



UNIVERSITY OF HAWAII FOUNDATION

Financial Statements

June 30, 2018 and 2017

(With Independent Auditors' Report Thereon)



KPMG LLP
Suite 2100
1003 Bishop Street
Honolulu, HI 96813-6400

Independent Auditors' Report

The Board of Trustees
University of Hawaii Foundation:

Report on the Financial Statements

We have audited the accompanying financial statements of the University of Hawaii Foundation, which comprise the statements of financial position as of June 30, 2018 and 2017, and the related statements of activities 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 U.S. generally accepted accounting principles; 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.

Auditors' 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 auditors' 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 the University of Hawaii Foundation as of June 30, 2018 and 2017, and the changes in its net assets and its cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles.

KPMG LLP

Honolulu, Hawaii
November 12, 2018

UNIVERSITY OF HAWAII FOUNDATION

Statements of Financial Position

June 30, 2018 and 2017

Assets	2018	2017
	<u> </u>	<u> </u>
Cash and cash equivalents	\$ 8,511,690	6,891,683
Contributions receivable, net	41,869,952	40,620,872
Prepaid expenses and other receivables	2,815,831	2,624,210
Property and equipment, at cost, net of accumulated depreciation and amortization of \$1,647,877 in 2018 and \$1,441,458 in 2017	10,543,768	10,512,675
Other assets, at cost	2,103,674	3,138,989
Investments	433,332,934	407,512,702
Beneficial interest in trusts held by others	96,782,348	94,080,627
	<u> </u>	<u> </u>
Total assets	\$ <u>595,960,197</u>	<u>565,381,758</u>
Liabilities and Net Assets		
Liabilities:		
Accounts payable	\$ 10,074,232	7,461,350
Liabilities under split-interest agreements	12,566,682	12,631,497
Amounts held for others	3,935,980	3,881,690
Long-term debt	8,200,000	8,200,000
Other liabilities	683,799	449,554
	<u> </u>	<u> </u>
Total liabilities	35,460,693	32,624,091
Net assets:		
Unrestricted	(663,535)	67,472
Temporarily restricted	204,779,761	195,246,706
Permanently restricted	356,383,278	337,443,489
	<u> </u>	<u> </u>
Total net assets	560,499,504	532,757,667
Commitments and contingencies		
	<u> </u>	<u> </u>
Total liabilities and net assets	\$ <u>595,960,197</u>	<u>565,381,758</u>

See accompanying notes to financial statements.

UNIVERSITY OF HAWAII FOUNDATION

Statement of Activities

Year ended June 30, 2018

	Net assets			Total
	Unrestricted	Temporarily restricted	Permanently restricted	
Revenue:				
Contributions	\$ 614,315	39,855,808	14,811,918	55,282,041
Fees, honoraria, royalties, and other	3,937,650	1,038,847	1,051	4,977,548
Investment income, net	2,329,589	21,604,997	4,765,025	28,699,611
Administrative fees	6,293,101	(5,570,178)	(722,923)	—
Fund-raising events and projects	—	870,190	84,718	954,908
	<u>13,174,655</u>	<u>57,799,664</u>	<u>18,939,789</u>	<u>89,914,108</u>
Net assets released from restrictions	<u>48,266,609</u>	<u>(48,266,609)</u>	<u>—</u>	<u>—</u>
	<u>61,441,264</u>	<u>9,533,055</u>	<u>18,939,789</u>	<u>89,914,108</u>
Expenses:				
Program services:				
Extension and public services	804,977	—	—	804,977
Academic support	7,127,118	—	—	7,127,118
Research	12,567,178	—	—	12,567,178
Student aid and services	8,952,019	—	—	8,952,019
Faculty and staff support	3,880,837	—	—	3,880,837
Capital projects	2,020,505	—	—	2,020,505
Athletics	3,041,421	—	—	3,041,421
Special programs	7,851,588	—	—	7,851,588
Other	2,020,966	—	—	2,020,966
Total program services	<u>48,266,609</u>	<u>—</u>	<u>—</u>	<u>48,266,609</u>
Supporting services:				
Administrative, management, and fiscal services	5,144,266	—	—	5,144,266
Development	8,761,396	—	—	8,761,396
Total supporting services	<u>13,905,662</u>	<u>—</u>	<u>—</u>	<u>13,905,662</u>
Total expenses	<u>62,172,271</u>	<u>—</u>	<u>—</u>	<u>62,172,271</u>
Change in net assets	(731,007)	9,533,055	18,939,789	27,741,837
Net assets at beginning of year	<u>67,472</u>	<u>195,246,706</u>	<u>337,443,489</u>	<u>532,757,667</u>
Net assets at end of year	\$ <u>(663,535)</u>	<u>204,779,761</u>	<u>356,383,278</u>	<u>560,499,504</u>

See accompanying notes to financial statements.

