accounting principles. Net assets, revenues, gains and other support, and expenses are classified based on the existence or absence of donor-imposed restrictions. KAPF's temporarily and permanently restricted net assets amounted to $9.3 million and $9.1 million at June 30, 2006 and 2005, respectively. As the amounts are not significant, all net assets of the Schools and changes therein are classified and reported as unrestricted net assets.

(d) Cash Equivalents

Cash equivalents are held in financial institutions located in the state of Hawaii and other states, and an investment company. For purposes of the consolidated statements of cash flows, the Schools consider all highly liquid debt instruments with original maturities of three months or less to be cash equivalents. The Schools' net cash balances maintained in excess of available depository insurance limits amounted to approximately $9.7 million and $9.4 million at June 30, 2006 and 2005, respectively.

(e) Investments

Marketable Debt and Equity Securities – The Schools and KAPF

Debt and equity securities with readily determinable fair values are reported at fair value with unrealized gains and losses included in the consolidated statements of activities. Fair value is based on quoted market prices and, if applicable, discounted for restrictions on the sale of shares.

Marketable Debt and Equity Securities – BHC

Debt and equity securities are classified in one of three categories: trading, held-to-maturity, or available-for-sale. Trading securities are bought and held principally for the purpose of selling them in the near term. Held-to-maturity securities are those securities in which BHC has the ability and intent to hold the security until maturity. All securities not included in trading or held-to-maturity are classified as available-for-sale.

Trading and available-for-sale securities are recorded at fair value. Held-to-maturity securities are recorded at amortized cost, adjusted for the amortization or accretion of premiums or discounts. Unrealized and realized gains and losses on trading securities are included in earnings. Unrealized holding gains and losses, net of the related tax effect, on available-for-sale securities are excluded from earnings and are included in net assets - unrestricted in the accompanying consolidated balance sheets. Realized gains and losses from the sale of available-for-sale securities are determined on a specific-identification basis.

At June 30, 2006 and 2005, debt and equity securities were classified as available-for-sale and were reported at amounts which approximate fair value.

A decline in the market value of any available-for-sale security below cost that is deemed to be other-than-temporary results in a reduction in carrying amount to fair value. The impairment is charged to earnings and a new cost basis for the security is established. To determine whether an impairment is other-than-temporary, BHC considers whether it has the ability and intent to hold the investment until a market price recovery and considers whether evidence indicating the cost of the investment is recoverable outweighs evidence to the contrary. Evidence considered in this assessment includes the reasons for the impairment, the severity and duration of the impairment, changes in value subsequent to year end and forecasted performance of the investee. Premiums and discounts are amortized or accreted over the life of the related held-to-maturity investment as an adjustment to yield using the effective-interest method. Dividend and interest income are recognized when earned.

Other Investments

Effective July 1, 2005, the Schools changed its accounting policy for other investments to the fair value method rather than the previous policy of equity or cost method. Other investments include limited partnerships, hedge funds and other equity securities that do not have a readily determinable fair value. The Schools changed accounting methods as management believes that fair values provide a more relevant measure of the ability of the Schools' assets to support current and future operations, better information for measuring investment performance and fair value accounting is the predominant industry practice. The Schools recognized an increase in net assets of $136.8 million, which is presented as a cumulative effect of a change in accounting principle as of July 1, 2005 in the accompanying consolidated statements of activities.

Unrealized gains and losses on other investments are included in the consolidated statement of activities. Fair value is generally based on information provided by the respective external investment managers at the most recent valuation date and adjusted for cash flows from the valuation date to fiscal year end, if applicable. These valuations involve assumptions and methods that are reviewed by management. Because other investments are not readily marketable, their estimated value is subject to uncertainty and therefore may differ from the value that would have been used had a ready market for such investment existed.

For the year ended June 30, 2005 and prior, investments in which the Schools owned 20% to 50% of the equity interest (5% to 50% for partnership investments) were accounted for primarily on the equity method. Certain limited partnership investments for which the Schools have in excess of 50% interest but did not have control were also accounted for on the equity method. Other investments in which the Schools had no significant influence were accounted for at cost.

A decline in the fair value of any other investments below cost that was deemed to be other-than-temporary resulted in a reduction in carrying amount to fair value. The impairment was charged to earnings and a new cost basis for the investment was established.

(f) Receivables

Notes receivable consist primarily of receivables from the sale of residential leasehold lots to lessees under the single-family and multifamily residential land sales program, mortgage agreements from the sale of real estate to developers, and interest earned. The residential leasehold interests were sold under various collateralized financing arrangements with 12- to 15-year terms and monthly payments of both principal and interest or interest only. Annual interest rates range from 7% to 10% with a weighted average interest rate of approximately 7% at June 30, 2006 and 2005. The sale of leasehold lots under the financing arrangements is accounted for using the cost-recovery method whereby no profit is recognized until cash payments are received.

(g) Property and Equipment

Property and equipment are stated at cost. Depreciation on property and equipment is calculated on the straight-line method over the estimated useful lives of the assets. The estimated useful life of buildings and improvements is 30 years, land improvements is 30 years, and equipment is 5 to 10 years.

