FINAL VERSION
August 18, 1999

Kamehameha Schools Bishop Estate
Supplemental Appendix to Form 1023
Reaffirmation Submission
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TABLE OF CONTENTS

BACKGROUND

Kamehameha Schools Bernice Pauahi Bishop Estate (“KSBE”) was created in 1884 pursuant to the Last Will and Testament and Codicils (the “Will”) of Ke Ali’i Bernice Pauahi Bishop, the last direct descendant of Hawai’i’s royal Kamehameha line (see the Will attached as

Exhibit A). In her Will, Princess Pauahi set forth that her inheritance be used "to erect and maintain in the Hawaiian Islands two schools, each for boarding and day scholars, one for boys and one for girls to be known as, and called the Kamehameha Schools."

Under the auspices of the Will, the Kamehameha School for Boys first opened October 3, 1887 with thirty-four students. Seven years later, on December 19, 1894, the Kamehameha Schools for Girls began operating with twenty-seven students.

Through the decades, what began as two separate schools is now one of the largest private schools in the United States and provides a variety of educational opportunities. Today, KSBE educates approximately 4,000 students every year.

On February 2, 1939, the IRS determined that KSBE was a tax-exempt organization under Section 101(6) of the Revenue Act of 1938 (predecessor to IRC Section 501(c)(3)), which the IRS reconfirmed by a letter dated November 28, 1952. Additionally, the IRS determined that KSBE was an educational organization under IRC Section 501(c)(3) on April 16, 1969. On September 10, 1986, the IRS reconfirmed KSBE as an exclusively charitable trust under Section 501(c)(3) of the Internal Revenue Code and as an educational institution under Sections 509(a)(1) and 170(b)(1)(A)(ii) of the Internal Revenue Code, respectively.

For over one hundred years, the Kamehameha Schools have continuously provided quality education to descendents of Hawaiian ancestry (see the technical advice memorandum regarding KSBE's admissions policy attached as Exhibit B). In those years, approximately 17,000 students have graduated from the Kamehameha Schools.

Kamehameha Schools Bishop Estate
Supplemental Appendix to Form 1023
Reaffirmation Submission
FEIN: 99-0073480

The educational purpose of KSBE is articulated in its Mission and Vision Statements. These Statements will help guide future Trustees in their effort to provide a quality education to children of Hawaiian ancestry.

Kamehameha Schools Bishop Estate
Supplemental Appendix to Form 1023
Reaffirmation Submission
FEIN: 99-0073480

MISSION

Kamehameha Schools Bishop Estate exists to carry out in perpetuity the wishes of Ke Ali'i Bernice Pauahi Bishop to educate children and youth of Hawaiian ancestry to become good and industrious men and women. This Mission will be accomplished through the Kamehameha Schools as resources permit.

To accomplish this Mission KSBE will:

- Promote the educational development and growth of all people at KSBE;
- Foster Protestant religious worship, morals and spiritual values;
- Prudently and actively manage assets to meet our educational goals;
- Conduct ourselves with a clear commitment to *po'okela* – excellence;
- Encourage, cultivate and inspire students, graduates and staff to serve the Hawaiian community and the community at large;
- Preserve and perpetuate Hawaiian culture, traditions and values;
- Instill throughout the organization Hawaiian ancestral values including: *Pono* – To be moral and proper; *'Imi 'Ike* – To seek Knowledge; *Laulima* – To work cooperatively; *Lokomaika'i* – To share; *Na'au Pono* – To possess a deep sense of justice; *Malama* – To care for each other; and *Ha'aha'a* – To be humble.

FINAL VERSION
August 18, 1999

Kamehameha Schools Bishop Estate
Supplemental Appendix to Form 1023
Reaffirmation Submission
FEIN: 99-0073480

VISION

To carry out in perpetuity the wishes of Ke Ali'i Bernice Pauahi Bishop to educate children and youth of Hawaiian ancestry to become good and industrious men and women, the Kamehameha Schools Bishop Estate embraces as its Vision for KSBE the following 3 R's of Educational Responsibility:

> **Reach.** The Trustees of KSBE commit themselves to expanding the reach of KSBE educational resources to children and youth of Hawaiian ancestry through the prudent management of assets, planned increases in enrollment in existing programs and selective new programs, and through the use of new teaching and telecommunications technologies. The staff of KSBE commit themselves to assist the Trustees in achieving the educational goals and objectives of KSBE.
>
> **Readiness.** The administration, faculty and staff of Kamehameha Schools Bernice Pauahi Estate commit themselves to readying children and youth of Hawaiian ancestry to become good and industrious men and women through a planned program of high quality and cost-effective educational services.
>
> **Return.** The alumni and students of Kamehameha Schools commit themselves to returning to the Hawaiian community through their leadership and service some of the benefits they have received from their association with Kamehameha Schools.

ORGANIZATIONAL GOALS

Kamehameha Schools Bishop Estate
Supplemental Appendix to Form 1023
Reaffirmation Submission
FEIN: 99-0073480

Understanding the tasks required of all at KSBE to insure the successful implementation of the Will of Ke Ali'i Pauahi will be reflected in KSBE's statement of Goals. Although to be developed as a part of the strategic planning process described below, these Goals will be designed as organizational goals that will be used to shape both the current strategic planning activity, and subsequent operational planning endeavors. These Goals will be reviewed by the executive staff of KSBE who are the individuals who will participate in the development of the Goals and the development of appropriate strategic objectives. The strategic objectives will be specific, time-limited, measurable and achievable. The timetables and strategies for accomplishing these objectives will be detailed in a series of KSBE operational plans that will be developed based on the strategic plan.

FINAL VERSION
August 18, 1999

Kamehameha Schools Bishop Estate
Supplemental Appendix to Form 1023
Reaffirmation Submission
FEIN: 99-0073480

EDUCATION PROGRAMS AND SERVICES

Current Educational Programs

Kapalama Campus: On its central Kapalama Height Campus ("Kapalama Campus"), located on six hundred acres of land in Honolulu, KSBE operates the Kamehameha Elementary School and Kamehameha Secondary School ("Kamehameha Schools"). A preschool is also located on the Kapalama Campus.

The Kamehameha Elementary School curriculum is designed to prepare children for a challenging college preparatory education at the Kamehameha Secondary School ("Secondary School"). The curriculum emphasizes development of the whole child through academics, social skills, the arts, culture and physical education. Additional activities foster cultural awareness and promote social, emotional and spiritual development.

The Secondary School is a college preparatory school for Hawaiian students. The student body numbers approximately 2,500 in grades seven through twelve. In addition to classrooms and laboratories, the Secondary School includes two learning centers, a television studio, a performing arts complex, athletic facilities and a chapel. There are also dormitories for about five hundred boarding students.

The academic program at the Secondary School is rigorous. Extensive offerings in the academic areas (e.g., English, science) as well as performing and visual arts and health and fitness, challenge students and prepare them for the future. In addition, an honors program with advanced placement courses in all major subject areas is offered to the academically talented students. The Secondary School also offers its students a wide range of extracurricular activities and special opportunities outside Hawai'i, such as the Student Exchange Program and the Summer Talent Search Program.

Approximately four hundred and fifty students graduate from the Secondary School annually. Over ninety percent of Kamehameha graduates continue their education at institutions of higher learning, including such schools as Harvard, Stanford, Princeton and Columbia. Kamehameha graduates are among the ranks of doctors, engineers, business and government leaders and other professionals throughout the United States and the world.

Additional Educational Facilities: In line with its vision of expanding KSBE's educational resources to children and youth of Hawaiian ancestry, KSBE has started elementary schools on each of the islands of Maui and Hawai'i. Additionally, KSBE operates family-based education centers that include preschool programs throughout the State of Hawai'i.

Outreach Programs and Preschools: On June 17, 1999, the Trustees unanimously moved to establish an expansive educational outreach program and expand the reach of KSBE's preschools. Several important steps are part of this directive including the addition of preschool instruction for three-year-olds (previously limited to four-year-olds); the establishment of a new Kamehameha Schools' partnership with the State Department of Education; and the development of a new Kamehameha parent-infant educational program. State and Kamehameha School officials have noted that this program will have a significant effect on the education of children throughout Hawai'i.

Summer Programs: Campus Day Programs and Campus Boarding Programs are two summer programs operated by KSBE. These programs include Summer School, Performing

Arts Academy, Summer Science Institute, Ho'omaka'ika'i Explorations, Kamehameha Computer Camp, Kulia i Ka Pono, and International Studies Institute.

Publishing

Kamehameha Schools Press is the educational publishing arm of KSBE. In the beginning years of Kamehameha Schools, students learned printing as a craft, producing publications such as newspapers and manuals.

The first book identified as a Kamehameha Schools Press publication was published in 1933 and entitled, "Ancient Hawaiian Civilization." During the next twenty-five years Kamehameha Schools Press produced many other classic books on Hawai'i. However, in-house printing of books ended when Kamehameha Schools' curriculum shifted away from vocational and towards college preparatory in the 1960s.

Responding to the needs of teachers at the institution and the community at large for specialized materials, Kamehameha Schools Press now regularly issues new publications. Such publications include reference books on Hawaiian history, adult- and student-level biographies of key figures in Hawaiian history, collections of Hawaiian folklore and curriculum materials for the teaching of Hawaiian history and studies at various grade levels. One of the Kamehameha Schools Press's newest efforts is the re-issuing of biographical and folklore titles in modern Hawaiian translations, thus supporting and leading the contemporary revitalization of Hawaiian as a living spoken language.

The Future

KSBE's commitment to education will increase in the next hundred years. The Trustees are embarking on a number of initiatives that will expand educational opportunities for children of Hawaiian ancestry (for example, the outreach and preschool programs discussed above). In order to better identify programs that will serve the Trustees' goal of "touching as many of the beneficiaries" as possible, a strategic planning process is being undertaken.

Kamehameha Schools Bishop Estate
Supplemental Appendix to Form 1023
Reaffirmation Submission
FEIN: 99-0073480

STRATEGIC PLANNING

Request for Proposals

On October 2, 1998, sixteen stipulations involving recommendations for KSBE and its accounts were filed in the First Circuit Court of the State of Hawai'i (the "Probate Court"). In accordance with Stipulations No. 5 and 13, on June 15, 1999 the Probate Court approved a stipulation for a request for proposals ("RFP") in connection with KSBE's strategic planning (Exhibit C). The RFP has been issued by KSBE and responses have been received.

The RFP states that the strategic planning project will include the development of an educational plan in conjunction with a detailed spending plan, which in turn, will be supported by an investment plan. The educational plan will take into account the future potential of the financial resources of KSBE including all assets held by its taxable subsidiaries and tax-exempt affiliates, including Kamehameha Activities Association ("KAA") (hereinafter the term "KSBE Organizations" refers to KSBE, its subsidiary and supporting organizations including, without limitation, KAA and Bishop Holdings Corporation and the term "KSBE" refers to the Trust Estate). The spending plan (see discussion below) will be refined to meet projected educational program needs. The principal focus of this interrelated planning process is the furtherance of the educational mission of KSBE.

KSBE has received four proposals out of the eleven consulting firms solicited. After examination of these proposals, the Trustees will select a nationally known consultant to assist in KSBE's strategic planning. The RFP sets forth that work on the project will commence no later than thirty days from the date the strategic planning firm is engaged. The comprehensive educational and financial strategic plan and recommended governance structure to implement such plans must be completed and delivered to KSBE within twelve months from the date of engagement of the firm.

Kamehameha Schools Bishop Estate
Supplemental Appendix to Form 1023
Reaffirmation Submission
FEIN: 99-0073480

SPENDING AND INVESTMENT POLICY

Cambridge Associates has been engaged to assist KSBE in developing new integrated investment and spending policies consistent with the new and expanded educational program needs that are being identified and developed, in conjunction with the strategic planning process discussed above. These policies have been developed to ensure that the investment and spending policies are consistent with the educational objectives of KSBE and will be implemented as described below.

Development of an Interim Comprehensive Spending Policy

As part of KSBE's efforts to further its educational purposes, new and expanded educational program needs are already being identified and developed. It is anticipated that additional programs will be identified for consideration. A sustainable Spending Policy based upon a "Financial Equilibrium" concept (Exhibit D), developed with the assistance of Cambridge Associates, has been adopted. As provided by the Spending Policy, the target rate for expenditures on educational programming is 4 percent (the endowment spending rate) of the average market value of the investment assets (as modified as described below) of KSBE and the KSBE Organizations. With respect to fluctuations in the spending rate, KSBE will make every effort to ensure that actual spending will not fall below 2_ percent or exceed 6 percent of the average market value of included assets.

This Spending Policy has been developed taking into consideration several factors including the specific nature of assets of KSBE and the KSBE Organizations. For instance, when targeting the percentage of assets to be spent, certain assets may not be considered. As an example, the Schools and the assets used directly in educational programming will be excluded. Another example of excluded assets is the Hawaiian real estate classified as agricultural and conservation land. However, although the agricultural and conservation land is excluded from the calculation of KSBE's spending rate, the net income from this land (revenue less management and upkeep costs) will be spent on educational program expenses.

The Spending Policy represents the efforts of KSBE to further its tax-exempt purpose and its dedication to educational endeavors. The Spending Policy takes into consideration and addresses several items including the fact that KSBE is a perpetual trust, KSBE and the KSBE Organizations are the dominant source of revenues for KSBE (as opposed to gifts or donations), a need to moderate the volatility of investment markets exists, and KSBE needs flexibility in preparation for significant expansion of programs and changes in investment strategy. Under the provisions of the Spending Policy, investment related expenses are not included within the purview of the endowment spending rate. Rather, investment expenses are to be charged against the investment return of KSBE and the KSBE Organizations.

Once implemented, the educational program expenditures will be compared to the spending thresholds calculated pursuant to the Spending Policy. To the extent excess funding is available, additional program opportunities will be identified. If there is a shortfall, through the budgeting process KSBE will determine whether endowment or other assets, such as those of a subsidiary or an affiliate, should be liquidated in order to fund educational programs.

Investment Planning

The long term financial objective of KSBE and the KSBE Organizations is to provide a perpetual source of revenue to fund the organization's educational programs. In order to achieve this financial objective, KSBE and the KSBE Organizations should attain an average annual real return (as described below) equal to 5 percent (net of investment related expenses). Thus, the long-term Investment Objective of KSBE and the KSBE Organizations is this 5 percent average annual real return percentage.

A comprehensive initial Investment Policy supporting the expanded educational mission of KSBE while maintaining financial stability has been developed with the assistance of Cambridge Associates and adopted by KSBE (Exhibit E). This includes an asset allocation strategy that, while recognizing the unique character of KSBE's Hawaiian real estate holdings, is designed to support the expanded program service needs, maintenance of KSBE's physical facilities, and the perpetual nature of the endowment. Further, the Investment Policy takes into consideration several competing objectives including the need for moderation of the volatility of the market value of KSBE and the KSBE Organizations in order to provide a stable and growing source of support as well as the need to maintain adequate levels of liquidity to meet spending requirements and maintain diversification. The Investment Policy balances the need for predictable cash flow and the desire to maximize the return on endowment assets.

The assets affected by the Investment Policy include KSBE's and the KSBE Organizations' long-term investment assets ("Endowment Fund"). However, the Endowment Fund does not currently include agricultural and conservation land holdings or reserve funds of KSBE and the KSBE Organizations.

Management will be charged by the Board of Trustees to execute the Investment Policy. With the assistance of Cambridge Associates, current investments will be analyzed against the Investment Policy and the asset allocation strategy to assess the long-term "fit" of each investment into KSBE's overall plan. As appropriate, prudent exit strategies for selected investments will be developed.

Kamehameha Schools Bishop Estate
Supplemental Appendix to Form 1023
Reaffirmation Submission
FEIN: 99-0073480

KSBE has two general categories of assets, Core Assets consisting of Hawaiian real estate and other non-core investment assets. The Investment Policy provides for the use of established and institutional quality third-party investment managers for the majority of non-core assets. Along with other implementation guidelines, KSBE will establish policies for each managed portfolio in order to ensure that its marketable stock portfolios, in aggregate, are well diversified.

The Investment Policy provides for a formal review of the Investment Policy at least every five years with the assistance of a nationally recognized investment consulting firm, in order to assess the continued appropriateness of the Investment Policy. Included within this review will be a determination whether all or some of the agricultural land should be included in the Endowment Fund. The Investment Policy also provides for the continuous evaluation and adjustment to investment policies as necessary between formal reviews. Further, KSBE will undertake a comprehensive review of the Investment Policy in conjunction with the overall strategic planning process to ensure the investment objectives and vehicles are consistent with the educational objectives of KSBE.