UNIVERSITY OF HAWAII FOUNDATION

Statement of Activities

Year ended June 30, 2017

	Net assets			Total
	Unrestricted	Temporarily restricted	Permanently restricted	
Revenue:				
Contributions	\$ 237,491	32,621,355	62,868,317	95,727,163
Fees, honoraria, royalties, and other	3,886,107	1,140,142	823	5,027,072
Investment income, net	7,663,349	24,460,212	1,844,142	33,967,703
Administrative fees	5,521,701	(5,035,350)	(486,351)	—
Fund-raising events and projects	680	818,439	293,115	1,112,234
	<u>17,309,328</u>	<u>54,004,798</u>	<u>64,520,046</u>	<u>135,834,172</u>
Net assets released from restrictions	<u>51,451,189</u>	<u>(51,451,189)</u>	<u>—</u>	<u>—</u>
	<u>68,760,517</u>	<u>2,553,609</u>	<u>64,520,046</u>	<u>135,834,172</u>
Expenses:				
Program services:				
Extension and public services	961,197	—	—	961,197
Academic support	6,043,452	—	—	6,043,452
Research	11,651,921	—	—	11,651,921
Student aid and services	9,670,504	—	—	9,670,504
Faculty and staff support	4,082,630	—	—	4,082,630
Capital projects	5,578,573	—	—	5,578,573
Athletics	3,847,925	—	—	3,847,925
Special programs	7,322,513	—	—	7,322,513
Other	2,292,474	—	—	2,292,474
Total program services	<u>51,451,189</u>	<u>—</u>	<u>—</u>	<u>51,451,189</u>
Supporting services:				
Administrative, management, and fiscal services	4,750,812	—	—	4,750,812
Development	8,722,040	—	—	8,722,040
Total supporting services	<u>13,472,852</u>	<u>—</u>	<u>—</u>	<u>13,472,852</u>
Total expenses	<u>64,924,041</u>	<u>—</u>	<u>—</u>	<u>64,924,041</u>
Change in net assets	3,836,476	2,553,609	64,520,046	70,910,131
Net assets at beginning of year	<u>(3,769,004)</u>	<u>192,693,097</u>	<u>272,923,443</u>	<u>461,847,536</u>
Net assets at end of year	\$ <u>67,472</u>	<u>195,246,706</u>	<u>337,443,489</u>	<u>532,757,667</u>

See accompanying notes to financial statements.

UNIVERSITY OF HAWAII FOUNDATION

Statements of Cash Flows

Years ended June 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Cash flows from operating activities:		
Cash received from contributions	\$ 41,206,797	40,027,385
Cash received for fees, honoraria, royalties, and other	4,981,496	5,026,249
Investment return received	432,054	5,072,497
Program and supporting service expenses paid	<u>(59,628,716)</u>	<u>(63,481,588)</u>
Net cash used in operating activities	<u>(13,008,369)</u>	<u>(13,355,457)</u>
Cash flows from investing activities:		
Purchase of investments	(79,770,392)	(194,547,618)
Proceeds from sale of investments	76,809,589	196,142,488
Purchase of property and equipment	<u>(242,671)</u>	<u>(8,319,162)</u>
Net cash used in investing activities	<u>(3,203,474)</u>	<u>(6,724,292)</u>
Cash flows from financing activities:		
Amounts restricted for long-term investment	17,831,850	10,233,989
Borrowings on long-term debt	<u>—</u>	<u>8,200,000</u>
Net cash provided by financing activities	<u>17,831,850</u>	<u>18,433,989</u>
Net increase (decrease) in cash and cash equivalents	1,620,007	(1,645,760)
Cash and cash equivalents at beginning of year	<u>6,891,683</u>	<u>8,537,443</u>
Cash and cash equivalents at end of year	\$ <u><u>8,511,690</u></u>	<u><u>6,891,683</u></u>
Reconciliation of change in net assets to net cash used in operating activities:		
Change in net assets	\$ 27,741,837	70,910,131
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Amounts restricted for long-term investment	(17,831,850)	(10,233,989)
Contribution of remainder interest in real estate properties	—	(76,535,205)
Other noncash contributions	(2,376,791)	(10,795,862)
Depreciation and amortization	211,578	83,009
Realized and unrealized net gains on investments	(23,492,006)	(29,629,205)
Provision for uncollectible pledges, net	(157,553)	91,842
Changes in assets and liabilities:		
Contributions receivable	(1,091,527)	37,702,055
Prepaid expenses and other receivables	(191,621)	(1,375,308)
Other assets	1,342,962	(4,622)
Accounts payable	2,612,882	3,874,889
Liabilities under split-interest agreements	(64,815)	2,065,901
Amounts held for others, net	54,290	512,240
Other liabilities	<u>234,245</u>	<u>(21,333)</u>
Net cash used in operating activities	\$ <u><u>(13,008,369)</u></u>	<u><u>(13,355,457)</u></u>
Supplemental disclosure of cash flow information:		
Cash paid during the year for:		
Interest	\$ 249,417	—

See accompanying notes to financial statements.

UNIVERSITY OF HAWAII FOUNDATION

Notes to Financial Statements

June 30, 2018 and 2017

(1) Summary of Significant Accounting Policies

(a) Organization

The University of Hawaii Foundation (the Foundation) is a not-for-profit entity established to solicit and manage funds for the benefit of the University of Hawaii (the University). The Foundation is governed by a self-perpetuating board of trustees primarily consisting of elected volunteers.