(h) Real Estate Held for Development and Sale

Real estate assets held for development and sale are stated at cost, net of any write-downs. Cost includes land acquisition and holding costs, site development, construction, and other project related costs. In accordance with Statement of Financial Accounting Standards (SFAS) No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets,* management uses estimated expected future net cash flows (undiscounted and excluding interest costs) to measure the recoverability of real estate assets held for development. The recoverability of real estate assets held for sale is determined by comparing appraised value or the net present value of the estimated expected future cash flows (using a discount rate commensurate with the risks involved) to the carrying amount of the asset. The estimate of expected future net cash flows is inherently uncertain and relies to a considerable extent on assumptions regarding current and future economic conditions. If, in future periods, there are changes in estimates or assumptions, the changes could result in an adjustment to the carrying amount of real estate.

Profit on sales of real estate is recognized when title has passed, minimum down payment criterion is met, the terms of any note received are such as to satisfy continuing investment requirements and collectibility of the note is reasonably assured, the risks and rewards of ownership have been transferred to the buyer, and there is no substantial continuing involvement with the property. If any of the aforementioned criteria are not met, profit is deferred and recognized under either the installment, cost recovery, deposit, or percentage-of-completion method. Costs are charged to cost of sales on the basis of the relative sales value of the units sold to the total sales value of all units in the project.

(i) Vacation

Professional teaching employees are employed under one-year contracts for school years ending in mid-August. School years comprise a "teaching period" from mid-August to mid-June and a "professional improvement period" for the balance of the year. Vacations for these employees are provided during the professional improvement period.

Substantially all the Schools' employees, except for professional teaching employees, earn vacation benefits and are entitled to receive payments for unused vacation benefits based upon their regular salary at the time of their termination of employment.

(j) Employee Benefits and Postretirement Plans

The Schools have a defined benefit pension plan covering substantially all of its employees. The benefits are based on years of service and the employee's compensation. The cost of this program is being funded currently.

The Schools also sponsor a defined benefit health care plan for substantially all retirees and employees. The Schools measure the costs of its obligation based on its best estimate. The net periodic costs are recognized as employees render the services necessary to earn the postretirement benefits.

The Schools and BHC have employee savings and profit sharing plans under Section 403(b) and Section 401(k) of the Internal Revenue Code. The plans cover substantially all the Schools' and BHC's employees after satisfying service requirements. Participating employees may defer up to 20% and 50% (subject to certain limitations) of their pretax earnings for Section 403(b) and Section 401(k) plans, respectively. Effective July 1, 2002, the Schools commenced employer contributions up to a maximum of 3% of pretax employee earnings.

(k) Deferred Income

Deferred income consists primarily of prepaid lease rents, which are deferred and recognized as income ratably over the fixed term of the respective leases.

(l) Income Taxes

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

Income taxes for BHC are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. BHC utilizes the percentage method of allocating its consolidated tax liability among the entities of the BHC consolidated group.

(m) Use of Estimates

The preparation of the consolidated financial statements requires management of the Schools to make a number of estimates and assumptions relating to the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the period. Significant items subject to such estimates and assumptions include the carrying amounts of property and equipment and real estate held for development and sale; valuation allowances for receivables, investments, and deferred income tax assets; and assets and obligations related to employee benefits. Actual results could differ from those estimates.

(n) Impairment of Long-Lived Assets

In accordance with SFAS No. 144, long-lived assets, such as property and equipment, 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 estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the consolidated balance sheets and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated. The assets and liabilities of a disposed group classified as held for sale would be presented separately in the appropriate asset and liability sections of the consolidated balance sheets.

(Continued)

(o) ***Commitments and Contingencies***

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

(p) ***Reclassifications***

Certain amounts in the accompanying consolidated financial statements have been reclassified in 2005 to conform with classifications adopted in 2006. Such reclassifications had no effect on previously reported change in net assets.

(2) Investments

Investments at June 30, 2006 and 2005 consisted of the following (in thousands):

	2006	2005	
	Fair value	Carrying value	Fair value
Marketable debt and equity securities:			
Common and preferred stocks	$ 1,948,947	1,246,374	1,246,374
Fixed income	586,714	732,857	732,858
Short-term investments	403,034	190,208	190,207
Mutual and commingled funds	1,359,182	1,914,649	1,914,649
Other investments:			
Hedge funds	997,906	570,278	588,351
Private equity funds	241,811	168,059	203,714
Other, including direct financing lease	138,235	38,310	121,365
	$ 5,675,829	4,860,735	4,997,518

The Schools' investment policy guides its asset allocation, which allows for the use of derivatives and other strategies which are achieved through limited partnerships and mutual funds. These investments pose no off-balance sheet risk to the Schools due to the limited liability structure of the investments.

(a) ***Securities Lending***

In September 2003, the Schools commenced participation in a securities lending program administered by its custodian bank. Under the program, certain equity and fixed income securities of the Schools were lent to participating financial institutions (borrowers) in exchange for collateral. Borrowers are required to deliver collateral equal to a minimum of 102% of the securities loaned. The collateral is marked to market daily. As of June 30, 2006 and 2005, the Schools had limited credit exposure to borrowers because the fair value of collateral held by the Schools exceeded the

fair value of securities loaned. As of June 30, 2006 and 2005, the fair value of securities loaned amounted to $452.9 million and $374.6 million, respectively, and the associated collateral, comprised primarily of money market funds, amounted to $466.0 million and $386.4 million, respectively.