With input from Cambridge Associates, proposed policies and procedures have been developed to review investment performance annually. The Special Master is reviewing these policies and procedures with the assistance of Arthur Andersen. KSBE has agreed in Stipulation No. 8 (Exhibit F), that investment return will be analyzed against appropriate benchmarks, which have been established as part of the proposed policies and procedures. Establishment of benchmarks is critical to the long-term performance of an institution's investment program. If benchmarks are to be meaningful they must reflect the true purpose of the fund, be realistically achievable in the investment markets, be clearly quantifiable and incorporate a stated time horizon. As is typically done by large endowments, KSBE will use two sets of benchmarks; 1) a long-term benchmark for the total fund that reflects its financial objectives and 2) shorter-term benchmarks that compare fund results with current market returns. Also in accordance with Stipulation No.8, KSBE will annually prepare benchmarked investment performance schedules. The schedules shall be audited and attached to the annual financial statements submitted to the Probate Court with annual accounts of the Trustees (Exhibit L).

Under Stipulation No. 9 (Exhibit F), investment return analyses will be done utilizing measures such as time weighed return and/or internal rate of return to allow for meaningful comparisons. These calculations will be compared to the benchmarks identified above for purposes of evaluating an investment's performance and its ongoing place in the portfolios of KSBE and the KSBE Organizations.

Kamehameha Schools Bishop Estate
Supplemental Appendix to Form 1023
Reaffirmation Submission
FEIN: 99-0073480

GOVERNANCE

Selection of Trustees

The Will of Bernice Pauahi Bishop provides that KSBE shall have five trustees and, furthermore, that the trustees be selected by the Justices of the Supreme Court of Hawai'i. Four of the five current Supreme Court Justices have stated that they will no longer make appointments. Currently, it appears that the Probate Court has jurisdiction over the Trustee selection process. The Interim Trustees have filed a petition with the Probate Court containing a Recommendation for Trustee Selection Process ("Recommendation"), which sets out a proposed selection process for Trustees. Although the selection process may change after review by the Court, it is expected that the Court, in the exercise of its statutory and inherent powers, will adopt this or a similar process to provide for the selection and appointment of future Trustees.

The Recommendation (Exhibit G) contains several provisions regarding Trustee selection, including the Court appointment of a Trustee Selection Committee ("Committee"). Service on the Committee would be voluntary and members of the Committee would serve without pay from either KSBE or the Court. Under provisions of the Recommendation, the Committee would represent a diversity of interests and backgrounds such as the students' parents, the alumni of the Schools, the Hawaiian community, and the community-at-large. Further, the Committee would be composed of individuals qualified to fulfill the Committee's responsibilities. Additionally, in order to ensure their independence, the Recommendation imposes a disclosure requirement on Committee members in the event that a conflict of interest occurs between a member and an applicant for the position of Trustee.

Kamehameha Schools Bishop Estate
Supplemental Appendix to Form 1023
Reaffirmation Submission
FEIN: 99-0073480

Under provisions of the Recommendation, the Committee is charged with the task of screening potential candidates for Trustee and ensuring that any final candidate meets the qualifications to sit as a Trustee. Once the Committee has identified its top candidates, the names will be submitted to the Probate Court. The Court will appoint a nominee from that list or reject the list for cause and return the matter to the Committee for further nominations.

The Recommendation also contains a discussion of identified criteria and qualifications for a Trustee. In drafting the Recommendation, KSBE anticipated that the Probate Court would examine qualifications for serving as Trustee based on role and new organizational structure (see discussion below). As such, the Recommendation provides that a potential Trustee must have expertise in strategic planning and policy, business administration, finance and investment, or other general areas of interest such as education, law, governance or finance. The desired qualities or characteristics of a Trustee include a demonstrated reputation of integrity, the capacity to fulfill the responsibilities of a fiduciary under trust law, a commitment to the best interests of children, consistent and active leadership in the community-at-large, and a willingness and sincerity to uphold the purposes of KSBE.

In order to ensure the integrity of the Board of Trustees, the Recommendation also provides that the Trustees be subject to term limits. The applicable provisions state that a Trustee should serve a standard term of five years. At the end of the term, the Trustee may re-apply. The Committee could consider the Trustee for reappointment, along with other eligible candidates for the open Trustee position. Additionally, the Recommendation provides for a maximum service of two terms, with a recommendation to the Court for staggered terms in the event more than one trustee must be selected at a time.

Kamehameha Schools Bishop Estate
Supplemental Appendix to Form 1023
Reaffirmation Submission
FEIN: 99-0073480

Role of Trustee/Organizational Structure

The Trustees have adopted a "Governance Policy" ("Policy") which clearly defines the duties and responsibilities of the Trustees/Board (a copy of the Policy is attached as Exhibit H). The Policy provides:

> The Trustees' role is to create, sustain, and fulfill a vision whose primary focus is on furtherance of education, while leaving the development and execution of the plan to fulfill the vision to the Chief Executive Officer (CEO). **The Board sets policy; management implements policy; the Board is responsible for oversight of the Estate while the day-to-day management of the operations of the Estate is the responsibility of the CEO.** [emphasis supplied]

This definition is based on the specific acknowledgment included in the Policy preamble that "KSBE is a perpetual, charitable trust estate established for exclusively educational purposes, namely, 'to erect and maintain…the Kamehameha Schools.' All activities of KSBE must be consistent with and in furtherance of this primary purpose." In committing to governing KSBE "…through a continually improved commitment to its vision, mission and values" the Board is ensuring that the role of Trustee is now clearly defined with a primary focus on the furtherance of the educational mission of the KSBE.

As part of the Trustees' clearly defined role, the Policy provides that the Trustees are to be fiduciaries who serve to exercise oversight over KSBE. Further, as previously stated, the Policy provides that the Trustees will not be involved in management of the day-to-day operations of KSBE. Rather, the Trustees will primarily establish the policies of KSBE, including ensuring that education is KSBE's primary focus.

The Policy sets forth the organizational structure (See Exhibit I) of KSBE that has been agreed upon as a current approach to implementing Stipulation No. 14, part of the sixteen stipulations filed with the Probate Court on October 2, 1999 (see Exhibit F). Under this structure, a CEO will independently carry out the Policy decisions of the Trustees. The Board of Trustees will "[s]elect, regularly evaluate, fix the compensation of, and where appropriate, hire or replace the CEO of KSBE." The CEO is then "authorized to establish all further relevant administrative regulations, make all decisions, take all actions necessary to attain the goals and objectives of the Board, establish all practices and coordinate all new or expansions of programs." Certain day-to-day operations of the School will be led by the President of the School who reports directly to the CEO.

Also included in the Policy adopted is a specific provision entitled "Manner of Governing." Again, this policy requires the Board to maintain an oversight role. The policy requires the Board to "[e]nforce upon itself whatever discipline is needed to govern with excellence. Discipline will apply to matters such as attendance, policymaking principles, [and] respect of roles…." It further provides that the Board will "[m]onitor and discuss the Board's process and performance at least quarterly. Self-monitoring will include comparison of Board activity and discipline to policies in the Governance process and Board-CEO/President Relationship categories."

The organizational structure of KSBE and the KSBE Organizations ensures that an adequate system of checks, balances, and affirmative disclosure requirements exists within KSBE and the KSBE Organizations to provide safeguards against any abuse of power by the Trustees, individually or collectively, and any abuse of power by any senior managers on the staff of KSBE or the KSBE Organizations, individually or collectively. Additionally, there will be an adequate system of checks, balances, and affirmative disclosure requirements to provide safeguards against the mismanagement of Trust assets by the Trustees, or by any individuals or entities given access to said assets by KSBE or the KSBE Organizations.

The overall Governance Policy highlights the high fiduciary obligations of the Trustees and includes a Board of Trustees' Code of Conduct. The Trustees also have adopted a detailed Conflict of Interest Policy (see Exhibit J) as required by Stipulation No. 16 (see Exhibit F). This Conflict of Interest Policy applies equally to officers and key employees.

With respect to resignation or removal of a Trustee, the 'Forward' of the Policy states that "if for any reason a Trustee cannot fulfill or has violated his/her fiduciary duties and obligations, he or she, without hesitation, must voluntarily and loyally resign as a Trustee." In addition, a Trustee is subject to the laws of the State of Hawai'i including Hawai'i Revised Statutes (HRS) Section 560:7-201 which provides for the removal of a trustee for cause by the Circuit Courts of the State of Hawai'i. Removal is warranted if the court concludes that allowing a trustee to continue office would be detrimental to the estate. Grounds for removal of a trustee include, but are not limited to, the following:

- Incapacity;
- Unfitness;
- Extreme personal improvidence, insolvency, or bankruptcy;
- Commission of a serious crime, especially one involving dishonesty;
- Misconduct evidencing moral turpitude or abuse of office;
- Knowing failure to obey a court order;
- Knowing failure to comply with law and regulation applicable to the trust estate;
- Knowing failure to render complete and accurate accounts;
- Knowing misrepresentation of the affairs of the trust estate;

- Disobedience to the directions and terms of the trust instrument;
- Failure to act appropriately in the affairs of the trust;
- Activity detrimental to the obvious best interest of the trust;
- Neglect of the office of trustee;
- Unreasonable or corrupt failure to cooperate with co-trustees;
- Failure to respond in a timely and reasonable manner to reasonable requests of the court appointed master or the Attorney General as *parens patriae* for information concerning the affairs of the trust estate;
- Mismanagement of the trust estate;
- Commingling trust and personal funds;
- Acquiring a personal interest adverse to the trust;
- Self-dealing;
- Permitting or accepting any degree of private inurement;
- Failure to disclose known conflicts of interest;
- Failure to abstain from any involvement in transactions in which the trustee has a conflict of interest;
- Appropriation of trust property to personal use;
- Making unauthorized dispositions of trust property;
- Waste of trust assets;
- Activities which jeopardize the tax exempt status of the trust estate;
- Activities which expose the trust estate or its subsidiaries to significant civil or criminal penalties and forfeitures; and
- Willful and wanton abuse of discretion.

A trustee whose removal is sought has a fiduciary duty to assess the allegations against him or her. If it is clear that the allegations are substantially accurate and continued service would be detrimental to the estate, the trustee should resign.

With respect to documentation of the oversight function of the Board of Trustees, KSBE has established procedures which will ensure the proper and complete documentation and retention of all educational, investment and management decisions made by the Board of Trustees as well as key employees. The Board of Trustees' minutes will contain documentation to indicate the Trustees present at the meeting and will contain a record of the matters voted on, in addition to the acceptance or rejection of the particular matter. Any staff reports presented will be attached and filed with the appropriate minutes.

Trustee Compensation

A Probate Court approved program for setting Trustee compensation has been established as well as a system for monitoring compliance with that system (see Probate Court Order dated May 10, 1999 at Exhibit K), with the participation of KSBE, the Master and the Attorney General (see Stipulation No. 15 attached as Exhibit F).

Under the compensation plan ("Plan"), the Probate Court shall periodically appoint a committee to determine the compensation of the Trustees of KSBE ("Compensation Committee"). Pursuant to the Order, the Compensation Committee must consist of "knowledgeable and informed persons, each of whom the Court finds to possess the integrity, probity, competence and disinterested status necessary to be qualified and serve as an independent and unconflicted Committee member under applicable IRS regulations."

The sole purpose of the Compensation Committee is the determination of what constitutes a reasonable amount of annual compensation to be paid to each of the Trustees of KSBE. The Probate Court Order ("Order") allows the Compensation Committee to "commission an independent compensation survey from a national, independent, professional consulting firm active in the field of executive and trustee compensation." The Order further provides that the survey must be based on "functionally comparable positions."

Based on the study (or studies) commissioned, the Compensation Committee will report its determination of reasonable Trustee compensation which may be expressed as a range or an amount up to a specified limit. The determination may provide for differing levels of compensation for individual Trustees based upon any considerations determined to be appropriate under state and federal law and regulations. The Compensation Committee's report must include an explanation of the basis for its determination and must be accompanied by copies of all documents referred to in its report.

The Probate Court will schedule a hearing regarding the determination rendered by the Compensation Committee and then may approve, disapprove or modify the recommendation. If the Probate Court modifies the recommendation, the Judge is required to do so in a manner "consistent with applicable provisions of state and federal law and regulations with the object of assuring that the compensation paid the KSBE Trustees is reasonable within the meaning of both state and federal law and regulations."

Kamehameha Schools Bishop Estate
Supplemental Appendix to Form 1023
Reaffirmation Submission
FEIN: 99-0073480

After the CEO is in place and following an appropriate transition period, KSBE will submit a Ruling Request to the IRS seeking approval for a method for determining Trustee compensation going forward.

The Compensation Committee shall be reasonably compensated for its services with the compensation to be fixed by the Court. No amount of the compensation will be paid to the Compensation Committee for its services until a recommendation has been provided to the Court.

On May 10, 1999, the Probate Court appointed the initial Compensation Committee. The Trustees have provided the Compensation Committee with a copy of the Governance Policy that has been adopted which outlines the Organizational Structure being implemented and the associated Role of the Trustees (see discussion above). Further, the Compensation Committee has selected a compensation consultant to conduct the required survey. The members have also been briefed on the intermediate sanctions legislation and proposed regulations.

Pursuant to Stipulation No. 14, KSBE, as of August 6 , 1999, adopted a plan to institute a single Chief Executive Officer ("CEO") structure to oversee the management of KSBE. The CEO will serve under and report directly to the Board of Trustees. It is envisioned that this new management structure will give the Trustees the responsibility of creating, sustaining and fulfilling KSBE's vision and mission, while making the CEO accountable for the development and execution of the plan to fulfill that mission and vision. Thus, any determination of reasonable compensation for Trustees will take this organizational structure and the duties delegated to the CEO into consideration.

Kamehameha Schools Bishop Estate
Supplemental Appendix to Form 1023
Reaffirmation Submission
FEIN: 99-0073480

FINANCIAL REPORTING & INTERNAL CONTROLS

The Probate Court, as mandated by state law, will continue to oversee the affairs of KSBE. These oversight functions include appointing KSBE's Board of Trustees and reviewing and approving KSBE's Annual Accounts. In addition, several other controls are being adopted by KSBE including internal controls such as an internal audit function, employment and contract procedures, standard procurement practices, and internal control review.

Internal Audit Function

The Board of Trustees of KSBE and the KSBE Organizations are re-implementing an independent internal audit function to achieve, among other things, the following objectives:

- The terms of the Will of Bernice Pauahi Bishop are fulfilled in perpetuity.
- The assets of KSBE are properly safeguarded and used primarily for educational purposes.
- Policies and procedures established by the Board of Trustees are being adhered to.
- Compliance with applicable state and federal laws and regulations.
- Compliance with the terms of the Closing Agreement between KSBE and the IRS is monitored and maintained throughout the duration of the Closing Agreement.

As a large complex organization with significant land holdings and investments, KSBE is subject to certain significant business risks and challenges. As a charitable trust, it must comply with numerous state and federal laws, court orders and stipulations entered into since inception. Because KSBE is also a tax-exempt organization, it must abide by certain strict rules and regulations to maintain its tax-exempt status.

For these as well as other important reasons, KSBE will re-implement an independent internal audit function to internally monitor its processes to ensure the organization's risks are adequately managed, that it is in compliance with legal and regulatory restrictions and that it is effectively utilizing the resources of KSBE to fulfill the terms of the Will of Bernice Pauahi Bishop. This function will be established in an organized manner with the proper purpose, structure, resources and commitment from the Board of Trustees.

The Board of Trustees has an established policy for the Internal Audit Function that outlines the mission of this function, its goals and objectives, as well as a general audit strategy. The mission of this function is as follows:

> The mission of the Internal Audit Department is to assist the Trustees in the effective discharge of their fiduciary responsibilities through independent appraisal and examination of all control functions within KSBE, including functions of the Board of Trustees.

In order to establish a strong internal audit function and achieve the stated goals and objectives, the Board of Trustees has developed the following internal audit structure:

> *Audit Committee:* KSBE will establish an audit committee that will be responsible for oversight of the audit process including both the internal and external audit functions. One of the primary responsibilities of the Audit Committee will be to set the "tone" for quality operational, financial and investment reporting, sound business risk

controls and ethical behavior throughout the organization. The Audit Committee will be comprised of two Trustees, the Court Master and a representative from the State of Hawaii Attorney General's office.