(b) Financial Statement Presentation

The financial statements have been prepared to focus on the Foundation as a whole and to present balances and transactions according to the existence or absence of donor-imposed restrictions. This has been accomplished by classification of net assets and transactions into three classes (unrestricted, temporarily restricted, or permanently restricted) as follows:

Unrestricted Net Assets – Net assets that represent resources generated from operations or that are not subject to donor-imposed stipulations.

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

Permanently Restricted Net Assets – Net assets subject to donor-imposed stipulations that must be maintained permanently by the Foundation. Generally, the donor of these assets permits the Foundation to use all or part of the income earned on related investments for general or specific purposes in support of the University.

(c) Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles (U.S. 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 revenue and expenses during the reporting period. Actual results could differ from those estimates.

(d) Cash Equivalents

Short-term investments held for operations with original maturities of three months or less when purchased are classified as cash equivalents. Cash equivalents include short-term U.S. Treasury securities and other short-term, highly liquid investments and are carried at cost, which approximates fair value. Short-term investments held for investment purposes are reflected as investments.

(e) Contributions and Contributions Receivable

Contributions received and unconditional promises to give are recorded at their fair values and are reported as an increase in net assets.

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Notes to Financial Statements

June 30, 2018 and 2017

The Foundation 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. Certain noncash contributions are reported as other assets until liquidation. When a donor restriction expires, that is, when a stipulated time restriction ends or the 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.

Unconditional promises to give (contributions receivable) that are expected to be collected within one year are recorded at net realizable value. Pledges receivable that are expected to be collected in future years are recorded at the present value of their estimated future cash flows. The discounts on those amounts are computed using a fair value interest rate commensurate with the associated risk to the years in which the promises are received. Amortization of the discounts is included in contribution revenue. The Foundation provides an allowance for uncollectible pledges based upon historical experience with its donors as well as individual donor circumstances.

(f) Investments

Investments are reported at fair value with unrealized gains and losses reported in the statements of activities as increases or decreases in unrestricted net assets unless their use is temporarily or permanently restricted by explicit donor stipulations or by law.

Fair value for investments in debt, equity and certain pooled investments in natural resources, real estate and hedge funds are based on quoted market prices for the security or quoted market prices for the underlying securities in the pooled investment.

Fair value for investments in certain alternative investments, including limited partnership investments in domestic and foreign equities, natural resources and real estate, hedge funds and private equity securities, are generally based on information provided by the respective external investment manager at the most recent valuation date and from the valuation date to fiscal year-end, if applicable. The private equity, venture capital, and real estate investments are not readily marketable and involve assumptions and methods that are reviewed by management. Because these investments are not readily marketable, their estimated value is subject to uncertainty and, therefore, may differ from the value that would have been used had a ready market for such investment existed. A portion of the investments made by certain hedge funds is also not readily marketable; additionally, hedge fund managers may not provide the detail of their underlying marketable securities. The hedge fund valuation process is carefully reviewed by management with the assistance of an outside consultant. As described in note 1(k), the Foundation utilized the net asset value per share for certain investments in alternative structures as a practical expedient for the estimation of the fair value of these investments.

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Notes to Financial Statements

June 30, 2018 and 2017

(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 as follows:

Equipment	3–5 years
Furniture and fixtures	5 years
Leasehold improvements	10 years
Buildings	30 years

The components of net property and equipment at June 30, 2018 and 2017 were as follows:

	<u>2018</u>	<u>2017</u>
Land	\$ 7,927,482	7,906,881
Buildings	2,456,024	2,476,624
Equipment	1,685,465	1,447,954
Leasehold improvements	58,253	58,253
Furniture and fixtures	<u>64,421</u>	<u>64,421</u>
	12,191,645	11,954,133
Less accumulated depreciation	<u>(1,647,877)</u>	<u>(1,441,458)</u>
Property and equipment, net	<u>\$ 10,543,768</u>	<u>10,512,675</u>

The Foundation reports gifts of property and equipment at fair value as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, the Foundation reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

On April 20, 2017, the Foundation purchased the Charles Atherton House and the Mary Atherton Richards House (the Atherton property) for a total of \$8.3 million. The Foundation entered into a construction credit facility to purchase the Atherton property. Refer to note 10.

(h) Split-Interest Agreements

The Foundation's split-interest agreements with donors consist of irrevocable pooled income funds, charitable remainder trusts, and charitable gift annuities for which the Foundation serves as trustee. Assets held under these split-interest agreements are included in investments. Contribution revenue is recognized at the date the split-interest agreements are established after recording liabilities for the present value (utilizing discount rates ranging between 1.2% and 8.2%) of the estimated future payments to be made to the donors and/or other beneficiaries. The liabilities are adjusted during the term of the split-interest agreements for changes in the fair value of the assets, accretion of the discount, and other changes in the estimates of future benefits. For the years ended June 30, 2018 and

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Notes to Financial Statements

June 30, 2018 and 2017

2017, contributions revenue attributed to split-interest agreements were \$1,022,550 and \$1,763,820, respectively. For the years ended June 30, 2018 and 2017, net investment realized and unrealized gains (losses) include a net gain of \$127,273 and \$659,754, respectively, for changes in the value of split-interest agreements.