(b) Direct Financing Lease

BHC holds a 40-year lease for a golf course facility located in Virginia. The lease is accounted for as a direct financing lease. At June 30, 2006, the total minimum lease payments to be received and unearned finance charges were $74.5 million and $36.5 million, respectively. At June 30, 2005, the total minimum lease payments to be received and unearned finance charges were $75.6 million and $38.2 million, respectively. Future minimum annual lease payments amount to $1.6 million from 2007 to 2011, and $66.5 million in the aggregate thereafter. In addition to fixed minimum rentals, the lease agreement provides for percentage rent based on adjusted gross revenue of the golf course. There was no percentage rent for the years ended June 30, 2006 and 2005. In January 2004, BHC waived the percentage rent for the calendar years 2004 through 2008 contingent upon the golf club funding certain capital improvements. The lessee has the option to purchase the golf club facilities either at the conclusion of the lease term or anytime during the lease term based on amounts specified in the lease agreement.

(c) Equity in Earnings of Other Investments

Combined and condensed unaudited financial information (most recent available) for other investments that were accounted for on the equity method as of June 30, 2005 is as follows (in thousands):

		2005
Assets	$	3,186,137
Liabilities		498,505
Equity	$	2,687,632
Revenues	$	198,560
Expenses		106,940
Net income	$	91,620

The Schools' equity in earnings of other investments amounted to $8.4 million for the year ended June 30, 2005 and was included in investment income in the accompanying consolidated statements of activities.

(d) Investment Income, Net

Investment income for the years ended June 30, 2006 and 2005 is as follows (in thousands):

		2006	2005
Interest and dividend income	$	129,597	88,633
Equity in earnings of other investments		—	8,411
Management fees		(16,681)	(16,342)
	$	112,916	80,702

(e) Net Realized and Unrealized Gains on Investments

Net realized and unrealized gains on investments for the years ended June 30, 2006 and 2005 for investments reported at fair value was $559.7 million and $292.2 million, respectively. Net realized and unrealized gains on investments for the years ended June 30, 2006 and 2005 for investments reported at other than fair value was nil and $189.9 million, respectively.

(3) Receivables, Net

Receivables, net at June 30, 2006 and 2005 consisted of the following (in thousands):

		2006	2005
Note agreements	$	16,412	12,764
Less deferred profit on note agreements		(16,412)	(12,764)
		—	—
Interest		7,958	10,116
Trade		3,237	6,926
Tenant and tuition		6,768	6,769
Other		5,487	3,735
		23,450	27,546
Less allowance for doubtful accounts		(4,869)	(7,777)
	$	18,581	19,769

(4) Property and Equipment, Net

Property and equipment, net at June 30, 2006 and 2005 consisted of the following (in thousands):

		2006	2005
Educational property and equipment:			
Land	$	16,201	16,067
Buildings, improvements, and equipment		636,386	601,241
Less accumulated depreciation		(148,315)	(126,533)
		504,272	490,775
All other property and equipment:			
Land and land improvements		54,145	45,347
Buildings, improvements, and equipment		329,086	307,442
Less accumulated depreciation and amortization		(187,310)	(176,357)
		195,921	176,432
Construction in progress		50,244	58,065
	$	750,437	725,272

The provision for depreciation and amortization amounted to approximately $36.6 million and $34.5 million for the years ended June 30, 2006 and 2005, respectively.

For the year ended June 30, 2006, the book values of certain properties, buildings, and improvements were impaired. The properties were adjusted to fair value, which resulted in impairment losses of approximately $9.5 million (see note 10). No impairment losses were recorded for the year ended June 30, 2005.

(5) Real Estate Held for Development and Sale

Real estate held for development and sale of $29.1 million and $34.1 million at June 30, 2006 and 2005, respectively, represents properties primarily held by BHC.

(6) Notes Payable

At June 30, 2006 and 2005, unsecured notes payable consisted of the following (columns in thousands):

	2006	2005
Senior promissory notes payable at the rate of 6.89% per annum with annual principal payments of $11.9 million beginning June 22, 2004, with final payment on June 22, 2013. The note agreement contains certain restrictions on assumption of additional debt and requires maintenance of a minimum endowment value and a certain liquidity ratio	$ 83,020	94,880
Senior promissory notes payable under a $150.0 million private shelf facility. The note agreement contains certain restrictions and requires maintenance of a minimum endowment value and a certain liquidity ratio:		
Interest rate of 6.80% per annum with annual principal payments of $952,000 beginning March 1, 2007, with final payment on March 1, 2027	20,000	20,000
Interest rate of 4.88% per annum with annual principal payments of $3,333,000 beginning June 10, 2008, with final payment on June 10, 2028	70,000	70,000
Interest rate of 4.93% per annum with annual principal payments of $4,000,000 beginning April 14, 2009, $3,000,000 beginning April 14, 2016, $2,000,000 beginning April 14, 2022, and $1,000,000 beginning April 14, 2028, with final payment due on April 14, 2029	60,000	60,000
Senior promissory notes payable under a $200.0 million private shelf facility at a rate of 5.15% per annum with annual principal payments of $2,000,000 beginning March 1, 2008, with the final payment on March 1, 2012. The note agreement contains certain restrictions and requires maintenance of a minimum endowment value and a certain liquidity ratio	10,000	—
	$ 243,020	244,880

In July 2006, the Schools borrowed $20.0 million at a rate of 5.15% per annum under the $200.0 million private shelf facility. Annual principal payments of $4,000,000 begin March 1, 2008 with final payment due on March 1, 2012.