Director of Internal Audit: The Board of Trustees recognizes that a very important aspect of establishing an effective internal audit function is having a qualified Director of Internal Audit ("Director"). The Board of Trustees will appoint an individual with strong leadership, interpersonal, technical (business, finance and accounting), analytical, administrative and supervisory skills. Because the KSBE is a tax-exempt organization, KSBE will seek an individual for this position who also possesses tax knowledge and has experience in the area of tax-exempt organizations (see Appendix E of the Governance Policy attached as Exhibit H).

The Director will be empowered with full authority for directing the internal audit function of KSBE and report directly to the Audit Committee. The primary role of the Director will be to develop and direct a Comprehensive Audit Program within KSBE that accomplishes the mission as stated above. Administrative responsibility (i.e. performance evaluations, salary reviews, etc.) for the Director will rest with an appropriate level of upper management, which in the proposed organizational structure would be the Chief Executive Officer (CEO) of KSBE.

Internal Audit Function: In the execution of its responsibilities, the internal audit function will be independent of all other departments within the organization. The internal audit function will be a separate department reporting directly to the Audit Committee and, for audits that relate to or impact the taxable subsidiaries or affiliated organizations, reporting will also be made to the Boards of Directors of the applicable taxable subsidiary or affiliated organizations.

The individuals in the internal audit function will have full and unrestricted access to all KSBE information and records, including those of the taxable subsidiaries, the affiliated organizations and the Board of Trustees. Accordingly, appropriate protections will be established to ensure the individuals in this function are immune from retribution from any member of the Board of Trustees, individually or in the aggregate, in the execution of their duties. Protections will also be made to ensure individuals within KSBE feel free to provide information to the internal audit function without detrimental or retaliatory actions as a result of their activities.

Due to the unlimited access to all KSBE information, all internal audit personnel will be held to the highest standard of integrity and confidentiality. They will serve as a role model for other departments.

Internal Audit Staffing: The Audit Committee and Director will determine the necessary staffing requirements for this function. The team will be comprised of qualified individuals with the varying core competencies necessary to effectively execute the audit work plan. The Board of Trustees has recognized that the way to build an effective internal audit group is not to limit the staff to those with traditional auditing backgrounds. The complexity of the organization will require the internal auditors to understand KSBE's strategy and the specific aspects of its critical program and operational processes. Therefore, KSBE will identify/hire individuals with experience in areas that are relevant to KSBE's educational purpose in addition to individuals with traditional audit experience.

Kamehameha Schools Bishop Estate
Supplemental Appendix to Form 1023
Reaffirmation Submission
FEIN: 99-0073480

All audit results will be made in writing and addressed to the CEO, CFO, Audit Committee and the Principal Executive(s) responsible for the area audited. For the taxable subsidiaries and affiliated organizations, the report will also be addressed to the entity's Board of Directors (or designated committee), President and Chief Financial Officer. Copies will also be provided to other appropriate audit customers/process owners. Copies of all internal audit reports will also be kept on file by the Director and made available to the Court Master during the Annual Account review process.

Under the terms of the Closing Agreement, KSBE is to establish an independent internal audit function to monitor KSBE's compliance with the terms of the Closing Agreement, all Court orders and stipulations relevant to the Agreement and adherence to the Conflict of Interest Policy. The internal audit function will have responsibility to annually report the results of their monitoring of KSBE's compliance to the IRS as "Special Filings" during the term of the Closing Agreement. The Special Filings will be signed under the penalties of perjury and will also be filed by KSBE with the Court Master and the Attorney General of the State of Hawaii. The following summarizes the items to be included in the Special Filing.

- The internal auditor will evaluate and report whether business meetings between the Interim Trustees, Top Executives and the Incumbent Trustees are documented in writing detailing the purpose of the meeting and the persons who attended said meeting. For purposes of this reaffirmation submission, the term "Top Executive" is defined as an "Organization Manager" within the meaning of IRC Section 4958(f)(2).

- The internal auditor will report whether the Trustees are performing an annual performance review of the Chief Executive Officer.

Kamehameha Schools Bishop Estate
Supplemental Appendix to Form 1023
Reaffirmation Submission
FEIN: 99-0073480

- The internal auditor will evaluate whether a trustee or Top Executive has failed to comply with the Conflict of Interest policy during the term of the Closing Agreement. If a violation is identified, the internal auditor will report any apparent conflicts to the Board of Trustees for appropriate action. The internal auditor will include in the Special Filing the disposition of the apparent conflict to the Board of Trustees.

- The internal auditor will monitor KSBE's compliance with its established procurement practices and will review all contracts entered into over $100,000 to ensure the practices were followed.

- The internal auditor will monitor KSBE's employment practices to ensure that appropriate standard employment procedures are followed and will review all new employment contracts over $50,000.

- The internal auditor will evaluate KSBE's compliance with established procedures to ensure the proper and complete documentation and retention of all educational, investment and management decisions made by the Board of Trustees and by the Top Executives. The internal auditor will monitor whether the Board of Trustees' minutes contains documentation to indicate the Trustees present at the meeting and a record of the matters voted on, in addition to the acceptance or rejection of the particular matter. The internal auditor will also ensure any staff reports presented are attached and filed with the appropriate minutes and that in all instances where these documents concern the Trustees' fiduciary responsibilities as Trustees, these documents are readily available for inspection.

- The internal auditor will monitor KSBE's policy of not employing, or paying for the services of an elected or appointed member of the legislative, judicial or executive branches of government, whether state, federal or local, where such a relationship would create the appearance of a conflict of interest, until a period of three years has passed since the individual's status with the governmental entity has terminated.

Financial Statements

Pursuant to Stipulation No. 1 (Exhibit F), KSBE has adopted a specified format for financial statement reporting including the supplemental schedules (see example at Exhibit L). These financial statements will be audited and presented in conformity with orders of or stipulations approved by the Probate Court, and will, at a minimum, conform to general accepted accounting principles (GAAP).

KSBE will submit its financial statements to the Probate Court with the Annual Accounts. Additionally, for the effective period of the Closing Agreement, the financial statements, including all supplemental schedules, will be provided to the IRS.

Investment Schedules

In accordance with Stipulation No. 8, KSBE will annually prepare benchmarked investment performance schedules. The schedules shall be audited and attached to the annual financial statements submitted to the Probate Court with annual accounts of the Trustees (Exhibit L).

Under Stipulation No. 9 (Exhibit F), investment return analyses will be done utilizing agreed upon measures such as time weighed return and/or internal rate of return to allow for meaningful comparisons. These calculations will be compared to the benchmarks identified above for purposes of evaluating an investment's performance and its ongoing place in the portfolios of KSBE or the KSBE Organizations.

Employment and Contractual Relationships

KSBE is reviewing various relationships with providers of services or products in order to evaluate the cost-effectiveness and the efficiency of such relationships. The review of these relationships represents KSBE's effort to minimize waste and maximize the operations of KSBE in order to more effectively further its educational purposes.

KSBE has undertaken a review of existing contractual, consultative, employment, and professional service relationships in existence as of June 30, 1999 to ensure that the services provided under such contracts or through such relationships are necessary to the operation of KSBE and the KSBE Organizations and that the prices and/or compensation paid for such services are reasonable and commensurate with services rendered. Further, all significant job classifications in existence as of June 30, 1999 will be reviewed to ensure that the job positions and compensation for such positions are necessary and appropriate for the accomplishment of KSBE's exempt purpose and that the individuals occupying such positions are qualified to perform the responsibilities of the position.

In a continuing effort to improve efficiency and effectiveness, KSBE will adopt standard procedures for all new contractual and employment relationships. These procedures will be followed for the contracting or hiring of any individual. Documentation will be maintained demonstrating the need for the services, why the proposed service provider/employee is the most qualified candidate, that the price/salary is reasonable and the means to evaluate that the appropriate result/effort is gained from the service provider. In the case of all independent contractors, reports or other evidence that the contracted service was performed will be retained.

Finally, KSBE will establish a policy of not employing, reimbursing, or paying for the services of (including expenses of), an elected or appointed member of the legislative, judicial or executive branches of government, whether state, federal, or local, unless it receives the express permission of the Probate Court or such employee is specifically excluded from this policy under the terms of the Closing Agreement. This policy is applicable only when less than three years have passed since the individual's status with the governmental entity was terminated.

Procurement Practices

KSBE will adopt standard procurement practices to ensure that significant contracts will be awarded on the basis of open and competitive bidding, and that exceptions to competitive bidding will be specifically defined (see attached Exhibit M). These standard procurement practices include establishing approved vendor lists. Vendors would be added to the approved vendor list only if the vendors meet certain criteria established by management. Such criteria will include, but not be limited to, improving quality, gaining access to innovative technology, reducing total cost, and streamlining the purchasing process.

ORDER OF PRECEDENCE

FINAL VERSION
August 18, 1999

Kamehameha Schools Bishop Estate
Supplemental Appendix to Form 1023
Reaffirmation Submission
FEIN: 99-0073480

This reaffirmation narrative is intended to only summarize the exhibits hereto. To the extent there are inconsistencies between this narrative summary and the exhibits, the exhibits control.

Exhibit A

Will of Bernice Pauahi Bishop

Know all Men by these Presents, That I, Bernice Pauahi Bishop, the wife of Charles R. Bishop, of Honolulu, Island of Oahu, Hawaiian Islands, being of sound mind and memory, but conscious of the uncertainty of life, do make, publish and declare this my last Will and Testament in manner following, hereby revoking all former wills by me made:

First. I give and bequeath unto my namesakes, E. Bernice Bishop Dunham, niece of my husband, now residing in San Joaquim County, California, Bernice Parke, daughter of W. C. Parke Esq., of Honolulu, Bernice Bishop Barnard, daughter of the late John E. Barnard Esq. of Honolulu, Bernice Bates, daughter of Mr. Dudley C. Bates, of San Francisco, California, Annie Pauahi Cleghorn of Honolulu, Lilah Bernice Wodehouse, daughter of Major J. H. Wodehouse, of Honolulu, and Pauahi Judd the daughter of Col. Charles H. Judd of Honolulu, the sum of Two hundred Dollars ($200.) each.

Second. I give and bequeath unto Mrs. William F. Allen, Mrs. Amoe Haalelea, Mrs. Antone Rosa, and Mrs. Nancy Ellis, the sum of Two Hundred Dollars ($200.) each.

Third. I give and bequeath unto Mrs. Caroline Bush, widow of A .W. Bush, Mrs. Sarah Parmenter, wife of Gilbert Parmenter Mrs. Keomailani Taylor, wife of Mr. Wray Taylor, to their sole and separate use free from the control of their husbands, and to Mrs. Emma Barnard, widow of the late John E Barnard Esq. the sum of Five hundred dollars ($500.) each.

Fourth. I give, devise and bequeath unto H. R. H. Liliuokalani, the wife of Gov. John 0. Dominis, all of those tracts of land known as the "Ahupuaa of Lumahai," situated on the Island of Kauai, and the "Ahupuaa of Kealia", situated in South Kona Island of Hawaii; to have and to hold for and during the term of her natural life; and after her decease to my trustees upon the trusts below expressed.

Fifth. I give and bequeath unto Kahakuakoi (w) and Kealohapanole, her husband, and to the survivor of them, the sum of Thirty Dollars ($3O.) per month, (not $30. each) so long as either of them may live. And I also devise unto them and to their heirs of the body of either, the lot of land called "Mauna Kamala", situated at Kapalama Honolulu; upon default of issue the same to go to my trustees upon the trusts below expressed.

Sixth. I give and bequeath unto Mrs. Kapoli Kamakau, the sum of Forty Dollars ($4O.) per month during her life; to my servant woman Kaia the sum of Thirty Dollars ($30.) per month during her life, and to Nakaahiki (w) the sum of Thirty Dollars ($30.) per month during her life.

Seventh. I give, devise and bequeath unto Kapaa (k) the house-lot he now occupies, situated between Merchant and Queen Streets in Honolulu, to have and to hold for and during the term of his natural life; upon his decease to my trustees upon the trusts below expressed.

Eighth. I give, devise and bequeath unto Auhea (w) tile wife of Lokana (k) the house-lot situated on the corner of Richard and Queen Streets, now occupied by G. W. Macfarlane & Co; to have and to hold for and during the term of her natural life; upon her decease to my trustees upon the trusts below expressed.

Ninth. I give, devise and bequeath unto my husband, Charles R. Bishop, all of the various tracts and parcels of land situated upon the Island of Molokai, comprising the "Molokai Ranch", and all of the live-stock and personal property thereon; being the same premises now under the care of R. W. Myer Esq.; and also all of the real property wherever situated, inherited by me from my parents, and also all of that devised to me by my aunt Akahi, except the two lands above devised to H. R. H. Liliuokalani for her life; and also all of my lands at Waikiki, Oahu, situated makai of the government main road leading to Kapiolani Park; to have and to hold together with all tenements, hereditaments, rights, privileges and appurtenances to the game appertaining, for and during the term of his natural life; and upon his decease to my trustees upon the trusts below expressed.

Tenth. I give, devise and bequeath unto Her Majesty Emma Kaleleonalani, Queen Dowager, as a token of my good will, all of the premises situated upon Emma Street in said Honolulu, known as Kaakopua, lately the residence of my cousin Keelikolani; to have and to hold with the appurtenances for and during the term of her natural life; and upon her decease to my trustees upon the trusts below expressed.

Eleventh. I give and bequeath the sum of Five thousand Dollars ($5000.) to be expended by my executors in repairs upon Kawaiahao Church building in Honolulu, or in improvements upon the same-

Twelfth. I give and bequeath the sum of Five thousand Dollars ($5000.) to be expended by my executors for the benefit of the Kawaiahao Family School for Girls (now under charge of Miss Norton) to be expended for additions either to the grounds, buildings or both.

Thirteenth. I give, devise and bequeath all of the rest, residue and remainder of my estate real and personal, wherever situated unto the trustees below named, their heirs and assigns forever, to hold upon the following trusts, namely: to erect and maintain in the Hawaiian Islands two schools, each for boarding and day scholars, one for boys and one for girls, to be known as, and called the Kamehameha Schools.

I direct my trustees to expend such amount as they may deem best, not to exceed however one-half of the fund which may come into their hands, in the purchase of suitable premises, the erection of school buildings, and in furnishing the same with the necessary and appropriate fixtures furniture and apparatus.

I direct my trustees to invest the remainder of my estate in such manner as they may think best, and to expend the annual income in the maintenance of said schools; meaning thereby the salaries of teachers, the repairing buildings and other incidental expenses; and to devote a portion of each years income to the support and education of orphans, and others in indigent circumstances, giving the preference to Hawaiians of pure or part aboriginal blood; the proportion in which said annual income is to be divided among the various objects above mentioned to be determined solely by my said trustees they to have full discretion.

I desire my trustees to provide first and chiefly a good education in the common English branches, and also instruction in morals and in such useful knowledge as may tend to make good and industrious men and women; and I desire instruction in the higher branches to be subsidiary to the foregoing objects.

For the purposes aforesaid I grant unto my said trustees full power to lease or sell any portion of my real estate, and to reinvest the proceeds and the balance of my estate in real estate, or in such other manner as to my said trustees may seem best.

I also give unto my said trustees full power to make all such rules and regulations as they may deem necessary for the government of said schools and to regulate the admission of pupils, and the same to alter, amend and publish upon a vote of a majority of said trustees.

I also direct that my said trustees shall annually make a full and complete report of all receipts and expenditures, and of the condition of said schools to the Chief Justice of the Supreme Court, or other highest judicial officer in this country; and shall also file before him annually an inventory of the property in their hands and how invested, and to publish the same in some Newspaper published in said Honolulu; I also direct my said trustees to keep said school buildings insured in good Companies, and in case of loss to expend the amounts recovered in replacing or repairing said buildings.

I also direct that the teachers of said schools shall forever be persons of the Protestant religion, but I do not intend that the choice should be restricted to persons of any particular sect of Protestants.

Fourteenth. I appoint my husband Charles R. Bishop, Samuel M. Damon, Charles M. Hyde, Charles M. Cooke, and William 0. Smith, all of Honolulu, to be my trustees to carry into effect the trusts above specified.

I direct that a majority of my said trustees may act in all cases and may convey real estate and perform all of the duties and powers hereby conferred; but three of them at least must join in all acts.