(i) Interest in Trusts Held by Others

The Foundation is also the beneficiary of certain trusts held and administered by others. The fair value of the estimated future cash receipts from the trusts is recognized as assets and contribution revenue when the Foundation is notified of their existence. The reported value of the assets is fair value. For the years ended June 30, 2018 and 2017, contribution revenue, excluding contributions of remainder interest in real estate properties, totaled \$157,418 and \$128,026, respectively, attributable to their beneficial interest in trusts held by others. The Foundation received remainder interests in real estate properties amounting to \$76,535,205 during the year ended June 30, 2017. For the years ended June 30, 2018 and 2017, net investment realized and unrealized gains (losses) associated with the beneficial interest in trust held by others include a net gain of \$4,025,244 and \$1,459,610, respectively.

(j) Amounts Held for Others

Resources received in transactions that the Foundation acts as an agent are reported as amounts held for others. Investment income earned on amounts received increases amounts held for others. Distributions to specified recipients decrease amounts held for others. Unrealized gains (losses) on assets held for others were \$37,696 and \$112,137 for the years ended June 30, 2018 and 2017, respectively.

(k) Fair Value Measurements

The Foundation applies the provisions of Financial Accounting Standards Board (FASB) Accounting Standard Codification (ASC) Topic 820, *Fair Value Measurement*, for fair value measurements of financial assets and financial liabilities and for fair value measurements of nonfinancial items that are recognized or disclosed at fair value in the financial statements on a recurring basis. ASC Topic 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC Topic 820 also establishes a framework for measuring fair value and expands disclosures about fair value measurements (note 9).

The Foundation also applies the provisions of ASC Topic 820 to fair value measurements of nonfinancial assets and nonfinancial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis.

(l) Recent Account Pronouncements

In February 2016, the FASB issued ASU No. 2016-02, *Leases* (Topic 842), which supersedes FASB ASC Topic 840, *Leases*, and makes other conforming amendments to U.S. GAAP. ASU No. 2016-02 requires, among other changes to the lease accounting guidance, lessees to recognize most leases on balance sheet via a right-of-offset asset and lease liability, and additional qualitative and quantitative disclosures. ASU No. 2016-02 is effective for the Foundation for annual periods in fiscal years beginning after December 15, 2019, permits early adoption, and mandates a modified retrospective transition method. The Foundation is required to adopt ASU No. 2016-02 on

UNIVERSITY OF HAWAII FOUNDATION

Notes to Financial Statements

June 30, 2018 and 2017

July 1, 2020. The Foundation is currently evaluating the potential impact of adopting this guidance on the financial statements.

In August 2016, the FASB issued ASU No. 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities*. This guidance reduces the number of net asset classes presented on the balance sheet from three to two, requires presentation of expenses by their functional and natural classification in one location in the financial statements, and requires quantitative and qualitative information about management of liquid resources and availability of financial assets to meet cash needs within one year of the balance sheet date. This guidance will be effective for the Foundation's fiscal year ending June 30, 2019. The Foundation is currently evaluating the potential impact of adopting this guidance on the financial statements.

In June 2018, the FASB issued ASU No. 2018-08, *Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. The new standard provides clarification in characterizing grants and similar contracts with resource providers as either exchange transactions or contributions and in determining whether a contribution is conditional when applying the revenue recognition guidance. The new standard is effective for the Foundation's fiscal year ending June 30, 2020. The Foundation is currently evaluating the potential impact of adopting this guidance on the financial statements.

(2) Contributions Receivable

At June 30, 2018 and 2017, contributions receivable, net of discount for present value and allowance for uncollectible contributions, consisted of the following:

	<u>2018</u>	<u>2017</u>
Contributions receivable	\$ 45,067,486	45,550,340
Less discount to present value (1.2%–6.1% discount rate)	<u>(666,544)</u>	<u>(2,240,925)</u>
Subtotal	44,400,942	43,309,415
Less allowance for uncollectible pledges	<u>(2,530,990)</u>	<u>(2,688,543)</u>
Contributions receivable, net	\$ <u>41,869,952</u>	<u>40,620,872</u>
Amounts to be collected in:		
Less than one year	\$ 21,467,211	17,965,912
One year to five years	<u>23,600,275</u>	<u>27,584,428</u>
Total	\$ <u>45,067,486</u>	<u>45,550,340</u>

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Notes to Financial Statements

June 30, 2018 and 2017

(3) Investments

Investments at June 30, 2018 and 2017 consisted of the following:

	2018		2017	
	Fair value	Cost	Fair value	Cost
Domestic equities	\$ 40,295,522	24,154,600	44,375,348	32,471,424
Fixed-income securities	137,510,216	142,455,359	133,569,768	135,808,757
Foreign equities	79,749,701	56,011,994	75,467,795	56,329,218
Money market funds	7,294,598	7,294,598	3,513,864	3,513,864
Hedge funds	104,983,101	60,245,029	97,213,274	61,209,466
Private equity securities	23,041,425	21,782,135	16,625,530	16,859,135
Natural resources/real estate	40,458,371	44,173,144	36,747,123	41,758,402
	<u>\$ 433,332,934</u>	<u>356,116,859</u>	<u>407,512,702</u>	<u>347,950,266</u>

The Foundation invests in various types of investment securities. Investment securities are exposed to various risks, such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the statements of financial position.