In March 2007, the Schools are committed to borrow $20.0 million at a rate of 5.15% per annum under the $200.0 million private shelf facility. Annual principal payments of $4,000,000 begin March 1, 2008 with final payment due on March 1, 2012.

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

Year ending June 30:		
2007	$	12,812
2008		18,146
2009		22,146
2010		22,145
2011		22,145
Thereafter		145,626
	$	243,020

Interest expense incurred for the years ended June 30, 2006 and 2005 are summarized as follows (in thousands):

		2006	2005
Interest expense incurred	$	14,682	15,257
Less interest expense capitalized		(1,137)	(1,360)
Interest expense	$	13,545	13,897

(7) Income Taxes

Total income tax expense (benefit) amounted to approximately $(16.4) million and $6.7 million for the years ended June 30, 2006 and 2005, respectively. These amounts are included in other management and general expenses in the accompanying consolidated statements of activities.

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities as of June 30, 2006 and 2005 are presented below (in thousands):

		2006	2005
Deferred tax assets:			
Difference in basis of investments and real estate	$	17,167	8,575
State tax provisions		3	1,963
Deferred income		1,734	1,619
Allowance for doubtful accounts		571	4,296
Net operating loss carryforwards		7,576	21
Other		2,950	1,368
Valuation allowance		(25,473)	(15,826)
		4,528	2,016
Deferred tax liabilities:			
Depreciation		(2,046)	(1,854)
Investment basis difference and other		(182)	(162)
		(2,228)	(2,016)
Net deferred taxes	$	2,300	—

The change in valuation allowance was an increase of $9.6 million and $2.7 million for the years ended June 30, 2006 and 2005, respectively.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portions or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods which the deferred tax assets are deductible, management believes it is more likely than not that it will realize $2.3 million of these deductible differences, net of the existing valuation allowances at June 30, 2006. The amount of the deferred tax assets considered realizable, however, could be increased in the near term if estimates of future taxable income during the carryforward period are increased. The Schools and BHC have passive activity losses of $13.5 million available to carryforward indefinitely for Federal and state of Hawaii purposes and have net operating losses of $8.2 million of which $2.3 million will be carried back to the year ended June 30, 2005 and $5.9 million is available to carryforward, expiring June 30, 2026.

IRS Audit

In 1995, the IRS began an audit of the Schools and Pauahi Holding Company (PHC), the Schools' former wholly owned taxable subsidiary, for the years ended June 30, 1992 to 1994. It was later expanded to include the years ended June 30, 1995 to 1998. In March 1999, the IRS began an audit of Kamehameha Activities Association (KAA) for the years ended June 30, 1997 and 1998. KAA, formerly a subsidiary of the Schools, merged with KAPF effective June 28, 2002, with KAPF as the surviving entity. This audit was later expanded to include the year ended June 30, 1999.

In January 1999, the IRS had proposed revocation of the Schools' tax-exempt status. Through settlement, negotiation, and the execution of a closing agreement in February 2000, which included removal of the five former Trustees, a settlement payment (including interest) of $14.0 million, and other conditions that required special filings made to the IRS annually through February 2005, the Schools were able to preserve their tax-exempt status.

PHC executed a closing agreement with the IRS in December 2000 to settle tax matters through June 30, 1998. The agreement resulted in a settlement payment (including interest) of $29.8 million that was paid during the year ended June 30, 2001.

In fiscal year 2002, the Schools and its related entities signed closing agreements with the IRS that resolved all outstanding tax issues relating to the taxable year ended July 31, 1998 for PHC, the taxable years ended through June 30, 1999 for KAA, and the taxable years ended through June 30, 2000 for the Schools. Under the agreements, KAA paid the IRS approximately $17 million (plus interest) and the for-profit subsidiaries paid $55.6 million in taxes (plus interest). The closing agreements also resulted in the transfer of the majority of KAA's assets to the Schools and the subsequent merger of KAA into KAPF, with KAPF as the surviving entity.

As a result of the IRS audit settlements, various states have initiated or are planning to initiate examinations of the Schools, KAA, and related entities. As of June 30, 2006, the states of California, Hawaii, and New York, and New York City have initiated examinations, but no final assessments have been received, except by the state of Hawaii, which management intends to appeal. The New York State examination of a PHC subsidiary for the year ended July 31, 1998 resulted in a settlement payment of $1.6 million in taxes (plus interest) in fiscal year 2004. In fiscal year 2006, the state of Hawaii cancelled its tax assessment and New York City settled for $3.9 million in taxes (plus interest) in relation to the examination of a PHC subsidiary for the year ended July 31, 1998. Management believes that it has adequately accrued for these taxes, and that the results of these examinations will not have a significant adverse effect on the Schools' consolidated financial position.