I further direct that the number of my said trustees shall be kept at five; and that vacancies shall be filled by the choice of a majority of the Justices of the Supreme Court, the selection to be made from persons of the Protestant religion.

Fifteenth. In addition to the above devise to Queen Emma, I also give, devise and bequeath to her (said Emma Kaleleonalani Queen Dowager (sic) the Fish-pond in Kawaa, Honolulu near Oahu Prison, called "Kawa", for and during the term of her natural life; and after her decease to my trustees upon the trusts aforesaid.

Sixteenth. In addition to the above devise to my husband, I also give and bequeath to him, said Charles R. Bishop all of my personal property of every description, including cattle at Molokai; to have and to hold to him, his executors., administrators and assigns forever.

Seventeenth. I hereby nominate and appoint my husband Charles R. Bishop and Samuel M. Damon, executors of this my will.

In witness whereof I, said Bernice Pauahi Bishop, have hereunto set my hand and seal this thirty-first day of October A. D. Eighteen hundred and eighty-three.

BERNICE P. BISHOP (SEAL)

The foregoing instrument, written on eleven pages, was signed, sealed, published and declared by said Bernice Pauahi Bishop, as and for her last will and testament in our presence, who at her request, in her presence, and in the presence of each other, have hereunto set our names as witnesses thereto, this 31st day of October A. D. 1883.

F. W. MACFARLANE

FRANCIS M. HATCH

Codicil No. 1

This is a Codicil to the last Will and Testament of me, Bernice P. Bishop, dated October thirty-first A. D. Eighteen hundred and eighty-three:

1st. I give and bequeath unto Mrs. William F. Allen the sum of One thousand Dollars ($1000.) in place of the amount given to her in my said will.

2nd. I revoke the devise to Her Majesty Emma Kaleleonalani of the premises situated upon Emma Street in Honolulu, known as "Kaakopua", contained in the tenth article of my said will; and in place thereof I give, devise and bequeath unto her, said Emma Kaleleonalani, all of those parcels of land situated in Nuuanu Valley, Oahu, on both sides of the road, known as "Laimi"; to hold for and during the term of her natural life; and upon her decease to my trustees upon the trusts expressed in my said will. Said Emma to also have the fish pond known as "Kawa", as provided in the fifteenth article of my said will.

3rd. In addition to the bequests to my husband named in my said will I also give, devise and bequeath unto my said husband, Charles R. Bishop, the land known as Waialae-nui, as well as Waialae-iki and also the land known as "Maunalua", Island of Oahu; and also all of the premises situated in said Honolulu, known as the Ili of "Kaakopua", extending from Emma to Fort Street and also all kuleanas in the same, and everything appurtenant to said premises; to hold for his life, remainder to my trustees.

4th. I give, devise and bequeath unto Kuaiwa (k) and Kaakaole (w), old retainers of my parents, that piece of land now occupied by them, situated in upper Kapalama, in said Honolulu, called ""Wailuaakio""; to have and to hold for and during the term of their natural lives and that of the survivor of them; remainder to my trustees upon the trust named in my said will.

5th. I give, devise and bequeath unto Kaluna (k) and Hoopii, his wife, those premises now occupied and cultivated by them in Kauluwela, Liliha Street, Honolulu; to have and to hold for and during the terms of their natural lives and that of the survivor of them; remainder to my trustees upon the trusts named in my said will.

6th. I give, devise and bequeath unto Naiapaakai (k) and Loika Kahua his wife, that lot of land now enclosed and occupied by them, in Kauluwela in said Honolulu, the size of said lot not to exceed one acre; to have and to hold for and during the term of their natural lives, and that of the survivor of them; remainder to my trustees upon the trusts named in my said will.

7th. I give and bequeath unto Lola Kahailiopua Bush, of said Honolulu, the sum of Three hundred Dollars ($300.) per year during her minority, to be applied towards her education and clothing; and upon her becoming of age the sum of One thousand Dollars, ($1000.) to her sole and separate use, free from the control of any husband she may marry.

8th. I give and bequeath unto Bernice B. Barnard, of said Honolulu the sum of Three hundred Dollars ($300.) a year during her minority, to be applied towards her education and clothing;

and upon her becoming of age the sum of One thousand Dollars ($1000.) to her sole and separate use, free from the control of any husband she may marry. This in lieu of the $200. given by my will.

9th. I give, devise and bequeath unto my friend Samuel M. Damon, of said Honolulu, all of that tract of land known as the Ahupuaa of Moanalua, situated in the District of Honolulu, Island of Oahu; and also the fishery of Kaliawa; to have and to hold with the appurtenances to him, his heirs and assigns forever.

10th. I give and bequeath unto my servants Kaleleku (k) and (k) his brother, each the sum of Twenty Dollars ($20.) per month, during the term of the natural life of each of them.

11th. I revoke so much of the fifth article of my said will as devises the land known as "Mauna Kamala" to Kahakuakoi (w) and Kealohapanole her husband; and in lieu thereof I give, devise and bequeath unto said Kahakuakoi (w) and Kealohapanole (k) all of that tract of land known as Hanohano, situated at Ewa, Island of Oahu, formerly the property of Puhalahua; to have and to hold as limited in said fifth article of my said will.

12th. I give and bequeath unto the Bishop's School in Honolulu, called "Iolani College", the sum of Two thousand Dollars ($2000.) ; and to the English Sisters School called "St. Albans Priory" the sum of Two thousand Dollars ($2000.); and to "St Andrews Church" the sum of Two thousand Dollars ($2000.).

13th. I give, devise and bequeath unto Kaiulani Cleghorn, daughter of A. S. Cleghorn, of Honolulu, all of that parcel of land and spring situated at Waikiki-uka, Oahu, known as Kanewai; to have and to hold for and during the term of her natural life; remainder to my trustees upon the trusts named in my said will.

14th. I give and bequeath unto the Rev. Henry H. Parker, of Honolulu, the sum of Five hundred Dollars ($500.)

15th I give and bequeath unto Mary R. Collins, if she be with me at the time of my death, the sum of Two hundred Dollars ($200.); and unto Maggie Wynn, if she be then with me, the sum of One hundred Dollars ($100.)

16th. I hereby give the power to all of the beneficiaries named in my said will, and in this codicil, to whom I have given a life interest in any lands, to make good and valid leases of such lands for the term of ten years; which said leases shall hold good for the remainder of the several terms thereof after the decease of said devisees; the rent however, after such decease to be paid to my executors or trustees; provided however that no rent be collected for a longer period in advance at any one time than for six months, and no bonus be taken by said devisees, or any of them, on account of such leases or lease; in either of which cases such lease or leases shall cease and determine, at the option of my executors or trustees, upon the death of such devisee or devisees, who shall have collected rent for a longer period in advance than for six months, or who shall have taken such bonus.

17th. I give unto the trustees named in my will the most ample power to sell and dispose of any lands or other portion of my estate, and to exchange lands and otherwise dispose of the same; and to purchase land, and to take leases of land whenever they think it expedient, and generally to make such investments as they consider best; but I direct that my said trustees shall not purchase land for said schools if any lands come into their possession under my will which in their opinion may be suitable for such purpose; and I further direct that my said trustees shall not sell any real estate, cattle ranches, or other property, but to continue and manage the same, unless in their opinion a sale may be necessary for the establishment or maintenance of said schools, or for the best interest of my estate.

I further direct that neither my executors, nor trustees shall have any control or disposition of any of my personal property, it being my will that my husband, Charles R. Bishop, shall have absolutely all of my personal property of every description.

And I give unto my executors named in my said will full power to sell any portion of my real estate for the purpose of paying debts or legacies without obtaining leave of Court; and to give good and valid deeds for the same, the purchasers under which are not to be responsible for the application of the purchase money.

In witness whereof I, said Bernice P. Bishop, have here-unto set my hand and seal this fourth day of October A. D. Eighteen hundred and eighty-four. The words "to hold for his life, remainder to my trustees" interlined on 2d page before signing.

BERNICE P. BISHOP (SEAL)

Signed, sealed, published and declared by the said Bernice P. Bishop as and for a codicil to her last will and testament, in our presence, who at her request, in her presence and in the presence of each other, have subscribed our names as witnesses thereto. Oct. 4, 1884

WILLIAM W. HALL

FRANCIS M. HATCH

Codicil No. 2

This is a second Codicil to the last Will and Testament of me, Bernice P. Bishop, dated thirty-first October A. D. Eighteen hundred and eighty three:

1st. In addition to the lands devised in the fourth article of my said will to H. R. H. Liliuokalani, the wife of John 0. Dominis, I also give, devise and bequeath unto her, said Liliuokalani, all of that tract of land situated in the District of Honolulu, Island of Oahu, adjoining Waialae nui, known as "Kahala", together with the buildings thereon, and the fishing rights appurtenant thereto; to have and to hold for and during the term of her natural life, remainder to my trustees upon the trusts named in my said will.

2nd. In addition to the house lot devised to Kapaa (k) in the seventh article of my said will, which house lot was formerly the property of his wife Akahi, I also give, devise and bequeath unto him, said Kapaa (k) all of that parcel of land adjoining said houselot, fronting on Queen Street and extending to Richards Street, and now under lease to Henry R. Macfarlane; he, said Kapaa, to pay the taxes upon the same and upon the parcel devised by me to Auhea; to have and to hold for and during the term of the natural life of him said Kapaa, remainder to my trustees, upon the trusts named in my said will.

3rd. I revoke the devise to Auhea (w) wife of Lokana, set forth in the eighth article of my said will. And I give, devise and bequeath unto said Auhea, that house lot situated on said Richards Street (not on the corner of Queen Street) formerly occupied by said Auhea, and which was formerly the dwelling of Akahi; the same adjoining the premises under lease to Henry R. Macfarlane but not included in said lease; to have and to hold for and during the term of the natural life and her, said Auhea, free from the control of her husband; remainder to my trustees upon the trusts named in my said will.

4th. Of the two schools mentioned in the thirteenth article of my said will, I direct the school for boys shall be well established and in efficient operation before any money is expended or anything is undertaken on account of the new school for girls.

It is my desire that my trustees should do thorough work in regard to said schools as far as they go; and I authorize them to defer action in regard to the establishment of said school for girls, if in their opinion from the condition of my estate it may be expedient, until the life estates created by my said will have expired, and the lands so given shall have fallen into the general fund.

I also direct that my said trustees shall have power to determine to what extent said school shall be industrial, mechanical, or agricultural; and also to determine if tuition shall be charged in any case.

In witness whereof I, said Bernice P. Bishop have hereunto set my hand and seal this ninth day of October A. D. 1884.

BERNICE P. BISHOP

Signed, sealed, published and declared by the said Bernice P. Bishop as and for a codicil to her last will and testament in the presence of us, who at her request, in her presence and in the presence of each other have hereunto subscribed our names as witnesses thereto.

October 9th 1884.

0. TROUSSEAU
J. BRODIE

REAFFIRMATION SUBMISSION

EXHIBIT C

FIRST CIRCUIT COURT
STATE OF HAWAII
FILED

1999 JUN 15 PM 4:10

F. PAGAY
CLERK

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Attorney for The Trustees under the Will and of the Estate of Bernice Pauahi Bishop, Deceased

IN THE CIRCUIT COURT OF THE FIRST CIRCUIT

STATE OF HAWAI'I

In the Matter of the Estate Of BERNICE P. BISHOP, Deceased.	EQUITY NO. 2048 **STIPULATION CONCERNING REQUEST FOR PROPOSALS PURSUANT TO STIPULATION NO. 13; EXHIBIT "A"; ORDER** **Date: June 18, 1999** **Time: 9:00 a.m.** **Judge: Presiding Judge**

STIPULATION CONCERNING
REQUEST FOR PROPOSALS PURSUANT TO STIPULATION NO. 13

This Stipulation is made and entered into by and among ROBERT KALANI UICHI KIHUNE, FRANCIS AHLOY KEALA, DAVID PAUL COON, CONSTANCE HEE LAU and RONALD DALE LIBKUMAN, the duly appointed, qualified and acting Trustees under the Will and of the Estate of Bernice Pauahi Bishop, Deceased, acting in their fiduciary and not in their individual capacities (the "Trustees"), THOMAS R. KELLER, ACTING ATTORNEY GENERAL OF THE STATE OF HAWAI'I, as *parens patriae* (the "Attorney General"), and

I do hereby certify that this is a full, true, and correct copy of the original on file in this office.

Clerk, Circuit Court, First Circuit
State of Hawaii

RBG:235302.02

COLBERT M. MATSUMOTO, Master with respect to the Trustees' 109th, 110th, and 111th Annual Accounts (the "Master").

1. Stipulation No. 13 of those certain Stipulations Concerning Master's Recommendations (109th, 110th, and 111th Annual Accounts) and Order entered herein on October 2, 1998 ("October 2, 1998 Stipulations") provides that the Trustees shall prepare a request for proposals ("RFP"), *"the objective of which shall be the development of a comprehensive educational and financial strategic plan"* for the Kamehameha Schools Bernice Pauahi Bishop Estate.

2. Stipulation No. 5 of the October 2, 1998 Stipulations provides that *"[t]he Trustees' strategic planning process . . . shall incorporate planning for the expenditure of accumulated income."*

3. Stipulation No. 13 further provides that *"[t]he Trustees shall seek comment from the Master and the Attorney General regarding the RFP and shall obtain the approval of the RFP from the Court, through a stipulation or order ..."* The Stipulation contemplated that Court approval would be obtained by December 31, 1998.

4. On November 13, 1998, the Trustees' predecessors in trust filed herein the Trustees' First Response to Stipulation No. 13 (Request for Proposals) ("Trustees' First Response") requesting the Master's and Attorney General's written comments concerning the proposed RFP, if any.

5. On November 20, 1998, the Attorney General filed the Attorney General's Response to Trustees' First Response to Stipulation No. 13.

6. On March 15, 1999, the Trustees' predecessors in trust filed a Petition for Court Approval of Request for Proposals Pursuant to Stipulation No. 13 (the "Petition").

7. On April 14, 1999 and April 27, 1999, the Attorney General filed the Attorney General's Objection to Petition for Court Approval of Request for Proposals Pursuant to Stipulation No. 13 Filed March 15, 1999.

8. The Petition came on regularly for hearing before the Honorable Kevin S.C. Chang at 9:00 a.m. on Friday, June 4, 1999. At hearing, the parties represented to the Court that they had reached agreement concerning the form of the RFP, expected to submit a stipulation to that effect, and requested a continuance of hearing of the Petition. The Court continued hearing of the Petition to June 18, 1999 at 9:00 a.m.

9. The parties have reached mutual agreement as to the form of the RFP.

Now Therefore, It Is Hereby Stipulated And Agreed by and among the Trustees, the Attorney General, and the Master that the RFP in the form attached hereto as Exhibit "A" is hereby approved as the form of the RFP to be disseminated by the Trustees pursuant to Stipulation No. 13 of the October 2, 1998 Stipulations.

DATED: Honolulu, Hawai'i, this 15th of June, 1999.

ROBERT BRUCE GRAHAM, JR.
Attorney for the Trustees Under the Will and of the Estate of Bernice Pauahi Bishop, Deceased

Hugh R. Jones, For

THOMAS R. KELLER
Acting Attorney General, State of Hawai'i
Parens Patriae
DOROTHY SELLERS
Deputy Attorney General, State of Hawai'i

Colbert Matsumoto

COLBERT M. MATSUMOTO
Master, 109th, 110th, and 111th Annual Accounts

APPROVED AND SO ORDERED:

KEVIN S.C. CHANG

Judge of the Above-Entitled Court

REQUEST FOR PROPOSAL

TO DEVELOP
A COMPREHENSIVE EDUCATIONAL AND FINANCIAL STRATEGIC PLAN
FOR
KAMEHAMEHA SCHOOLS BERNICE PAUAHI BISHOP ESTATE

OBJECTIVE

The Kamehameha Schools Bernice Pauahi Bishop Estate (KSBE) seeks to engage one or more qualified strategic planning firms with specialized expertise in education, investment and financial planning (Consultant) to develop a comprehensive educational and financial strategic plan for KSBE. This strategic planning process is being undertaken pursuant to December, 1997 and October, 1998 Orders (Orders) of the probate court of the First Circuit, State of Hawai'i (Court), which has jurisdiction of KSBE. Copies of the Orders accompany this Request.