Investments are generally pooled and managed under various asset diversification strategies, depending upon the investment objectives and to avoid significant concentrations of market risk. Earnings on permanently restricted contributions (endowment), which the donor designates as being available for program operations, are considered temporarily restricted until the specific restrictions have been met. Investments classified as permanently restricted net assets were \$260,935,690 and \$246,050,610 at June 30, 2018 and 2017, respectively. Under the Foundation's endowment spending policy, certain amounts (based on a percentage of the adjusted fair value of the investment pool) are appropriated and are available to support operations. In 2018 and 2017, \$11,345,371 and \$10,245,703, respectively, was made available to support programs. Investment management fees amounted to \$1,128,625 in 2018 and \$1,084,655 in 2017.

The following schedule summarizes the components of investment return:

	Net assets			
	Unrestricted	Temporarily restricted	Permanently restricted	Total
2018:				
Dividends and interest	\$ 2,090,074	3,060,367	57,164	5,207,605
Realized and unrealized gains, net	<u>239,515</u>	<u>18,544,630</u>	<u>4,707,861</u>	<u>23,492,006</u>
Total investment income	<u>\$ 2,329,589</u>	<u>21,604,997</u>	<u>4,765,025</u>	<u>28,699,611</u>

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Notes to Financial Statements

June 30, 2018 and 2017

		Net assets			
		Unrestricted	Temporarily restricted	Permanently restricted	Total
2017:					
	Dividends and interest	\$ 1,892,595	2,406,325	39,578	4,338,498
	Realized and unrealized gains, net	<u>5,770,754</u>	<u>22,053,887</u>	<u>1,804,564</u>	<u>29,629,205</u>
	Total investment income	<u>\$ 7,663,349</u>	<u>24,460,212</u>	<u>1,844,142</u>	<u>33,967,703</u>

(4) Income Taxes

The Foundation is an organization exempt from income tax under Section 501(c)(3) of the Internal Revenue Code and is generally not subject to federal or state of Hawaii income taxes. However, the Foundation is subject to income taxes on any net income that is derived from a trade or business, regularly carried on, and not in furtherance of the purposes for which it was granted exemption. No income tax provision has been recorded as the net income, if any, from any unrelated trade or business, in the opinion of management, is not material to the basic financial statements taken as a whole.

(5) Retirement Annuity Plan

The Foundation has defined-contribution retirement annuity plans with Teachers Insurance and Annuity Association covering substantially all of its employees. The Foundation recorded contribution expense of \$811,865 and \$827,547 in 2018 and 2017, respectively.

(6) Leases

The Foundation leases office space from the University under an annual operating lease, which provides for a nominal rental amount. The estimated fair rental value of the property has been reported as unrestricted contribution revenue with an offsetting amount charged to supporting services of \$387,684 and \$376,392 in 2018 and 2017, respectively.

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(7) Restricted Net Assets

Restricted net assets consisted of the following restricted amounts at June 30, 2018 and 2017:

	<u>Temporarily restricted</u>	<u>Permanently restricted</u>
2018:		
Extension and public services	\$ 3,863,772	2,038,202
Academic support	31,073,160	20,824,436
Research	34,986,980	7,767,946
Student aid and services	30,830,428	110,672,925
Faculty and staff support	19,166,328	179,245,249
Capital projects	17,114,639	2,384,308
Athletics	3,842,716	630,762
Special	23,570,469	19,352,426
Other	<u>40,331,269</u>	<u>13,467,024</u>
Total	\$ <u>204,779,761</u>	<u>356,383,278</u>
	<u>Temporarily restricted</u>	<u>Permanently restricted</u>
2017:		
Extension and public services	\$ 4,033,241	1,989,677
Academic support	32,682,702	20,172,326
Research	39,486,950	7,680,137
Student aid and services	28,781,561	102,620,577
Faculty and staff support	15,309,550	171,536,460
Capital projects	16,064,513	2,360,423
Athletics	3,455,952	614,747
Special	23,128,989	18,295,393
Other	<u>32,303,248</u>	<u>12,173,749</u>
Total	\$ <u>195,246,706</u>	<u>337,443,489</u>

Net assets are released from donor restrictions primarily by incurring expenses that satisfy the restricted purpose. For the years ended June 30, 2018 and 2017, net assets released from restriction totaled \$48,266,609 and \$51,451,189, respectively.