(8) Pension and Other Postretirement Benefits

The Schools have a defined benefit pension plan covering substantially all of its employees. The benefits are based on years of service and the employee's compensation. The Schools make annual contributions to the plan equal to the maximum amount that can be deducted for income tax purposes.

In addition to the Schools' defined benefit pension plan, the Schools sponsor a defined benefit health care plan that provides postretirement medical benefits to full-time employees who meet minimum age and service requirements. The Schools have the right to modify the terms of these benefits.

In December 2003, the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Act) became law in the United States. In May 2004, the Financial Accounting Standards Board (FASB) issued Staff Position 106-2, *Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003,* which was effective for the periods beginning after June 15, 2004. The impact of adopting the Act is the reduction in the Schools' accumulated postretirement benefit obligation and net periodic benefit cost of $3.5 million and $0.5 million, respectively, for the year ended June 30, 2005.

The measurement date used to determine pension and other postretirement benefit measures for the pension plan and the postretirement medical plan is June 30.

The funded status of the plans as of June 30, 2006 and 2005 is as follows (in thousands):

		Pension benefits		Postretirement benefits	
		2006	**2005**	**2006**	**2005**
Benefit obligation at June 30	$	206,636	224,564	23,863	25,457
Fair value of plan assets at June 30		160,023	136,071	—	—
Funded status	$	(46,613)	(88,493)	(23,863)	(25,457)
Accrued benefit cost recognized in the consolidated balance sheets	$	47,832	48,684	23,465	22,223

The accumulated benefit obligation for the pension plan was $167.7 million and $177.5 million at June 30, 2006 and 2005, respectively.

The amounts of net periodic benefit cost, employer contributions, and benefits paid for the years ended June 30, 2006 and 2005 are as follows (in thousands):

		Pension benefits		Postretirement benefits	
		2006	**2005**	**2006**	**2005**
Benefit cost	$	12,059	9,180	2,197	1,749
Employer contributions		12,911	6,728	955	882
Benefits paid		7,281	6,271	955	882

(Continued)

The assumptions used in the measurement of the Schools' benefit obligation and net periodic benefit cost for the years ended June 30, 2006 and 2005 are as follows:

	Pension benefits		Postretirement benefits	
	2006	**2005**	**2006**	**2005**
Benefit obligation:				
Discount rate	6.25%	5.25%	6.25%	5.25%
Expected return on plan assets	8.50	8.00	N/A	N/A
Rate of compensation increase	4.80	4.80	N/A	N/A
Net periodic benefit cost:				
Discount rate	5.25%	6.25%	5.25%	6.25%
Expected return on plan assets	8.50	8.00	N/A	N/A
Rate of compensation increase	4.80	4.80	N/A	N/A

The Schools' overall expected long-term rate of return on plan assets is 8.5%. The expected long-term rate of return on plan assets was projected by the plan's investment consultants based on strategies outlined in the portfolios policies and guidelines.

For measurement purposes, a 10% and 15% annual rate of increase in the per capita cost of covered medical and drug benefits, respectively, was assumed for 2006. The rate was assumed to decrease gradually to 4.75% by the year 2013 and remain at that level thereafter.

(a) Plan Assets

The weighted average asset allocation of the Schools' pension plan is as follows:

	Pension plan assets at June 30			
			Targeted	
	2006	**2005**	**Allocation**	**Range**
Asset category:				
Equity securities	65%	71%	60%	47.5 – 72.5%
Debt securities	26	23	35	22.5 – 50%
Real estate	9	6	5	2.5 – 10%
Total	100%	100%	100%	

The Schools' investment goals for defined benefit pension plan assets are to maximize returns subject to specific risk management policies. Its risk management policies permit investments in debt and equity securities and real estate and other inflation-hedging assets. Readily marketable securities are utilized to pay benefit obligations as they become due.

(b) Cash Flows

The Schools expect to contribute $11.1 million to their pension plan and $0.9 million to their postretirement medical plan in 2007.

The benefits expected to be paid from the respective plans in each year ending June 30, 2007 to 2011 are as follows (in thousands):

		Pension	Postretirement
Year ended June 30:			
2007	$	7,919	941
2008		8,583	995
2009		9,472	1,072
2010		10,074	1,146
2011		10,944	1,236
	$	46,992	5,390

The aggregate benefits expected to be paid under the Schools' pension and postretirement medical plans in the five years from 2012 to 2016 are $69.4 million and $7.3 million, respectively. The expected benefits are based on the same assumptions used to measure the Schools' benefit obligation at June 30 and include estimated future employee service.

The Schools also sponsor a 401(k) retirement savings plan covering substantially all eligible employees. The Schools make matching contributions to the 401(k) plan up to a maximum 3% of employee pretax earnings. Participants are immediately and fully vested in the Schools' contribution. Contributions to the 401(k) plan for the years ended June 30, 2006 and 2005 amounted to approximately $2.2 million and $1.9 million, respectively.

(9) Deferred Compensation Plan

On January 1, 1976, the Schools adopted a deferred compensation plan that allowed employees and others who perform services for the Schools under contract to defer compensation earned. Individual accounts are maintained for each participant and earnings are computed on the basis of alternative investment programs available. The liability has been fully funded and investments are included in marketable debt and equity securities in the consolidated balance sheets.