BACKGROUND

Created in 1884, KSBE is a substantially endowed private educational charitable trust established by the Will of Bernice Pauahi Bishop (Will). KSBE's primary mission is the education of children of Hawaiian ancestry. The Kamehameha Schools, founded in 1887, operate a main K-12 campus located at Kapalama Heights in Honolulu, Hawai'i, a statewide preschool program, a system of satellite elementary schools located on neighboring islands, a unique summer school program, and a post high school financial aid program. The Kamehameha Schools are conducted as Protestant schools. Annual costs to operate the Kamehameha Schools now exceed $100 million. Current enrollment is as follows:

PROGRAM	ENROLLMENT
Preschools	936
Elementary	962
Secondary	2,501
Summer Schools	5,190
Financial Aid	3,050

KSBE's investment properties are located in Hawai'i and elsewhere. KSBE's asset and financial portfolio includes:

- Annual revenues exceeding $300 million.
- Trust assets, including assets vested in subsidiary and support organizations, valued at approximately $7.1 billion.
- 173,000 acres of conservation land; 189,000 acres of agricultural land; and, 833 acres of commercial property. The commercial property generates approximately 84% of KSBE's income.

- Multiple subsidiary and supporting organizations.

KSBE has a board of five (5) trustees. The incumbent Trustees were appointed by the Court on May 7, 1999 to serve for an indefinite, interim term following the resignation of a former Trustee and removals of the remaining four former Trustees by the Court. The interim Trustees are vested with full power and authority as to KSBE and are empowered to enter into a binding contract with a strategic planner.

KSBE is presently comprised of five (5) Groups each headed by a Principal Executive. The Groups include the Education Group, Asset Management Group, Budget & Review Group, Legal Group, and Administration Group. Pursuant to Stipulation No. 14 of the October, 1998 Order, KSBE is instituting a CEO based management system. A copy of the Stipulation is enclosed. The governance policies and procedures necessary to effect this change in management structures are subject to review by the Court.

These structural changes are being implemented in accordance with the Orders and are based in part upon a management report rendered in July, 1998 by Arthur Andersen, LLP, and upon the Master's Consolidated Report filed in the Court on August 7, 1998. An executive summary of the Arthur Andersen report, prepared by Arthur Andersen, is enclosed as is a copy of relevant portions of the Master's Consolidated Report.

Additional pertinent materials are enclosed and qualified prospective bidders will be offered an orientation meeting and additional materials.

KSBE is committed to expanding the reach of its educational resources to children and youth of Hawaiian ancestry through planned increases in enrollment in existing programs and new programs, through the use of new teaching (distance learning) and telecommunications technologies, and by other means consistent with the Will and applicable law and judicial decrees (Governing Law). KSBE has commenced a process of expansion to satellite campuses on the islands of Hawai'i and Maui

There is considerable existing information that may be relevant to this strategic planning project, including earlier strategic plans, operational plans, short and long-term budgets and various assessments, reports and analyses prepared by the Trustees, staff and consultants. All of these plans, budgets, analyses and reports will be available to assist the consultant.

KSBE is a charitable entity having tax exempt status under Internal Revenue Code Section 501(c)(3) and is organized and operated for educational purposes within the meaning of Section 170(b)(1)(A)(ii) of the Internal Revenue Code.

SCOPE

The scope of the strategic planning project shall involve the development of an educational plan in conjunction with an investment plan. Strategic planning must be consistent with KSBE's existing tax exempt status under Sections 501(c)(3) and 170(b)(1)(A)(ii) of the Internal Revenue Code. Strategic planning must be consistent with the requirements of the Orders, particularly Stipulations 5, 13 and 14 of the October, 1998 Order.

The educational plan must take into account the existing and foreseeable potential of the financial resources of KSBE, including the resources of its taxable subsidiaries and exempt support organizations. The investment plan must be fashioned to meet projected educational program needs. The principal focus of this interrelated planning process should be the educational mission of the Kamehameha Schools.

The investment plan must take into full account diversification (including thoughtful goal-oriented asset allocation), risk (including income volatility), cost-conscious administration, the perpetual nature of the Trust, the terms of the Will and Governing Law.

The strategic plan for KSBE must incorporate planning for the expenditure of KSBE's accumulated income and anticipated growth in revenues. KSBE calculates that, as of June 30, 1998, there was in excess of $444 million in accumulated income. KSBE projects that its revenues will grow substantially during the ensuing ten years and thereafter. KSBE is committed to the development of a strategic plan for the expenditure of its income on its educational purposes, including planning for appropriate transfers of revenues from subsidiaries and support organizations to the support and maintenance of the Kamehameha Schools.

KSBE is a perpetual, self-sustaining charitable institution. The strategic plan must balance the income and corpus requirements of the present and those of the future in a manner consistent with the Will and Governing Law.

The strategic planner will be provided with current information concerning the Trust Estate's core assets, portfolio investments and projected revenues and its current and projected educational expenditures, including anticipated expansion costs. The strategic planning process should include development of integrated investment and educational plans that provide for deployment of the endowment and development of educational services in a manner reasonably calculated to assure consistent funding and orderly growth of educational services without impairing the real value of the endowment. The strategic planning process should identify parameters and assumptions for the development of KSBE's long-range plans.

The strategic plan for KSBE must be consistent in all respects with the Will and Governing Law, and must be developed in accordance with the provisions of Stipulations 5, 13 and 14 of the October, 1998 Order.

PROPOSAL

The proposal to be submitted to KSBE must include the following elements:

Credentials and Qualification. The proposal must present your professional qualifications and expertise (a) to develop a comprehensive educational and financial strategic plan and (b) to propose an organizational structure for the implementation of these plans. Particular emphasis should be given to your experience in education, investments and financial planning. Indicate the names of other organizations, particularly educational institutions, for which you have performed similar engagements and the scope of such engagements.

Approach and Process. The proposal should present your approach to develop the comprehensive educational and financial strategic plan and organizational structure including the proposed work plan for completion of the engagement.

The strategic planning process shall include input concerning the educational plan component of the strategic plan from appropriate persons, including, but not limited to, administrators, teachers, staff, parents, students, and alumni.

Governance structure is an important element for implementation of both plans.

Provide an outline of the structure of your anticipated report to be submitted at completion of the engagement.

Resources. Indicate the resources to be used in conduct of the development of the strategic plan and proposed governance structure. Provide resumes for those individuals you anticipate will be involved in the engagement and indicate how the engagement team will be structured.

Time Frame. Work on the engagement should commence no later than thirty (30) days from the date the strategic planning firm is engaged. The comprehensive educational and financial strategic plan and recommended governance structure to implement such plans must be completed and delivered to KSBE within twelve (12) months from the date of engagement of the strategic planning firm, unless extended for good cause upon notice to the Court, the Master and the Attorney General of the State of Hawai'i as *parens patriae*. KSBE expects that the final report will be completed and submitted in an expeditious manner.

Fees. Provide an estimate of the cost of your services and your billing practice.

LOGISTICS

KSBE requests that your proposal be submitted no later than **[Date to be inserted - six to eight weeks after Court approval]** to:

Mr. Rodney J. Park
Director, Administration Group
Kamehameha Schools Bernice Pauahi Bishop Estate
567 South King Street, Suite 200
Honolulu, Hawaii 96813
Phone: (808) 523-6200
Fax: (808) 541-5340

Qualified bidders should contact Mr. Park to arrange to have representatives attend an informational briefing, at which time additional background information will be provided.

SELECTION CRITERIA

KSBE has made no pre-commitment to any bidder concerning the strategic planning process. Selection will be based upon the proposals received, responsiveness, resources, qualifications, references, proposed fees and other standard considerations. All proposals received will be submitted to the Court, the Master and the Attorney General for review in conjunction with the Court's approval of KSBE's selection of a Consultant.

Enclosures

REAFFIRMATION SUBMISSION

EXHIBIT F

COLBERT M. MATSUMOTO 2276-0
Suite 2000, Amfac Tower
700 Bishop Street
Honolulu, Hawaii 96813
Telephone No. 523-2999

Master

FIRST CIRCUIT COURT
STATE OF HAWAII
FILED

1998 OCT -2 PM 4:03

O. SAKIMOTO
CLERK

IN THE CIRCUIT COURT OF THE FIRST CIRCUIT

STATE OF HAWAII

In the Matter of the Estate	) EQUITY NO. 2048
	)
of	) STIPULATIONS CONCERNING
	) MASTER'S RECOMMENDATIONS
BERNICE P. BISHOP,	) (109th, 110th, and 111th
	) ANNUAL ACCOUNTS) and ORDER
Deceased.	)
	) Hearing Date: Oct. 2, 1998
	) Hearing Time: 9:00 a.m.
	) Judge: Colleen K. Hirai

STIPULATIONS CONCERNING MASTER'S RECOMMENDATIONS
(109th, 110th, and 111th ANNUAL ACCOUNTS)

These Stipulations are entered into by and among Petitioners RICHARD SUNG HONG WONG, OSWALD KOFOAD STENDER, MARION MAE LOKELANI LINDSEY, GERARD AULAMA JERVIS and HENRY HAALILIO PETERS, TRUSTEES UNDER THE WILL AND OF THE ESTATE OF BERNICE PAUAHI BISHOP, DECEASED (hereinafter the "Trustees"); and Respondent MARGERY S. BRONSTER, ATTORNEY GENERAL OF THE STATE OF HAWAII, as *parens patriae* (hereinafter the "Attorney General");

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TWENTIETH DIVISION

and COLBERT M. MATSUMOTO, Master with respect to the Trustees' One Hundred Ninth, One Hundred Tenth and One Hundred Eleventh Annual Accounts (hereinafter the "Master").

On August 7, 1998, the Master filed herein his Master's Consolidated Report on the 109th, 110th, and 111th Annual Accounts (the "*Master's Consolidated Report*"). The *Master's Consolidated Report* makes nineteen specific Recommendations concerning the Trust Estate and its annual accounts.

On September 9, 1998, the Trustees filed herein their Trustees' Response to the Master's Consolidated Report on the One Hundred Ninth, One Hundred Tenth and One Hundred Eleventh Annual Accounts of the Trustees (the "*Trustees' Response*"). The *Trustees' Response* addresses each of the nineteen Recommendations made by the Master in the *Master's Consolidated Report*.

On September 9, 1998, the Attorney General filed herein her Attorney General's Response to the Master's Consolidated Report on the 109th, 110th, and 111th Annual Accounts (the "*AG's Response*"). The *AG's Response* agrees with each of the Master's nineteen Recommendations, suggests amendments and additions to them, and suggests additional court action based upon the *Master's Consolidated Report*.

On September 9, 1998, Trustee Oswald Kofoad Stender filed herein his Trustee Oswald Kofoad Stender's Response to Master's Report (*"Trustee Stender's Response"*). *Trustee Stender's Response* recommends approval of the Master's Recommendations.

Since September 9, 1998, the parties each have filed additional or supplemental reports, responses or objections herein.

The parties acknowledge that there are material differences of opinion concerning the statements and contentions in the *Master's Consolidated Report*, the *Trustees' Response*, the *AG's Response*, and other reports, responses and objections filed herein. Without conceding the accuracy of any such statements and contentions, the parties have agreed that it is in the best interest of the Trust Estate that the Stipulations hereinafter set forth be implemented.

The Stipulations hereinafter set forth concern sixteen CUH ~~seventeen~~ of the nineteen Recommendations made by the Master in his *Master's Consolidated Report*, and, upon approval by this Court, shall be a Court order binding upon the parties hereto and their respective successors in office. The Master's seventeenth, eighteenth and nineteenth Recommendations are not covered by these Stipulations.

NOW, THEREFORE, IT IS HEREBY STIPULATED AND AGREED by and among the Master, the Trustees and the Attorney General as follows:

Nothing herein contained shall be deemed or construed to preclude, estop or otherwise bar any party from seeking other or further relief from the Court in this proceeding or upon any petition, response or objection now pending or filed hereafter, provided however, that these Stipulations shall not be amended or superseded by implication but only by express order of the Court entered upon agreement of the parties or after hearing at which all parties, or their respective successors in office, shall have had notice and a reasonable opportunity to be heard. Subject to the foregoing, nothing contained in these Stipulations shall be deemed or construed to preclude any party from petitioning the Court for further instructions concerning any matter.

Nothing herein contained shall be deemed or construed as an admission or concession of any liability on the part of any party hereto.

Without limiting the generality of the foregoing paragraph, the Trustees and the Attorney General hereby expressly reserve all claims, arguments, defenses, responses and objections which have been or may hereafter be raised by them in their respective Responses to the *Master's Consolidated Report* and any supplement thereto, and in their respective cross-responses and cross-objections herein.

The following are the ~~seventeen~~ sixteen stipulations of the parties:

Stipulation No. 1: New Financial Statement Presentation Shall Be Adopted.

The Trustees shall adopt the format of the financial statement and supplemental schedules recommended in the *Andersen Report*, with the same level of detail, and shall file the audited financial statement and supplemental schedules with each annual account, beginning with the 112th Annual Account (FY 1997). The foregoing financial statement shall be prepared as a special purpose financial statement and shall be audited in full compliance with Generally Accepted Accounting Principles ("GAAP").

Stipulation No. 2: Corpus And Revenue Activity Shall Be Specifically Reported.

Effective with their 112th Annual Account (FY 1996-1997) and for each Account thereafter, the Trustees shall submit a special purpose financial statement which conforms to the trust accounting format as proposed by the *Andersen Report*.

Stipulation No. 3: Accumulated Income Shall Be Restored To The Revenue Account.

The Trustees shall not reclassify accumulated or unexpended income to corpus and shall restore to the revenue account all accumulated income which previously was reclassified to corpus. The Trustees shall provide to the Master a report of their actions pursuant to this paragraph within 60 days from the date upon which the Court enters its order approving this Stipulation.

Stipulation No. 4: An Accounting Of Accumulated Income And Independent Verification Shall Be Provided.

The Trustees shall provide to the Master an accounting of all accumulated income within 60 days from the date upon which the Court enters its order approving this Stipulation. The Master shall cause the Trustees' accounting to be reviewed and verified by Arthur Andersen LLP and shall report that firm's conclusions to the Court.

Stipulation No. 5: Strategic Planning Shall Incorporate Planning For Expenditure Of Accumulated Income.

The Trustees' strategic planning process, which is described more fully below, shall incorporate planning for the expenditure of accumulated income.

Stipulation No. 6: No Future Reclassification Of Accumulated Income Shall Be Made Without Prior Court Approval.

The Trustees shall not reclassify accumulated or unexpended income to corpus pursuant to H.R.S. Chapter 517D, the Uniform Management of Institutional Funds Act, except with the prior approval of the Court obtained upon a petition for instructions with notice to the Attorney General as *parens patriae* of the Trust Estate.

Stipulation No. 7: The Replacement Cost Reserve Shall Be Discontinued Pending Further Instructions Of The Court.

The Trustees shall discontinue the Replacement Cost Reserve pending further instructions of this Court obtained upon a petition for instructions with notice to the Attorney General as *parens patriae* of the Trust Estate. Nothing herein shall be deemed or construed to amend or supersede prior orders of this Court concerning the depreciation reserve.

Stipulation No. 8: **Investment Performance Schedules Shall Be Regularly Prepared And Shall Be Incorporated As Supplemental Schedules To The Financial Statements.**

Beginning with the 112th Account and at least annually thereafter, the Trustees shall cause benchmarked investment performance schedules to be prepared. If the Trustees believe an appropriate benchmark does not exist or cannot reasonably be developed, the Trustees shall provide a reasonable explanation in the schedules for their inability to identify or develop such a benchmark. The presentation of this information shall evolve to include at least one-year, five-year, and ten-year annualized income yield and total return analyses. The schedules shall be audited and attached as supplemental schedules to the special purpose financial statements submitted to the Court with the annual accounts of the Trustees. The Trustees shall consult with experts to develop appropriate benchmarks which shall be utilized in connection with such supplemental schedules, subject to the review and approval by the Court, through a stipulation or order, within 60 days from the date on which the Court enters its order approving this Stipulation.

Stipulation No. 9: Investment Return Analysis Shall Use Appropriate Performance Measures.

In preparing performance return analyses, the Trustees shall utilize appropriate measures such as time weighed return (TWR) and internal rate of return (IRR) for various time spans to allow meaningful comparisons against performance benchmarks.

Stipulation No. 10: Investment Policies Shall Be Reviewed.

The Trustees shall undertake a comprehensive review of their investment policies as recommended by the *Andersen Report* in conjunction with the overall strategic planning process described below.