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(8) Endowment

The Foundation's endowment consists of approximately 1,472 individual funds established for a variety of purposes. The endowment includes both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments. As required by U.S. GAAP, net assets associated with endowment funds, including funds designated by the board of trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions. At June 30, 2018 and 2017, the endowment net assets amounted to \$321,039,892 and \$294,688,609, respectively.

For the years ended June 30, 2018 and 2017, the changes in endowment net assets are as follows:

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Endowment net assets, June 30, 2016 \$	(9,073,144)	49,944,800	218,311,158	259,182,814
Investment return:				
Investment income	54,463	1,900,888	—	1,955,351
Net appreciation, realized and unrealized	<u>6,266,341</u>	<u>23,331,774</u>	<u>—</u>	<u>29,598,115</u>
Total investment return	6,320,804	25,232,662	—	31,553,466
Contributions, net of expenses	729	316,834	18,334,029	18,651,592
Appropriations and management fees	<u>(491,781)</u>	<u>(14,207,482)</u>	<u>—</u>	<u>(14,699,263)</u>
Endowment net assets, June 30, 2017	<u>(3,243,392)</u>	<u>61,286,814</u>	<u>236,645,187</u>	<u>294,688,609</u>
Investment return:				
Investment income	71,074	2,091,463	—	2,162,537
Net appreciation, realized and unrealized	<u>1,605,156</u>	<u>19,543,911</u>	<u>—</u>	<u>21,149,067</u>
Total investment return	1,676,230	21,635,374	—	23,311,604
Contributions, net of expenses	756	3,350,935	15,565,464	18,917,155
Appropriations and management fees	<u>(530,341)</u>	<u>(15,347,135)</u>	<u>—</u>	<u>(15,877,476)</u>
Endowment net assets, June 30, 2018 \$	<u><u>(2,096,747)</u></u>	<u><u>70,925,988</u></u>	<u><u>252,210,651</u></u>	<u><u>321,039,892</u></u>

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Donor-restricted and board-designated endowment net asset composition is as follows as of June 30, 2018 and 2017:

	2018			
	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ (3,901,359)	70,925,988	252,210,651	319,235,280
Board-designated endowment funds	1,804,612	—	—	1,804,612
	<u>\$ (2,096,747)</u>	<u>70,925,988</u>	<u>252,210,651</u>	<u>321,039,892</u>

	2017			
	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ (4,854,663)	61,286,814	236,645,187	293,077,338
Board-designated endowment funds	1,611,271	—	—	1,611,271
	<u>\$ (3,243,392)</u>	<u>61,286,814</u>	<u>236,645,187</u>	<u>294,688,609</u>

Description of amounts classified as permanently restricted net assets and temporarily restricted net assets is as follows:

	<u>2018</u>	<u>2017</u>
Permanently restricted net assets:		
The portion of endowment funds that is required to be retained permanently either by explicit donor stipulation or by HUPMIFA	\$ 252,210,651	236,645,187
Contribution and other receivables, net	6,542,325	7,389,528
Beneficial interest in trusts held by others	95,447,589	91,392,879
Split-interest agreements, net and other assets	2,182,713	2,015,895
Total permanently restricted net assets	<u>\$ 356,383,278</u>	<u>337,443,489</u>
Temporarily restricted net assets:		
The portion of temporarily restricted net assets, excluding endowment funds, subject to purpose restrictions	\$ 90,886,668	92,405,195
The portion of the perpetual endowment funds subject to time restriction under HUPMIFA with purpose restrictions	70,925,988	61,286,814
Contribution and other receivables, net	37,249,402	34,915,735
Beneficial interest in trusts held by others	1,334,759	2,687,748
Split-interest agreements, net and other assets	4,382,944	3,951,214
Total temporarily restricted net assets	<u>\$ 204,779,761</u>	<u>195,246,706</u>

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(a) Interpretation of Relevant Law

The Board of Trustees of the Foundation has interpreted Hawaii's Uniform Prudent Management of Institutional Funds Act (HUPMIFA), which was enacted by the State of Hawaii on July 1, 2009, as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Foundation classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are expended by the organization in a manner consistent with the standard of prudence prescribed by HUPMIFA. In accordance with HUPMIFA, the organization considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- (1) The duration and preservation of the fund
- (2) The purposes of the organization and the donor-restricted endowment fund
- (3) General economic conditions
- (4) The possible effect of inflation and deflation
- (5) The expected total return from income and the appreciation of investments
- (6) Other resources of the organization
- (7) The investment policies of the organization

(b) Funds with Deficiencies

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or HUPMIFA requires the Foundation to retain as a fund of perpetual duration. At June 30, 2018 and 2017, in accordance with U.S. GAAP, deficiencies of this nature that are reported in unrestricted net assets were \$3,901,359 and \$4,854,663, respectively. These deficiencies resulted from unfavorable market fluctuations and continued appropriation for certain programs that were deemed prudent by the board of trustees.

(c) Return Objectives and Risk Parameters

The Foundation has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the organization must hold in perpetuity or for a donor-specified periods, as well as board-designated funds. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of the S&P 500 index while assuming a moderate level of investment risk. The Foundation expects its endowment funds, over time, to provide an average rate of return of

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approximately 5.5% annually (including inflation). Actual returns in any given year may vary from this amount.