(10) Net Gain on Property Sales

Net gain on property sales for the years ended June 30, 2006 and 2005 consisted of the following (in thousands):

	2006	2005
Property sales	$ 200,381	140,047
Less cost of property sales	(7,609)	(19,717)
Net property sales	192,772	120,330
Impairment loss on property and equipment (note 4)	(9,499)	—
	$ 183,273	120,330

(11) Fair Value of Financial Instruments

The following table presents the carrying amounts and estimated fair values of the Schools' financial instruments at June 30, 2006 and 2005 (in thousands). The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties.

	2006		2005	
	Carrying amount	Fair value	Carrying amount	Fair value
Cash and cash equivalents	$ 50,498	50,498	64,956	64,956
Investments	5,675,829	5,675,829	4,860,735	4,997,518
Collateral received for loaned securities	466,038	466,038	386,352	386,352
Receivables, net	18,581	32,178	19,769	28,443
Notes payable	243,020	232,166	244,880	255,208
Obligation to repay securities lending collateral	466,038	466,038	386,352	386,352
Accounts payable and accrued expenses	71,064	71,064	60,119	60,119
Income taxes payable	13,734	13,734	31,794	31,794

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

Cash and cash equivalents, collateral received for loaned securities, obligation to repay securities lending collateral, accounts payable and accrued expenses, and income taxes payable: The carrying amounts approximate fair value because of the short maturity of these instruments.

Investments: The fair value of marketable debt and equity securities is based on quoted market prices, and if applicable, discounted for time restrictions. Different techniques and many factors were considered in estimating the fair value of other investments. Several investments have been valued based on the underlying asset value.

Receivables, net: The fair value of note agreements and mortgage notes is valued at the present value of expected future cash flows discounted at an interest rate commensurate with the risk associated with the respective receivables. The carrying value of interest and other receivables approximates fair value because of the short maturity of these instruments.

Notes payable: The fair value of notes payable is estimated using the current rates at which similar loans would be made by lenders to borrowers with similar credit ratings and similar remaining maturities.

(12) Commitments and Contingencies

(a) Rental Income

The majority of land and buildings are generally leased under long-term lease arrangements. At June 30, 2006, future rental income from these leases based on present effective minimum rentals is summarized as follows (in thousands):

Year ending June 30:		
2007	$	84,823
2008		78,410
2009		69,752
2010		61,541
2011		54,653
Thereafter		819,230
	$	1,168,409

Percentage rental income, based on stipulated percentages of gross lessees’ sales, amounted to approximately $14.7 million for each of the years ended June 30, 2006 and 2005.

(b) Capital Commitments

At June 30, 2006 and 2005, the Schools were committed under agreements with certain partnerships and corporations to invest an additional $448 million and $245 million, respectively.

At June 30, 2006 and 2005, open construction, renovation, major repair, and other contracts amounted to approximately $57 million and $13 million, respectively.

(c) Litigation

The Schools, in the normal course of conducting their business, are a defendant or party in a number of civil actions. Management of the Schools is of the opinion that substantially all of these actions are either adequately covered by liability insurance or agreements with lessees or developers of the Schools' real estate and should not have a material adverse effect on the Schools' consolidated financial position.

(d) Trustee Matters

The Trustees receive an annual retainer of $30,000, payable monthly, and will receive a meeting fee of $1,500 per meeting, except for the chairperson, who will receive $2,000 per meeting. On January 23, 2004, the Court approved increasing the maximum number of meetings from 45 to 90 during a 12-month period. The Trustees elected to waive compensation for meetings in excess of 45 during the calendar years 2006, 2005, and 2004. For the years ended June 30, 2006 and 2005, total Trustee compensation amounted to $500,000 and $510,000, respectively.

Schedule 1

KAMEHAMEHA SCHOOLS
AND SUBSIDIARIES

Schedules of Trust Spending

Years ended June 30, 2006, 2005, 2004, 2003, and 2002

(In thousands)

		2006	2005	2004	2003	2002
Trust spending, net:						
Campus-based programs:						
Kapalama	$	75,342	74,931	75,871	72,336	69,679
Hawaii		24,509	22,400	20,806	12,798	5,790
Maui		24,253	20,286	18,559	12,946	5,430
Outreach programs:						
Community Education (includes funding for Ho`okako`o, a not-for-profit organization, of $2,517, $790, $1,327, and $280 for the years ended June 30, 2006, 2005, 2004, and 2003, respectively)		42,674	36,793	35,115	27,872	21,585
Scholarships		14,662	15,650	16,176	16,637	16,503
Educational support services		8,372	5,821	4,716	2,267	1,977
Ke Ali'i Pauahi Foundation		559	378	730	1,984	3,322
Other program expenditures		8,654	9,845	10,948	6,810	1,525
Base spending		199,025	186,104	182,921	153,650	125,811
Less tuition, fees, and other education income (net)		(12,978)	(10,313)	(7,787)	(4,557)	(4,128)
Base distributions		186,047	175,791	175,134	149,093	121,683
Major repairs		4,341	5,738	5,529	5,837	3,907
Capital projects		18,060	36,995	90,618	127,176	116,256
Interest on debt		7,335	7,734	4,776	1,360	—
Debt financing of capital projects		—	—	(60,000)	(70,000)	(20,000)
Total trust spending before reserve activity		215,783	226,258	216,057	213,466	221,846
Reserve activity – operating, net		5,000	(3,800)	4,500	6,000	1,000
Total trust spending	$	220,783	222,458	220,557	219,466	222,846
Average fair value of Endowment	$	5,803,821	5,614,498	5,461,640	5,392,443	5,210,717
Trust spending rate before reserve activity		3.7%	4.0%	4.0%	4.0%	4.3%
Trust spending rate		3.8	4.0	4.0	4.1	4.3

See accompanying independent auditors' report and notes to schedules of trust spending.