Stipulation No. 11: Due Diligence And Investment Monitoring Policies, Practices, And Procedures Shall Be Strengthened.

The Trustees shall improve and strengthen the due diligence and investment monitoring policies, practices, and procedures as recommended in the *Andersen Report*. The Trustees shall report their implementation plan to the Master within 60 days from the date on which the Court enters its order approving this Stipulation.

Stipulation No. 12: Investment And Management Decisions Shall Be Properly Documented.

The Trustees shall ensure that appropriate documentation of their investment and management decisions is prepared and maintained as recommended in the *Andersen Report*. Such documentation shall be made available for review by the court's master in connection with the annual account review process. The Trustees shall report their implementation plan to the Master within 60 days from the date on which the Court enters its order approving this Stipulation.

Stipulation No. 13: Strategic Planning Shall Be Implemented.

The Trustees shall prepare a request for proposals ("RFP"), the objective of which shall be the development of a comprehensive educational and financial strategic plan for consideration and adoption by the Trustees. The RFP shall more specifically define the scope of the strategic planning project to be undertaken. The RFP shall be disseminated to strategic planning firms. The RFP shall identify the qualification criteria of the strategic planning firms from which proposals shall be solicited. Such qualifications should include expertise in education, investments and financial planning. The Trustees shall seek comment from the Master and the Attorney General regarding the RFP and shall obtain the approval of the RFP from the Court, through a stipulation or order, within 90 days from the date on which the Court enters its order approving this Stipulation.

The Trustees shall review the responses to the RFP and, subject to the review and approval by the Court, through a stipulation or order, the Trustees shall select one or more qualified strategic planning firms within 120 days from the date on which the RFP is approved by the Court.

The scope of the strategic planning project should involve the development of an educational plan in conjunction with an investment plan. The educational plan should take into account the future potential of the financial resources of the Trust Estate. The investment plan should be fashioned to meet projected educational program needs. The principal focus of this interrelated planning process should be the educational mission of the Trust Estate.

The investment plan should take into full account diversification (including thoughtful goal-oriented asset allocation), risk (including income volatility), cost-conscious administration, the perpetual nature of the Trust, and preservation of the corpus of the Trust Estate consistent with the terms of the Will.

The strategic planning firm should begin its work no later than 30 days from the date of its engagement. The strategic plan should be completed and presented to the Trustees, the Court and the Attorney General as *parens patriae* within twelve months from the date of engagement of the strategic planning firm, unless extended for good cause upon notice to the Court, the Master and the Attorney General as *parens patriae*.

The strategic planning process shall include input concerning the educational plan component of the strategic plan from appropriate persons, including, but not limited to, administrators, teachers, staff, parents, students, and alumni. The Trustees, in the prudent exercise of their discretion, shall act upon the proposed strategic plan within 90 days after it is presented to them and shall present a report to the Court and the Attorney General, as *parens patriae*, regarding their decision.

The Master shall have full access to the strategic planning firm to monitor and review the ~~development~~ progress of the strategic planning process, including stakeholder input, and may require such status reports and meetings as he reasonably sees fit.

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This Stipulation supersedes the stipulation set forth in Part I, Section G of the Stipulation Concerning Master's Recommendations (109th Annual Account) filed herein on December 19, 1997.

Stipulation No. 14: A New CEO Based Management System Shall Be Instituted.

The Trustees shall cease to employ the "lead trustee" system of management in administering the Trust Estate.

The Trustees shall adopt and implement a CEO based system of management for the Trust Estate consistent with the concept recommended in the *Andersen Report* and hire a CEO within 180 days after the date on which the Court enters its order approving this Stipulation. The system shall incorporate a formal governance policy which more clearly defines the roles of the Board of Trustees and that of the CEO. The role of the CEO shall be consistent with standards for delegation of authority under trust law.

The Master shall have full access to the Trustees to monitor and review the development of the CEO based management system, the formal governance policy, and the selection of the CEO, and may require such status reports and meetings as he reasonably sees fit.

The Trustees shall seek comment from the Master and the Attorney General, as *parens patriae*, regarding the CEO based management system and the formal governance policy and shall obtain the approval of the CEO based management system and formal governance policy from the Court, through a stipulation or order.

Stipulation No. 15: A Compliance Plan For Determining Trustee <u>Compensation Shall Be Prepared.</u>

On or before November 13, 1998, the Trustees shall submit to this Court for its review and approval a plan for determining trustee compensation that is in compliance with and satisfies applicable requirements of state and federal law, including without exception, federal Intermediate Sanctions legislation and Treasury regulations incident thereto, and H.R.S. Section 607-20, as amended by Act 310 of the 1998 Hawaii State Legislature.

The plan shall include provision for the preparation of an independent professional study concerning reasonable trustee compensation which utilizes relevant and appropriate criteria. The study shall be commissioned under the auspices of the Court, by the Court's master or such other person or entity as the Court shall order, consistent with requirements of applicable law and regulation. The cost of any such independent professional study shall be borne as an expense of the Trust Estate. Should the Trustees or others wish to contest, rebut or supplement the study by commissioning another study, they shall do so at their own expense unless the Court first shall have approved the additional study as an expense of the Trust Estate.

Stipulation No. 16: Stricter Conflict Of Interest Policies And Procedures Shall Be Adopted.

The Trustees shall develop and adopt stricter guidelines and procedures to ensure appropriate compliance with fiduciary standards. The Trustees shall provide to the Master a report of their actions pursuant to this paragraph within 90 days from the date upon which the Court enters its order approving this Stipulation.

The Restated Guidelines shall be further amended to include a provision requiring that future masters review the Trustees' compliance with conflict of interest policies and procedures in connection with their review of the Trustees' Annual Accounts.

DATED at Honolulu, Hawaii, OCT 0 2 1998.

ROBERT B. GRAHAM, JR.
Attorney for Petitioners Richard Sung Hong Wong, Marion Mae Lokelani Lindsey, Gerard Aulama Jervis, and Henry Haalilio Peters, Trustees under the Will and of the Estate of Bernice Pauahi Bishop, Deceased

CRYSTAL K. ROSE
Attorney for Petitioners Oswald Kofoad Stender, Trustee under the Will and of the Estate of Bernice Pauahi Bishop, Deceased

MARGERY S. BRONSTER
KEVIN T. WAKAYAMA
Attorney General, State of Hawaii, in her capacity as *parens patriae*

COLBERT M. MATSUMOTO
Master

APPROVED AND SO ORDERED

FIRST CIRCUIT COURT SEAL STATE OF HAWAII

Colleen K. Hirai
Judge of the Above-Entitled Court

In the Matter of the Estate of Bernice P. Bishop, Deceased; Equity No. 2048; Stipulation Concerning Master's Recommendations (109th, 110th, And 111th Accounts) and Order

REAFFIRMATION SUBMISSION

EXHIBIT G

FIRST CIRCUIT COURT
STATE OF HAWAII
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G. HA
CLERK

ROBERT BRUCE GRAHAM, JR. 1305-0
ASHFORD & WRISTON
Alii Place, Suite 1400
1099 Alakea Street
Honolulu, Hawaii 96813
Telephone No. 539-0400

Attorney for Petitioners,
Robert Kalani Uichi Kihune,
David Paul Coon, Francis Ahloy Keala,
Constance Hee Lau and
Ronald Dale Libkuman,
Trustees under the Will and of the Estate of
Bernice Pauahi Bishop, Deceased

IN THE CIRCUIT COURT OF THE FIRST CIRCUIT

STATE OF HAWAII

In the Matter of the Estate Of BERNICE P. BISHOP, Deceased.	EQUITY NO. 2048 PETITION FOR THE ESTABLISHMENT OF A PROCEDURE FOR SELECTION OF FUTURE TRUSTEES; EXHIBIT "A"

PETITION FOR THE ESTABLISHMENT OF A PROCEDURE FOR SELECTION OF FUTURE TRUSTEES

Come now ROBERT KALANI UICHI KIHUNE, DAVID PAUL COON, FRANCIS AHLOY KEALA, CONSTANCE HEE LAU and RONALD DALE LIBKUMAN, the duly appointed, qualified and acting Interim Trustees under the Will and of the Estate of Bernice Pauahi Bishop, Deceased, acting in their fiduciary and not in their individual capacities, Petitioners herein, and respectfully petition this Court to establish a procedure for the selection of persons to serve as future trustees of the Estate of Bernice Pauahi Bishop, Deceased.

A. PROBATE RULE 126(c) STATEMENTS

1. Petitioners are the duly appointed, qualified and acting Trustees under the Will and of the Estate of Bernice Pauahi Bishop, Deceased, who died at Honolulu, Hawaii, on October 16, 1884, and whose Will and two codicils thereto were duly admitted to Probate in the Supreme Court of the Hawaiian Islands on December 2, 1884.

2. By the terms of her Will, namely Article *Thirteenth* thereof, Bernice Pauahi Bishop gave, devised and bequeathed all the rest, residue and remainder of her estate, subject to certain life interests which have lapsed or been surrendered, unto certain trustees, to hold upon the following trusts, namely:

> *to erect and maintain in the Hawaiian Islands two schools, each for boarding and day scholars, one for boys and one for girls, to be known as, and called the Kamehameha Schools.*

A true and accurate copy of said Will is on file herein.

3. The assets of the Trust Estate consist of real, personal and other properties having an estimated value in excess of Six Billion Dollars.

4. Petitioners' post office address is Kamehameha Schools Bernice Pauahi Bishop Estate, P.O. Box 3466, Honolulu, Hawaii 96801; Petitioners' business address is Kawaiaha'o Plaza, Suite 200, 567 South King Street, Honolulu, Hawaii 96813.

5. Petitioners DAVID PAUL COON and ROBERT KALANI UICHI KIHUNE are residents of the Island and County of Hawaii, State of Hawaii, and Petitioners FRANCIS AHLOY KEALA, RONALD DALE LIBKUMAN and CONSTANCE HEE LAU are residents of the City and County of Honolulu, State of Hawaii.

6. The Trust Estate is a perpetual, charitable trust estate of which there is no vested remainder beneficiary; the Trust Estate exists solely for the benefit of The Kamehameha

Schools; there are no unborn, unascertained or minor beneficiaries of the Trust Estate; and there are no persons interested in the Trust Estate within the meaning of Section 560:7-201 of the Hawai'i Uniform Probate Code or Rule 25 of the Hawaii Probate Court Rules other than the Attorney General of the State of Hawaii, acting as *parens patriae*, who will be given notice of this Petition.

7. The Court has jurisdiction of this Petition pursuant to Hawaii Revised Statutes Sections 560:7-201(a)(1) and 603-21.7(a)(3). This Petition is filed pursuant to Hawaii Probate Rules 3 and 126 (a) and (c).

B. **DISCUSSION**

1. Article *Fourteenth* of the Will of Bernice Pauahi Bishop, provides in part as follows:

> *I further direct that the number of my said trustees shall be kept at five; and that vacancies shall be filled by the choice of a majority of the Justices of the Supreme Court, the selection to be made from persons of the Protestant religion.*

2. In Estate of Bishop, 23 Haw. 575 (1917), the Hawaii Supreme Court held that the power of appointment is vested by the Will in the Justices in their individual capacities and not in their collective or official capacity as a Court.

3. Four of the five incumbent Justices of the Hawaii Supreme Court have declared that they will no longer make appointments to KSBE's board of trustees. Attached hereto as Exhibit "A" is a true and accurate copy of the Letter From The Justices Of The Supreme Court Of Hawai'i, filed herein on April 21, 1999.

4. Because the Justices' power of appointment is personal to them and is not an official act of the Court, they cannot be compelled to exercise the power if they decline to do so.

5. Additionally, because the power of appointment is personal to the five Justices and is not an act of the Supreme Court as a court, it cannot be referred by the Supreme Court to another court or panel of justices.

6. By reason of the personal decision of four of the five Justices to decline to exercise the power of appointment, the direction of the Will that vacancies on the board of trustees "*shall be filled by the choice of a majority of the Justices of the Supreme Court*" is ineffective.

7. By that certain Order Granting Petition For Removal of Trustee Marion Mae Lokelani Lindsey Filed On December 29, 1997 entered herein on May 6, 1999, the Court (Weil, J.) granted the Petition for Removal of Trustee Lindsey filed by Trustees Oswald Kofoad Stender and Gerard Aulama Jervis. On June 10, 1999, the Court (Weil, J.) entered its Findings Of Fact And Conclusions Of Law; Order Reaffirming May 6, 1999 Order Granting Petition For Removal Of Trustee Marion Mae Lokelani Lindsey Filed On December 29, 1997. Final Judgment was entered on June 17, 1999. Ms. Lindsey has appealed the orders decreeing her permanent removal but has not obtained a stay of them.

8. By that certain Order Regarding Order To Show Cause Regarding Special Purpose Trustees' Report And Order To Show Cause Regarding New CEO Based Management System entered herein on May 7, 1999, this Court (Chang, J.) removed Trustees Wong, Peters, Lindsey and Jervis from the board of trustees on an interim basis, and accepted the

interim resignation of Trustee Stender. By that same Order, this Court appointed Petitioners to act as Interim Trustees, to serve as such pending further order of the Court.

9. Although there are no existing vacancies on the board of trustees, Petitioners serve at the pleasure of the Court. Petitioners' appointments were intended to be interim in nature and vacancies on the board of trustees will arise in the future. It is in the best interest of the Trust Estate that a procedure for making future selections of trustees be established while there is a full board of trustees in office.

10. It is axiomatic that a trust will not be allowed to fail for want of a trustee and that the Court has inherent power to fill a vacancy on the board of a trust. It is vitally important that there be a definite procedure whereby future vacancies arising on KSBE's board of trustees may be filled in a manner as nearly consistent with the Will of Bernice Pauahi Bishop as possible.

11. The procedure employed should also be designed to ensure that the persons selected to serve as trustees (i) are qualified to serve as fiduciaries of an educational trust; (ii) understand the role and duties of trustees generally and are familiar with the specific terms and conditions of the Will; (iii) are able to serve without conflict of interest; and (iv) are sensitive to the unique role of the Kamehameha Schools Bernice Pauahi Bishop Estate in the Hawaiian and statewide communities.

12. Petitioners have identified the elements of a future selection process that Petitioners deem essential to the needs of the Trust Estate and to the perception of integrity and fairness. These are set forth below. Petitioners offer their observations and comments based upon their own insights and upon discussions with members of the Kamehameha ohana and

others in the community. Petitioners offer these observations and comments not by way of petition for their approval as written but as a submission to this Court for its consideration and review in connection with the establishment of a procedure for the selection of future trustees.

13. Petitioners urge the Court to establish a means by which persons other than Petitioners also may submit their observations and suggestions to the Court.

14. Petitioners respectfully submit that, pursuant to Rule 28(a) of the Hawaii Probate Rules, the Court should appoint a master to review this petition, and to receive, review and comment upon observations and suggestions offered the Court, including but not limited to the observations and suggestions of Petitioners set forth hereinbelow.

C. PETITIONERS' OBSERVATIONS AND COMMENTS

1. Appointment of a Selection Committee

a. A Trustee Selection Committee ("Committee") should be appointed by the Court. The purpose of the Committee should be to:

- Announce an existing or expected vacancy to the public;
- Receive applications and nominations for the vacant position;
- Solicit qualified candidates who may not have applied or been nominated;
- Review the applications according to an established set of criteria;
- Provide for written public comment; and
- Submit a list of recommended candidates to the Court.

b. The Committee should be comprised of persons representative of the Kamehameha ohana, including alumni, teachers and families of students, and of the Hawaiian community and the community at large. Members of the Committee should possess experience and insight into the operation and management of large private educational institutions, large financial institutions, or large charitable trusts or foundations. As a whole, the Committee should have a broad experience upon which to make its nominations to the Court.

c. The members of the Committee should appoint a chairperson from among them. The members should serve without compensation. Payment of the Committee's reasonable expenses should be made out of the Trust Estate upon approval by the Court.