(d) Strategies Employed for Achieving Objectives

To satisfy its long-term rate-of-return objectives, the Foundation relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Foundation targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

(e) Spending Policy

The Foundation has a policy of appropriating for distribution each year up to 6% of its endowment fund's average fair value over the prior 12 quarters through the calendar year-end preceding the fiscal year in which the distribution is planned. In establishing this policy, the Foundation considered the long-term expected return on its endowment. Accordingly, over the long-term, the Foundation expects the current spending policy to allow its endowment to grow at an average of 5.5% annually. This is consistent with the organization's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

(9) Fair Value Measurements

(a) Fair Value of Financial Instruments

The following table presents the carrying amounts and estimated fair values of the Foundation's financial instruments at June 30, 2018 and 2017. The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

	2018		2017	
	Reported amount	Fair value	Reported amount	Fair value
Cash and cash equivalents \$	8,511,690	8,511,690	6,891,683	6,891,683
Contributions receivable, net	41,869,952	41,869,952	40,620,872	40,620,872
Other receivables	2,815,831	2,815,831	2,624,210	2,624,210
Investments	433,332,934	433,332,934	407,512,702	407,512,702
Beneficial interest in trusts held by others	96,782,348	96,782,348	94,080,627	94,080,627
Accounts payable	10,074,232	10,074,232	7,461,350	7,461,350
Amounts held for others	3,935,980	3,935,980	3,881,690	3,881,690
Long-term debt	8,200,000	7,948,233	8,200,000	8,200,000
Other liabilities	683,799	683,799	449,554	449,554

The reported amounts shown in the table are included in the statements of financial position under the indicated captions.

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The fair values of the financial instruments shown in the above table as of June 30, 2018 and 2017 represent management's best estimates of the amounts that would be received to sell those assets or that would be paid to transfer those liabilities in an orderly transaction between market participants at that date. Those fair value measurements maximize the use of observable inputs. However, in situations where there is little, if any, market activity for the asset or liability at the measurement date, the fair value measurement reflects the Foundation's own judgments about the assumptions that market participants would use in pricing the asset or liability. Those judgments are developed by the Foundation based on the best information available in the circumstances.

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

Cash and cash equivalents, accounts payable, and other liabilities – The reported amounts approximate fair value because of the short maturity of these instruments.

Contributions receivable, net and other receivables – The carrying amount of the contributions receivables and other receivables approximates fair value as the present value of expected future cash flows are discounted at an interest rate commensurate with the risk associated with the respective financial instrument.

Investments, beneficial interest in trusts held by others, and amounts held for others – The fair value of investments in marketable securities and beneficial interest in trusts held by others is based primarily on quoted market prices. The fair value of other investments that do not have readily determinable fair values is generally based on quoted market prices of the underlying investments and 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. As described in note 1(k), the Foundation utilized the net asset value per share for certain investments in alternative structures as a practical expedient for the estimation of the fair value of these investments. The fair value for amounts held for others is based on the fair value of the underlying investments.

Long-term debt – The fair value of long-term debt is estimated by discounting scheduled cash flow payments over the contractual borrowing period at the estimated market rate for similar borrowing arrangements.

(b) Fair Value Hierarchy

ASC Topic 820 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 measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Foundation has the ability to access at the measurement date.
- Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3 inputs are unobservable inputs for the asset or liability.

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The level in the fair value hierarchy within which a fair value measurement in its entirety falls is based on the lowest-level input that is significant to the fair value measurement in its entirety at the measurement date.

The following tables present assets that are measured at fair value on a recurring basis at June 30, 2018 and 2017:

		Fair value measurements at reporting date using			
		Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Investments measured at net asset value
June 30, 2018					
Assets:					
Domestic equities	\$ 40,295,522	10,928,727	—	—	29,366,795 a
Fixed-income securities	137,510,216	122,652,102	14,858,114	—	—
Foreign equities	79,749,701	36,936,403	—	—	42,813,298 b
Money market funds	7,294,598	7,294,598	—	—	—
Natural resources/real estate	40,458,369	8,748,867	—	15,347,678	16,361,824 c
Hedge funds	104,983,101	5,883,079	—	—	99,100,022 d
Private equity securities	23,041,427	—	—	1,680,605	21,360,822 c
Total investments	433,332,934	192,443,776	14,858,114	17,028,283	209,002,761
Beneficial interest in trusts held by others	96,782,348	—	12,842,889	83,939,459	—
Total	<u>\$ 530,115,282</u>	<u>192,443,776</u>	<u>27,701,003</u>	<u>100,967,742</u>	<u>209,002,761</u>