KAMEHAMEHA SCHOOLS
AND SUBSIDIARIES

Notes to Schedules of Trust Spending

Years ended June 30, 2006, 2005, 2004, 2003, and 2002

(1) Background and Purpose

The Schools' spending policy governs annual trust spending from the Endowment to support its educational purpose. The spending policy targets annual trust spending at 4% of the average fair value of the Endowment plus the net income, if any, generated from the Schools' agriculture and conservation lands. The spending policy also provides for actual trust spending to vary annually in a range of 2.5% to 6%.

The schedule is prepared on a cash basis and presents the total distributions made from the Endowment to fund educational programs (trust spending) by major program and activity. It also presents the trust spending rates for the fiscal years ended June 30, 2006, 2005, 2004, 2003, and 2002.

(2) Trust Spending and Trust Spending Rate

Trust spending represents the amounts spent during the fiscal year on educational programs by major program and activity. The campus-based and outreach-based program costs represent direct and indirect costs of providing these programs. The Educational Support Services programs represent the costs of administering scholarships, financial aid, admissions, ancestry verification and other supporting functions for educational programs. Ke Ali'i Pauahi Foundation expenditures represent the direct and indirect costs of providing scholarships and other education-related programs through January 2003 at which time these functions returned to the Schools. Other program expenditures represent the direct and indirect costs related to certain educational services that benefit the various campus-based and outreach-based programs. Indirect costs, which represents the portion of the finance, operations, and legal services cost that support the Schools' educational programs and purpose, are allocated to education based on various methods depending on the type of cost including headcount, square footage, and proportion in relation to the other estimates based on management's best judgment. Major repairs, capital projects, interest on debt, and net borrowing of debt and repayment of principal, are directly attributable to education. Reserve activity represents the funding of an operating reserve, as approved by the Court, to ensure assets are readily available for unanticipated educational program expenses. Reserve activity may also include returning funds to the Endowment if there are sufficient operating reserves.

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

(3) Endowment and Average Fair Value of the Endowment

The Endowment consists of all consolidated investment assets of the Schools except agriculture and conservation lands and reserve funds as defined in the Schools' investment policy.

The average fair value of the Endowment is initially based on the average of the five prior fiscal June 30 year-end fair values and over time will be based on the average of the prior 20-quarter-end fair values. Accordingly, the trust spending rates for the years ended June 30, 2006, 2005, 2004, 2003, and 2002 are based on the estimated average fair values over the last five fiscal years utilizing the respective year-end and/or quarter-end values. The fair values for these fiscal years were based primarily on internal and external appraisals, to the extent available, and tax assessed values for the Hawaii real estate assets and the fair value of the other Endowment assets as reported in the audited consolidated financial statements for these fiscal years, net of any associated debt.

(4) Reclassifications

Certain amounts in the accompanying Schedules of Trust Spending have been reclassified in 2005, 2004, 2003, and 2002 to conform with classifications adopted in 2006. Such reclassifications had no effect on previously reported total trust spending.

Schedule 2

KAMEHAMEHA SCHOOLS
AND SUBSIDIARIES

Schedules of Total Return

June 30, 2006

Asset class and benchmarks	Fair value at June 30, 2006 (in thousands)	One-year total return%	Three-year total return%	Five-year total return%	Since July 1, 1999 total return%
Hawaii real estate	$ 2,026,311	29.5	18.4	12.7	10.0
CPI+5%		9.3	8.4	7.7	8.0
U.S. equity	1,690,508	10.8	13.8	5.6	7.1
Russell 3000		9.6	12.6	3.5	1.7
Non-U.S. equity	1,430,626	26.7	24.6	12.4	10.0
MSCI EAFE/Emerging Markets Free Index		28.3	25.6	11.5	6.2
Fixed income	916,452	—	3.2	6.0	6.2
Lehman Brothers Aggregate		(0.8)	2.1	5.0	5.8
Cash equivalents	59,740	4.2	2.5	2.5	3.3
Three-month U.S. Treasury Bill		4.0	2.4	2.3	3.2
Venture and private equity	212,597	22.2	22.8	2.1	4.3
CPI+8.75%		13.1	12.5	12.2	12.7
Hawaii targeted investments	517	N/A	N/A	N/A	N/A
CPI+8.75%		N/A	N/A	N/A	N/A
Absolute return	688,279	9.5	N/A	N/A	N/A
CPI+5%		9.3	N/A	N/A	N/A
Energy and other	462,596	32.3	38.5	34.7	42.8
CPI+5%		9.3	8.4	7.7	8.0
Real estate (Mainland)	175,216	24.3	39.2	25.2	23.3
NCREIF total property index		18.7	15.8	12.0	11.9
Total endowment	$ 7,662,842	17.0	15.1	9.9	9.8
Blended portfolio		11.1	11.3	7.4	6.4
Cambridge Associates Large Endowment Fund Median		14.4	14.7	8.6	9.5
CPI+5%		9.3	8.4	7.7	8.0

See accompanying independent auditors' report and notes to schedules of total return.