2. Selection Process

a. When a vacancy occurs or is expected to occur, the then-incumbent trustees should submit a petition to the Court requesting that a Committee be empanelled by the Court. If it is shown that there is or will be a vacancy, the Court should constitute the Committee, selecting its members based upon the considerations set forth above.

b. The Committee should have the authority to retain a consultant knowledgeable and experienced in the hiring of executive personnel. The consultant should assist the Committee in organizing, screening, and reviewing applications and nominations for the vacant trusteeship position. The consultant should verify information provided by the applicant, including the applicant's educational background, background in business, honors and awards, and volunteer work in the community.

c. The Committee should commence with a review of applications received. In the event of a conflict of interest between a Committee member and an applicant who has met the minimum qualifications, the member should declare that a conflict exists and fully describe the nature and extent of the conflict. The remaining members of the Committee should determine whether the member in question should withdraw from consideration of the candidate in question.

d. Based on information in the applications and gathered by the consultant, the number of persons under consideration should be reduced to six persons. The Committee then should proceed with interviews of the six persons to determine three finalists. The names of the three finalists then should be submitted to the Court in a writing filed as a public record. If there is more than one vacant position, the number of finalists should be the sum of three plus one for each additional vacancy. From this list of finalists, the Court should select the trustee(s). Ultimately, it is incumbent upon the Court to ascertain the fitness of the persons selected by it and, in the event that none of the finalists nominated by the Committee is approved by the Court, the Court should advise the Committee in writing of its reasons and request that the Committee submit an equivalent number of additional nominations. The Court should make its appointment(s) only from the nominations made by the Committee.

3. Selection Criteria

a. The optimal candidate would (i) have a history of success in business, finance or related areas; (ii) have received a formal education; (iii) possess outstanding personal traits including Hawaiian values such as *pono* (to be moral and proper), *'imi 'ike* (to seek knowledge), *laulima* (to work cooperatively), *lokomaika'i* (to share), *na'au pono* (to possess a deep sense of justice), *malama* (to care for each other), and *ha'a ha'a* (to be humble).

b. Categorically, the following criteria should be established:

(1) Experience

The candidate should possess expertise in one or more of the following areas:

- Business Administration: to include knowledge, skills, and prior successful experience in managing a large corporation;
- Finance and Investment: to include management of land and monetary assets of a multi-million dollar corporation;
- Strategic Planning and Policy Setting: to include responsibility for administering the affairs and/or setting policies for the direction and management of a large corporation or educational institution;

- General areas of interest, including education, law, finance or an especially relevant background in governance.

(2) Political Office

The candidate should not currently hold any elected political office nor have held any political office within the five years immediately preceding his or her nomination.

(3) Religious Affiliation

The Will of Bernice Pauahi Bishop provides that the selections for trustees shall be made from persons of the Protestant religion.

(4) Personal Qualities and Characteristics

The desirable qualities and characteristics of a trustee should include:

- A demonstrated reputation of integrity, the capacity to fulfill the responsibilities of a fiduciary under trust law, and a commitment to the best interests of children;
- Consistent and active leadership in the community-at-large;
- A willingness and sincerity to uphold the purposes of KSBE as stated in the Will of Bernice Pauahi Bishop.

(5) Preferences

If two candidates are perceived as equally qualified, preference should be given to the candidate who is:

- An alumnus of the Kamehameha Schools, or
- Of Hawaiian ancestry.

4. Term Limits and Retention Process

a. Each trustee should be appointed to a term of five years, after which the trustee may submit an application to the Court to serve another term of five years. The Court should refer any application for reappointment to a Committee constituted by the Court in accordance with these procedures. The Committee should either recommend reappointment of the trustee or proceed with the selection process and submit the names of three finalists to the Court, in which event the trustee applying for reappointment could be one of the three finalists submitted to the Court.

b. The trustees should be limited to a maximum of two five-year terms, whether or not consecutive. There should be no mandatory retirement age nor any other arbitrary limit upon the term of the trustees, except that where more than one trustee is selected at the same time, their respective terms should be staggered to ensure that no more than two trustee terms expire within the same year.

D. CONCLUSION

Upon the foregoing, Petitioners respectfully pray as follows:

1. That this Honorable Court make and enter its order fixing a date and time for hearing of this Petition;

2. That this Honorable Court appoint a master to review this Petition, to receive, review and comment upon observations and suggestions offered the Court, including but not limited to the observations and suggestions of Petitioners set forth herein; and report to the Court;

3. That upon hearing hereof, this Court make and enter its Order and Decree establishing a selection process for the appointment of future trustees of the Kamehameha Schools Bernice Pauahi Bishop Estate; and

4. That this Court grant such other and further relief as to this Honorable Court shall seem just and equitable in the premises.

Each of the undersigned persons understands that this Petition is deemed to include an oath, affirmation or statement to the effect that its representations are true as far as each of the undersigned persons knows or is informed, and that penalties for perjury may follow deliberate falsification.

DATED: Honolulu, Hawaii, this 6th day of August, 1999.

ROBERT KALANI UICHI KIHUNE

DAVID PAUL COON

FRANCIS AHLOY KEALA

CONSTANCE HEE LAU

RONALD DALE LIBKUMAN

Trustees Under the Will and of the Estate of Bernice Pauahi Bishop, Deceased

Hawaii Probate Rule 5(b) Certification:

Robert Bruce Graham, Jr.
Attorney for Petitioners
Trustees Under The Will and of
the Estate of Bernice Pauahi Bishop, Deceased

1999 APR 21 AM 8:37

G. IA
CLERK

ORIGINAL

IN THE CIRCUIT COURT OF THE FIRST CIRCUIT

STATE OF HAWAII

In the Matter of the Estate of BERNICE P. BISHOP, Deceased.	EQUITY NO. 2048 LETTER FROM THE JUSTICES OF THE SUPREME COURT OF HAWAI'I

LETTER FROM THE JUSTICES OF THE SUPREME COURT OF HAWAI'I

On April 20, 1999, the undersigned civil administrative and probate judge received a letter dated April 19, 1999, from the justices of the Supreme Court of Hawai'i. The above-referenced letter is attached hereto as Exhibit "1", and is hereby filed in Equity No. 2048.

Dated: Honolulu, Hawaii, April 21, 1999.

JUDGE OF THE ABOVE-ENTITLED COURT

EXHIBIT "A"

35

April 19, 1999

Hon. Kevin Chang
Administrative/Probate Judge
Circuit Court of the First Circuit
777 Punchbowl Street
Honolulu, HI 96813

Re: **EQUITY NO. 2048**

Dear Judge Chang:

On December 20, 1997, four of the five justices of the Supreme Court of Hawai'i advised probate judge, the Honorable Colleen Hirai, that they would no longer be exercising the powers to appoint trustees of the Board of the Bishop Estate granted by the will of Princess Bernice Pauahi Bishop. See attachment.

The undersigned justices of the Supreme Court of Hawai'i, in our individual capacities, hereby request that the attachment and this letter be properly docketed in Equity No. 2048.

Thank you for your attention to this matter.

Sincerely,

RONALD T. Y. MOON

ROBERT G. KLEIN (dissent)

STEVEN H. LEVINSON

PAULA A. NAKAYAMA

MARIO R. RAMIL

Attch.

EXHIBIT "1"

December 20, 1997

Hon. Colleen Hirai
Judge, Circuit Court of the First Circuit,
Probate Division
777 Punchbowl Street
Honolulu, HI 96813

RE: **Estate of Princess Bernice Pauahi Bishop**

Dear Judge Hirai:

The undersigned justices of the Supreme Court of Hawai`i, in our individual capacities, hereby give notice that we will not exercise the powers to appoint trustees to the Board of the Bishop Estate granted by the will of Princess Bernice Pauahi Bishop.

Sincerely,

RONALD T. Y. MOON

STEVEN H. LEVINSON

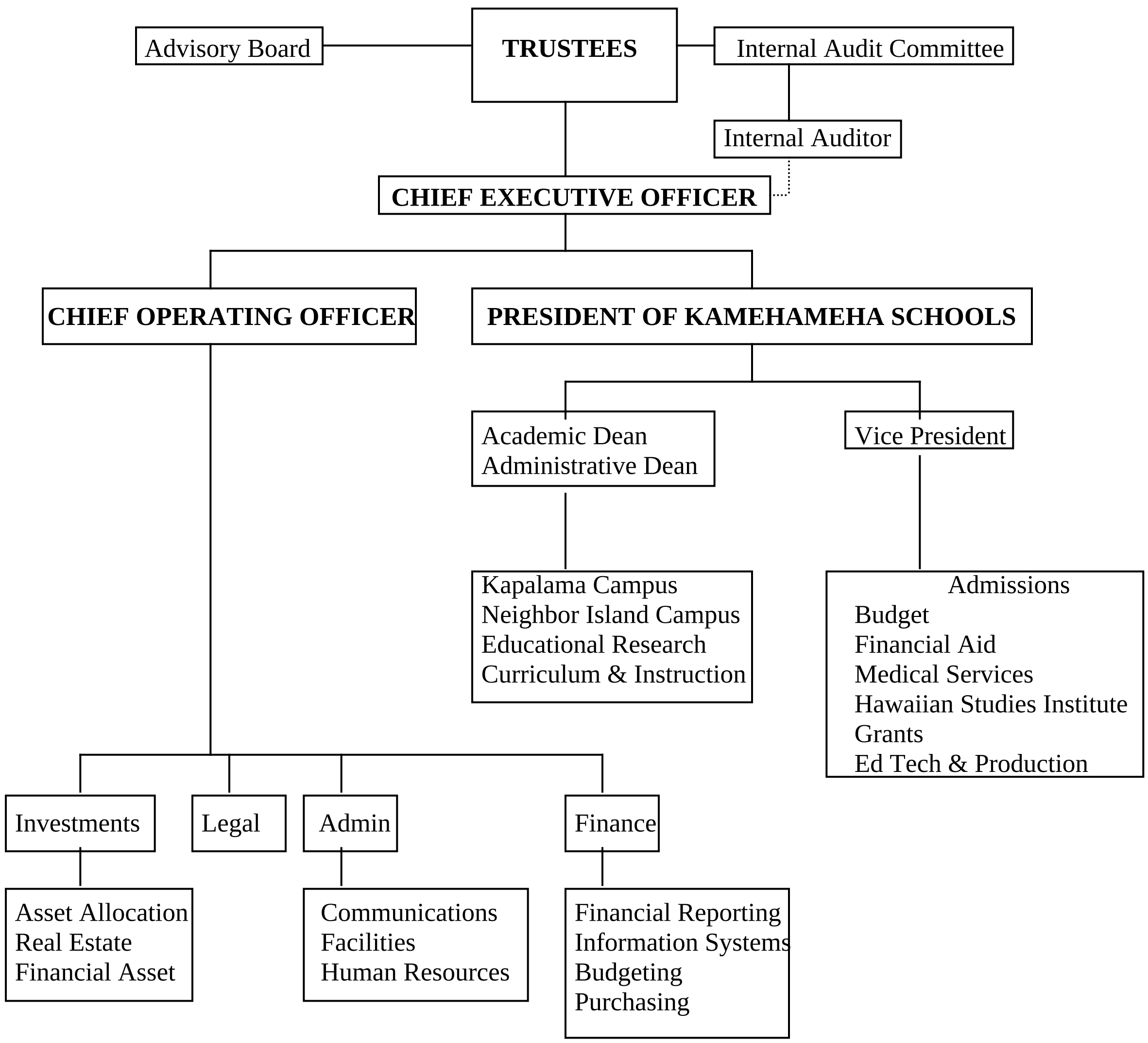
PAULA A. NAKAYAMA

MARIO R. RAMIL

cc: Hon. Virginia Lea Crandall
Administrative Judge
First Circuit Court

37

EXHIBIT I


Advisory Board
TRUSTEES
Internal Audit Committee
Internal Auditor
CHIEF EXECUTIVE OFFICER
CHIEF OPERATING OFFICER
PRESIDENT OF KAMEHAMEHA SCHOOLS
Academic Dean
Administrative Dean
Vice President
Kapalama Campus
Neighbor Island Campus
Educational Research
Curriculum & Instruction
Admissions
Budget
Financial Aid
Medical Services
Hawaiian Studies Institute
Grants
Ed Tech & Production
Investments
Legal
Admin
Finance
Asset Allocation
Real Estate
Financial Asset
Communications
Facilities
Human Resources
Financial Reporting
Information Systems
Budgeting
Purchasing

REAFFIRMATION SUBMISSION

EXHIBIT K

ROBERT BRUCE GRAHAM, JR. 1305-0
ASHFORD & WRISTON
Alii Place, Suite 1400
1099 Alakea Street
Honolulu, Hawaii 96813
Telephone No.: 539-0400

MAY 10 AM 8:25

E. PAGAY
CLERK

Attorney for Petitioners,
Richard Sung Hong Wong, Oswald Kofoad Stender, Marion Mae Lokelani Lindsey, Gerard Aulama Jervis and Henry Haalilio Peters
Trustees under the Will and of the Estate of Bernice Pauahi Bishop, Deceased

IN THE CIRCUIT COURT OF THE FIRST CIRCUIT

STATE OF HAWAII

In the Matter of the Estate Of BERNICE P. BISHOP, Deceased.	EQUITY NO. 2048 ORDER GRANTING PETITION FOR APPROVAL OF A PLAN FOR DETERMINING TRUSTEE COMPENSATION PURSUANT TO STIPULATION NO. 15 AND FOR CREATION OF A COMPENSATION COMMITTEE IN ACCORDANCE WITH THE PLAN; EXHIBIT "A" Hearing: April 30, 1999 Time: 10:00 a.m. Judge: Hon. Kevin S. C. Chang

ORDER GRANTING PETITION FOR APPROVAL OF A PLAN FOR DETERMINING TRUSTEE COMPENSATION PURSUANT TO STIPULATION NO. 15 AND FOR CREATION OF A COMPENSATION COMMITTEE IN ACCORDANCE WITH THE PLAN

This matter came on regularly for hearing on Friday, April 30, 1999, at 10:00 a.m. before the Honorable Kevin S. C. Chang in his courtroom in Ka'ahumanu Hale, Honolulu, Hawai'i. Deputies Attorney General Dorothy Sellers and Hugh R. Jones appeared for Margery S. Bronster,

RBG/228126.06

Attorney General, State of Hawaii, *parens patriae* to the Trust Estate. Robert Bruce Graham, Jr., appeared for Petitioners, the Trustees Under the Will and of the Estate of Bernice Pauahi Bishop, Deceased (the "Petitioners" or the "Trustees"). Also appearing was the Master, Colbert M. Matsumoto. Also present were David J. Gierlach for Trustee Marion Mae Lokelani Lindsey, Crystal K. Rose for Trustee Oswald Kofoad Stender, Ronald R. Sakamoto for Trustee Gerard Aulama Jervis, Kenneth M. Nakasone for Trustee Richard Sung Hong Wong, and Renee M. L. Yuen for Trustee Henry Haalilio Peters.

The Court has read and considered 1) the Trustees' Petition For Approval Of A Plan For Determining Trustee Compensation Pursuant To Stipulation No. 15 And For Creation Of A Compensation Committee In Accordance With The Plan and exhibits thereto filed herein on March 29, 1999 (the "Petition"); 2) the Objections Of Attorney General To Petition For Approval Of A Plan For Determining Trustee Compensation Pursuant To Stipulation No. 15 and exhibits thereto filed herein on April 27, 1999; 3) the Master's Report Regarding Trustees' Petition For Approval Of A Plan For Determining Trustee Compensation Pursuant To Stipulation No. 15 And For Creation Of A Compensation Committee In Accordance With The Plan Filed On March 29, 1999 and exhibits thereto filed herein on April 27, 1999 (the "Master's Report"); and 4) the records and files herein. All parties had an opportunity to be heard.

The Court accepts and approves the Master's Report.

NOW THEREFORE, good cause appearing and the Court being fully advised in the premises, IT IS HEREBY ORDERED, ADJUDGED AND DECREED as follows:

A. That the Trustees' Petition filed herein on March 29, 1999 be and is hereby GRANTED, subject to the following terms and conditions:

1. First, the Trustees' proposed plan shall be modified in accordance with the comments of the Master presented at pages 5 and 6 of the Master's Report; and

2. Second, by May 5, 1999, the Trustees shall provide complete, detailed answers to the Master' letter dated April 21, 1999, and produce all requested documents. Since Petitioners have apparently provided some information and documents to the Master on April 29, 1999, they are directed to review their production and, if necessary, supplement their answers and production to comply with the Court's order.

3. Third, while the proposed plan allows the Court-appointed committee up to six months to submit its determination of a reasonable compensation, the deadline for the initial committee to submit the determination shall be July 30, 1999, unless otherwise extended by the Court.