		Fair value measurements at reporting date using			
		Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Investments measured at net asset value
June 30, 2017					
Assets:					
Domestic equities	\$ 44,375,347	12,095,390	—	—	32,279,957 a
Fixed-income securities	133,569,768	115,281,655	18,288,113	—	—
Foreign equities	75,467,795	35,301,593	—	—	40,166,202 b
Money market funds	3,513,864	3,513,864	—	—	—
Natural resources/real estate	36,747,123	7,177,921	—	15,050,412	14,518,790 c
Hedge funds	97,213,275	5,746,915	—	—	91,466,360 d
Private equity securities	16,625,530	—	—	1,955,605	14,669,925 c
Total investments	407,512,702	179,117,338	18,288,113	17,006,017	193,101,234
Beneficial interest in trusts held by others	94,080,627	—	12,469,469	81,611,158	—
Total	<u>\$ 501,593,329</u>	<u>179,117,338</u>	<u>30,757,582</u>	<u>98,617,175</u>	<u>193,101,234</u>

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- a. Investments in this class can be redeemed on a monthly/quarterly basis, with notification provided between 15–30 days prior to redemption.
- b. Investments in this class can be redeemed on a monthly basis with notification provided between 5–30 days prior to redemption.
- c. Investments in this class can be redeemed at the discretion of the investment managers. The Foundation has commitments to contribute additional amounts to this class of investments of approximately \$43,947,452 at June 30, 2018.
- d. Redemption frequency for investments in this class range from monthly to annually redemptions, with notification provided between 2–90 days prior to redemption. Additionally, certain investments can be redeemed at the discretion of the investment managers.

The following table presents the Foundation’s activity for assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) as defined in ASC Topic 820 for the years ended June 30, 2018 and 2017:

	Assets		
	Private equity securities	Natural resources/ real estate	Total
Balance at June 30, 2016	\$ 2,375,000	6,440,277	8,815,277
Total gains (losses) included in income:			
Realized	(275,000)	—	(275,000)
Unrealized	(494,395)	18,846	(475,549)
Purchases	350,000	8,591,289	8,941,289
Balance at June 30, 2017	1,955,605	15,050,412	17,006,017
Total gains (losses) included in income:			
Realized	—	415,575	415,575
Unrealized	(275,000)	—	(275,000)
Purchases	—	(118,309)	(118,309)
Balance at June 30, 2018	\$ 1,680,605	15,347,678	17,028,283

Investments in hedge funds, private equity securities, and natural resources/real estate are recorded at estimated fair value based on the net asset value of the Foundation’s ownership interest in the partners’ capital, which includes assumptions and methods that were prepared by the general partner of the limited partnerships and were reviewed by the Foundation’s management. The Foundation believes that the reported amounts for these investments are a reasonable estimate of their fair value at June 30, 2018 and 2017.

Investments in real estate and certain private equity securities are recorded at estimated fair value at June 30, 2018 and 2017.

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All realized and unrealized gains (losses) for assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3), as defined in ASC Topic 820, are reported in investment return in the accompanying statements of activities.

(10) Long-Term Debt

On April 20, 2017, the Foundation entered into a 10-year \$13.2 million acquisition and construction credit facility (the Loan) for the purchase and renovation of the Charles Atherton House and the Mary Atherton Richards House (the Atherton property). The Loan is secured by the fee simple interest and improvements on the Atherton property, along with an assignment of a long-term lease and rents due thereunder from the University. Under terms of the credit facility, interest-only payments are required for the first 36 months at a fixed rate of 3.00% and, thereafter, monthly installments of principal and interest, based on a 25-year amortization schedule, at a fixed rate of 4.00% through the remaining term of the Loan. The Loan matures on April 1, 2027. As of June 30, 2018 and June 30, 2017, the outstanding balance on the Loan was \$8.2 million.

The aggregate maturities of the long-term debt for each of the five years subsequent to June 30, 2018 are \$0 in 2019, \$15,949 in 2020, \$195,589 in 2021, \$203,558 in 2022 and \$7,784,904 in 2023 and thereafter.

The Loan contains provisions for nonfinancial covenants. Management believes that the Foundation is in compliance with the covenants in its debt agreement.

(11) Transactions with the University

The Foundation has an agreement with the University to provide fund-raising and alumni services through June 30, 2018. Annual compensation from this agreement amounted to \$3,000,000 for each of the years ended June 30, 2018 and 2017. Under separate agreements to provide fund-raising and alumni services for individual University units, compensation amounted to \$336,961 and \$439,112 for the years ended June 30, 2018 and 2017, respectively. For these payments, sources other than the University tuition and fees special fund were used.

In conjunction with acquisition of the Atherton property in April 2017, the Foundation entered into a 15-year ground lease with the University expiring on April 30, 2032. Monthly lease rent is adjustable every six months during the entire lease term. The monthly lease rent may be increased to reimburse the Foundation for any costs, as mutually agreed upon between the Foundation and the University, in connection with the ownership, management, maintenance and operation of the property, including debt service and cost incurred to acquire the property. For the years ended June 30, 2018 and 2017, monthly lease rent was \$23,037 and \$22,000 per month, respectively. The University paid \$207,330 and 53,089 as rental income for the years ended June 30, 2018 and 2017, respectively.

(12) Subsequent Events

The Foundation has evaluated subsequent events from the balance sheet date through November 12, 2018, the date at which the financial statements were available to be issued.