(1) Background and Purpose

The Schools' investment policy establishes long- and intermediate-term investment objectives, asset allocation targets, and performance measurement guidelines for the Endowment. The overall long-term investment objective of the Endowment is to earn an average annual real return of 5% net of all investment related expenses.

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

(a) Hawaii Real Estate

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

(b) U.S. Equity

U.S. equity is comprised of marketable equity securities of U.S. companies.

(c) Non-U.S. Equity

Non-U.S. equity is comprised of marketable equity securities of companies outside the U.S. These primarily include stocks of companies overseas in both developed and emerging markets.

(d) Fixed Income

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

(e) Cash Equivalents

Cash equivalents is comprised of investments in debt securities issued by a corporation, government, or government agency, and money market instruments.

(f) Venture and Private Equity

Venture and private equity investments are high risk, high potential return investments in illiquid privately placed equity or equity-related securities of nonpublic companies, companies or parts of companies that are being taken private, or public entities. Investments are made in various types of businesses ranging from start-up enterprises to privately held middle-market firms to larger public firms seeking private financing for specific projects. The Schools' private equity and venture capital portfolio currently consists primarily of pooled fund investments in limited partnerships.

(Continued)

(g) Absolute Return

Absolute return investments have the general objective of producing relatively stable, positive returns independent of the performance of the broad equity and fixed income markets. Absolute return investments include hedge funds pursuing event-driven, relative value, market neutral, and equity long-short strategies.

(h) Energy and Other

Energy and other investments are intended to serve as the inflation hedge component of the portfolio. This asset class includes hedge funds, marketable equity securities, direct investments, and limited partnership interests in energy-related investments.

(i) Real Estate (Mainland)

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

(2) Fair Values

Fair value of an asset is the amount at which the asset could be exchanged in a current transaction between willing parties. The following methods and assumptions were used to estimate the fair value of each asset class:

(a) Hawaii Real Estate

The fair value of residential real property interests (single-family and multifamily) is estimated by internal appraisals using a discounted cash flow method for leased properties and sales comparison approach for unleased properties. The fee simple land values used as inputs within the discounted cash flow model for leased properties are based on estimates by external appraisers and are updated internally for current market conditions since the time that the appraisals were performed.

Commercial properties are divided into two primary categories – leased and unleased. In general, commercial properties are externally appraised every three years. The fair value of leased properties is typically estimated by the external appraisers using an income approach, while the value of unleased properties is typically estimated using a sales comparison approach. Prior to June 30, 2004, for the properties that were internally appraised, the fair value of leased properties was estimated by discounting future net cash flows at an appropriate discount rate over a ten-year period and the current tax-assessed values was used to approximate the fair value of unleased commercial properties.

Either current tax-assessed value or external appraised values are used to approximate the fair value of real estate held for future development and sale.

The fair value of purchase money mortgages is estimated by discounting the expected future net cash flows at a discount rate commensurate with the risk associated with the respective receivables.

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

(Continued)

(b) U.S. Equity

The market value of marketable equity securities is based on quoted market prices, and if applicable, discounted for time restrictions.

(c) Non-U.S. Equity

The market value of marketable equity securities is based on quoted market prices, and if applicable, discounted for time restrictions.

(d) Fixed Income

The market value of marketable debt securities is based on quoted market prices.

(e) Cash Equivalents

The market value of cash equivalents is based on quoted market prices.

(f) Venture and Private Equity

Different techniques and many factors were considered in deriving the fair value of these investments. Several investments have been valued based on the underlying asset value and are based on a number of different factors including, among others, original cost, third-party financing transactions, discounted cash flows and comparable industry multiples. In addition, restricted shares are valued at market prices less illiquidity discounts.

(g) Absolute Return

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

(h) Energy and Other

Different techniques have been utilized and factors considered in deriving the fair value of these investments. Marketable instruments are based on quoted market prices, and if applicable, discounted for time restrictions. Hedge funds, direct investments, and limited partnership interests have been valued based on underlying asset values. For certain assets, the fair value was deemed to approximate the carrying value.

(Continued)

(i) Real Estate (Mainland)

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

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

(3) Total Return

Total return is calculated using the Modified BAI Method, a time-weighted rate of return. Total returns for periods greater than one year are annualized.

(4) Benchmark Indices

The benchmarks indices are set forth in the Schools' investment policy. Amendments to the benchmark indices are incorporated when effective and include revised benchmarks, asset class target weights, and blended benchmark allocation methodologies. Certain asset classes may have varying benchmarks and an effective date indicating the current and previous benchmark. Blended portfolio benchmarks are generally weighted based upon the asset class targets set forth in the Schools' approved investment but may be based upon actual weights.

(5) Reclassifications

Certain amounts in the accompanying Schedules of Total Return have been reclassified in 2005, 2004, 2003, 2002, 2001, and 2000 to conform with classifications adopted in 2006. Such reclassifications had no effect on previously reported total return.