B. That attached hereto as Exhibit "A" and incorporated herein by this reference is the approved text of the Plan For Determining Trustee Compensation, which text includes the modifications made in accordance with the Master's comments (the "Plan").

C. That the following three (3) persons are appointed to serve as the initial members of the Committee created pursuant to the Plan for the purpose of determining the compensation of the trustees of the Kamehameha Schools Bernice Pauahi Bishop Estate:

per Cathy
Judge Chang's
Clerk
5/10/99

Allen K. Hoe

Michael E. Rawlins

Colbert Matsumoto

D. That the Court finds the foregoing persons are knowledgeable and informed persons each of whom possesses the integrity, probity, competence and disinterested status necessary to be qualified and serve as an independent and unconflicted Committee member under applicable IRS regulations.

E. That the Committee shall conduct itself according to the Plan (Exhibit "A") and shall render its decision in accordance with the Plan on or before close of business, Friday, July 30, 1999 unless the time is extended by the Court.

DATED: Honolulu, Hawaii, MAY 1 0 1999, 1999.

KEVIN S.C. CHANG
Judge of the above entitled Court

SEAL

APPROVED AS TO FORM:

DOROTHY SELLERS
HUGH R. JONES
Deputies Attorney General

COLBERT M. MATSUMOTO
Master

ROBERT BRUCE GRAHAM, JR.
Attorney for Trustees under the Will and of
The Estate of Bernice Pauahi Bishop,
Deceased

EQUITY NO. 2048 - Estate of Bernice Pauahi Bishop, Deceased
Order Granting Petition For Approval Of A Plan For Determining Trustee Compensation Pursuant To Stipulation No. 15 And For Creation Of A Compensation Committee In Accordance With The Plan; Exhibit "A"

EXHIBIT "A"

PLAN FOR DETERMINING TRUSTEE COMPENSATION

This is the Plan for determining the compensation of the trustees of the Kamehameha Schools Bernice Pauahi Bishop approved by the Circuit Court of the First Circuit, State of Hawai'i (the "Court").

PROCEDURAL BACKGROUND

Stipulation No. 15 of those certain Stipulations Concerning Master's Recommendations (109th, 110th, and 111th Annual Accounts) and Order entered herein on October 2, 1998, provides that Richard Sung Hong Wong, Oswald Kofoad Stender, Marion Mae Lokelani Lindsey, Gerard Aulama Jervis, and Henry Haalilio Peters, Trustees Under the Will and of the Estate of Bernice Pauahi Bishop, Deceased, (the "Trustees") shall submit to this Court for its review and approval a plan for determining trustee compensation that is in compliance with and satisfies applicable requirements of state and federal law, including without exception, federal Intermediate Sanctions legislation and Treasury regulations incident thereto, and H.R.S. Section 607-20, as amended by Act 310 of the 1998 Hawai'i State Legislature.

Stipulation No. 15 further provides that the plan shall include provision for the preparation of an independent professional study concerning reasonable trustee compensation which utilizes relevant and appropriate criteria, and that the study shall be commissioned under the auspices of the Court, by the Court's master or by such other person or entity as the Court shall order, consistent with requirements of applicable law and regulations.

Stipulation No. 15 also provides that the cost of any independent professional study shall be borne as an expense of the Trust Estate and that, should the Trustees or others wish to contest, rebut or supplement the study by commissioning another study, they shall do so at their own expense unless the Court first shall have approved the additional study as an expense of the Trust Estate.

THE TRUSTEES' RESPONSE

The Trustees filed herein on November 13, 1998, their Trustees' Response Concerning A Plan For Determining Trustee Compensation (the "Trustees' Response"). In the Trustees' Response, the Trustees set forth the following federal and state law backgrounds against which they proposed their plan:

Federal Background

As a tax-exempt educational organization, the Kamehameha Schools Bernice Pauahi Bishop Estate ("KSBE") may have its exempt status revoked if its net earnings "inure" in whole or in part to the benefit of individuals. It is well established, however, that the payment of reasonable compensation to individuals does not result in "private inurement" or private benefit. Under Section 4958 of the Internal Revenue Code, penalties are imposed, however, on "excess benefit transactions." A transaction is an excess benefit transaction if an economic benefit is provided by an exempt organization directly or indirectly to or for the use of any "disqualified person," such as a member of the entity's governing board, if the value of the economic benefit provided the disqualified person exceeds the value of the consideration received by the entity. Permitted consideration includes the performance of personal services.

In other words, while tax exempt entities are permitted to pay reasonable compensation for services rendered to them by members of their governing boards and other senior staff members, these persons are, generally speaking, "disqualified persons" for purposes of the Internal Revenue Code and Regulations, and their compensation is subject to federal scrutiny for reasonableness.

Proposed Internal Revenue Service ("IRS") regulations implementing Section 4958 were filed on July 30, 1998 in the Federal Register. They state that compensation of disqualified persons may not exceed *"what is reasonable under all the circumstances."* The proposed regulations also provide that *"[c]ompensation for the performance of services is reasonable if it is only such amount as would ordinarily be paid for like services under like circumstances."* Proposed Regulation § 53.4958-4(b)(3).

This standard is similar to the general rule of deductibility of compensation under existing IRS regulations. To be deductible as a business expense, compensation must be "reasonable." The applicable regulation, Reg. §1.162-7(b)(3), states in part as follows:

> *... the allowance [of a deduction] for the compensation paid may not exceed what is reasonable under all the circumstances. It is, in general, just to assume that reasonable and true compensation is only such amount as would ordinarily be paid for like services by like enterprises under like circumstances.*

Congressional reports describing proposed Section 4958 contain several statements that the standards developed under existing Reg. Section 162 are applicable in determining whether compensation is reasonable. The same reports state clearly that an individual is not required to accept reduced compensation merely because he or she renders services to a tax-exempt organization instead of a taxable entity.

The Congressional reports also state that the tax-writing committees expected the IRS to promulgate regulations under which a rebuttable presumption could be invoked if a tax-exempt organization followed a prescribed procedure for setting the compensation of its disqualified persons. Thus, the proposed Section 4958 regulations include such a rebuttable presumption procedure.

Under the proposed regulations, payments under a compensation arrangement between a tax-exempt educational organization and disqualified persons will be presumed to be reasonable if the following procedures are satisfied:

1. The compensation arrangement is approved by the organization's governing body or a committee of the governing body composed entirely of individuals who do not have a conflict of interest with respect to the arrangement;
2. The governing body, or a committee thereof, obtains and relies upon appropriate data as to comparability before making its determination; and
3. The governing body or committee adequately documents the basis for its determination concurrently with making that determination.

For a member of a committee or a governing body to be considered not to have a conflict of interest, the proposed regulations state that a member must not:

1. be related to (i.e., be a member of the family of) any disqualified person whose compensation is being determined;
2. be in an employment relationship subject to the direction or control of any such disqualified person;
3. be receiving compensation or other payments subject to the approval of such a disqualified person;
4. have any material financial interest that would be affected by the compensation arrangement; and
5. approve any arrangement with respect to a disqualified person who has approved or will approve a transaction providing economic benefits to the member.

In describing what data is appropriate as to comparability, the proposed regulations state that relevant information and appropriate data as to comparability would include, but not be limited to:

1. compensation levels paid by similarly situated organizations, both taxable and tax-exempt for functionally comparable positions;
2. the availability of similar services in the geographic area of the applicable tax-exempt organization;
3. independent compensation surveys compiled by independent firms; and
4. actual written offers from similar institutions competing for the services of the disqualified person.

State Law Background

Act 310 of the 1998 Hawai'i State Legislature amended the long-established method of determining the compensation of charitable trustees. Prior to January 1, 1999, trustee compensation was based upon a schedule of percentages applied to the annual income of the Trust Estate and certain other amounts. Effective January 1, 1999, the existing schedule is abolished as to the trustees of charitable trusts, although it remains in effect for trustees of other trusts.

As amended, § 607-20 of the Hawai'i Revised Statutes provides in full as follows:

> *(a) Notwithstanding any other provisions, in the case of a charitable trust, the compensation of the trustees shall be limited to an amount that is reasonable under the circumstances.*
>
> *(b) This section shall apply to existing and new charitable trusts established after the effective date of this Act: provided that any provisions in existing trust agreements regarding trustee compensation shall supersede this section.*

The preamble to Act 310 reads as follows:

> *The legislature finds that there is a long-standing tradition, whereby trustees of most charitable trusts serve without compensation. While the*

legislature considers such voluntary service to be admirable, it believes that trustees of charitable trusts should not be prohibited by statute from receiving compensation. However, trustees who receive compensation from a charitable trust have a fiduciary duty to make sure such compensation is not in excess of what is reasonable under the circumstances. In addition to this common law duty, such trustees are subject to penalty under federal intermediate sanctions law if they allow their compensation to exceed what is reasonable under the circumstances. Knowledgeable and well-intentioned people can differ on what is reasonable compensation in any particular situation, but such controversies are best resolved by a judge who can take into account all relevant circumstances as presented by parties on both sides of the issue. Thus, the purpose of this Act is to codify the duty of trustees not to accept compensation above what is reasonable under the circumstances.

THE PLAN

1. The Court shall periodically appoint a committee (hereinafter, the "Committee") for the purpose of determining the compensation of the trustees of the Kamehameha Schools Bernice Pauahi Bishop Estate (hereinafter, the "KSBE Trustees").

2. The Committee shall be comprised of three (3) to five (5) persons as determined by the Court from time to time.

3. The Court shall constitute the Committee upon the petition of the KSBE Trustees, the Attorney General as *parens patriae* to the Trust Estate, or the Court's then-incumbent master.

4. Initially, the Committee shall be constituted by the Court within thirty (30) days of the entry of an order approving this Stipulation. Thereafter, the Committee shall be constituted not less often than once every three (3) years and, failing petition by the Attorney General or the incumbent master, it shall be the responsibility of the KSBE Trustees to cause the filing of a petition at least every third year.

5. The Committee shall consist of knowledgeable and informed persons, each of whom the Court finds to possess the integrity, probity, competence and disinterested status

necessary to be qualified and serve as an independent and unconflicted Committee member under applicable IRS regulations.

6. The Court shall designate the members of the Committee.

7. The sole issue to be determined by the Committee shall be *"What is a reasonable annual amount of compensation to be paid to each of the trustees of the Kamehameha Schools Bernice Pauahi Bishop Estate?"*

8. The Committee shall commission an independent compensation survey from a national, independent, professional consulting firm active in the field of executive and trustee compensation. The Committee shall be authorized to commission additional independent compensation surveys if, by simple majority vote of its members, it shall determine that one or more additional surveys are reasonably necessary or appropriate.

9. The firm or firms commissioned by the Committee to make a compensation survey shall (i) study compensation levels paid by similarly situated organizations, both taxable and tax-exempt, for functionally comparable positions; (ii) review and report the availability of similar services in Hawai'i; (iii) interview the KSBE Trustees and their staff and the Attorney General as *parens patriae* to the Trust Estate; (iv) compile independent compensation surveys for review by the Committee; and (v) render its report to the Committee establishing a range of trustee compensation that is comparable, reasonable and consistent with applicable law and regulations. In addition to the factors enumerated above, the Committee shall have authority to require the consideration of other relevant factors by the firm or firms. The cost of any compensation surveys and reports commissioned by the Committee shall be borne out of the Trust Estate.

10. The KSBE Trustees and the Attorney General as *parens patriae* to the Trust Estate shall be entitled to submit such evidence, testimony and independent professional studies for the

Committee's review and consideration as may be pertinent and material to the Committee's deliberations.

11. The KSBE Trustees' reasonable costs and expenses may be paid out of the Trust Estate only upon the express approval of the Court.

12. The Attorney General's reasonable costs and expenses may be reimbursed out of the Trust Estate only in accordance with the provisions of H.R.S. Section 554-8.

13. The Committee's deliberations shall not be public proceedings and the Committee shall not be obliged to receive any public testimony unless the Committee by simple majority vote shall determine to do so. Without limiting the generality of the foregoing, the Committee shall not be obliged to receive any public testimony unless the same is responsible, probative, pertinent and material.

14. The KSBE Trustees or their representative, the Attorney General or a deputy, and the incumbent master shall be entitled to audit and observe but not participate in the proceedings of the Committee. Any testimony received by the Committee shall be in writing and shall be subject to inspection and copying by the KSBE Trustees, the Attorney General and incumbent master.

15. The Committee shall render its decision within six (6) months unless the time is extended by the Court for good cause.

16. No Committee shall be compensated, except for reimbursement of its reasonable out of pocket expenses, until its decision has been filed or as otherwise ordered by the Court.

17. If the Committee fails or is unable to render a timely decision, the Court, upon petition of the KSBE Trustees, the Attorney General, or the incumbent master, shall constitute a new Committee.

18. If a vacancy arises on a Committee, the Court, upon petition of the KSBE Trustees, the Attorney General, or the incumbent master, shall fill the vacancy.

19. The Committee shall file with the Court and deliver to the KSBE Trustees, the Attorney General and the incumbent master all professional compensation studies commissioned or received by it, together with statements of the credentials of the firms preparing the studies.

20. The studies shall be accompanied by a report of the Committee's determination of reasonable trustee compensation. The Committee's determination shall be consistent with the studies and with any other appropriate comparability data received by the Committee. The Committee's determination of reasonable trustee compensation may be expressed as a range of appropriate annual compensation or a limit upon annual compensation. It may provide for differing levels of compensation for individual trustees based upon considerations appropriate under state and federal law and regulations. The Committee's report of its determination shall include a clear, concise and concurrent exposition of the basis for its determination and shall be accompanied by true and correct copies of any and all documents specifically referred to therein.

21. The Committee may but shall not be required to file with the Court any other written evidence or submissions received, gathered or considered by it. Any such additional filings shall be delivered to the KSBE Trustees, the Attorney General and the incumbent master.

22. The Committee's determination shall be determined by a simple majority of the Committee. Dissenting Committee members shall be entitled to file with the Court a statement of their dissent and the reasons therefor.

23. Upon receipt of the report of the Committee, the Court shall schedule a hearing at which the KSBE Trustees, the Attorney General and the incumbent master shall be afforded an opportunity to be heard.

24. The Committee's determination shall be entitled to a presumption of reasonableness. The Court may approve, disapprove or modify the determination of the Committee. If approved by the Court, the determination of the Committee shall be final, conclusive and binding, subject only to appeal as provided in the rules of court. If the Court finds the Committee's determination to be clearly erroneous or the Committee to have abused its discretion, the Court may disapprove the determination, which then shall be null and void, and the Court shall either recommit the matter to the Committee or promptly constitute a new Committee.

25. If the determination of the Committee is modified by the Court, any such modification shall be made in manner consistent with applicable provisions of state and federal law and regulations with the object of assuring that the compensation paid the KSBE Trustees is reasonable within the meaning of both state and federal law and regulations.

26. The Court shall disapprove the Committee's determination in the following circumstances: (a) where the decision was procured by corruption, fraud or undue means; or (b) where there was evident partiality or corruption in the Committee or any of its members; or (c) where the Committee members or any of them were guilty of misconduct, in refusing or neglecting to obtain the required independent studies, or in refusing to hear evidence pertinent and material to the issue of compensation proffered by the KSBE Trustees or the Attorney General as *parens patriae* to the Trust Estate, or of any other misbehavior, by which the interests of KSBE or its trustees have been prejudiced; or (d) where the Committee exceeded its powers or so imperfectly executed them that a determination consistent with applicable law, court orders and IRS regulations, was not made.

27. The foregoing shall not be deemed or construed to limit the Court's authority to modify or disapprove the Committee's determination for other cause.

28. The Committee shall be reasonably compensated out of the Trust Estate for its services and its compensation shall be fixed by the Court.

29. The Committee, but not individual members, shall be authorized to retain competent tax counsel to advise it concerning its procedures and to assist it in its mandated activities. Any such retention shall be subject to the prior approval of the Court. Counsel's reasonable and approved fees shall be paid out of the Trust Estate upon approval by the Court.

30. Committee members shall not by reason of their service be deemed to be state officers nor officers of the Court and their action shall not constitute state action for any purpose.

31. The Committee's records and files shall be retained for the period under review and for seven (7) years thereafter at the offices of the Trust Estate. The Committee's records and files, except such as shall have been filed with the Court by the Committee, shall remain under seal of the Court, available for inspection only by the Court, future masters, the Attorney General as *parens patriae* to the Trust Estate, future Committees, and the Internal Revenue Service of the United States.