IN THE CIRCUIT COURT OF THE FIRST CIRCUIT

STATE OF HAWAII

---:---

In the Matter of the Estate	)	EQUITY NO. 2048
	)	
of	)	**EXHIBITS RE**
	)	**DEPOSITIONS OF**
BERNICE P. BISHOP,	)	**JOHN D. WAIHEE, VOL I**
	)	**MARION MAE LINDSEY**
Deceased.	)	**VOL III**
	)	(EXHIBITS 127 - 142)

EXHIBITS RE

DEPOSITIONS OF JOHN D. WAIHEE, VOLUME I &
MARION MAE LINDSEY, VOLUME III

Taken on November 26 & December 4, 1999.

TAB 1

VERNER, LIIPFERT, BERNHARD, MCPHERSON AND HAND
CHARTERED

901-15TH STREET N.W.
WASHINGTON D.C. 20005-2301

8280 GREENSBORO DRIVE
SUITE 601
MCLEAN VIRGINIA 22102
703 749-6000
TELECOPIER 703 749-6027

202 371-6000
TELECOPIER 202 371-6279

2600 TEXAS COMMERCE TOWER
600 TRAVIS
HOUSTON TEXAS 77002
713 237-9034
TELECOPIER 713 237-216

Douglas Ochs Adler
(202) 371-6037

PRIVILEGED AND CONFIDENTIAL
COMMUNICATION OF COUNSEL

March 15, 1995

Nathan T.K. Aipa, Esq.
General Counsel
Kamehameha Schools/Bernice Pauahi Bishop Estate
Legal Division
P.O. Box 3466
Honolulu, HI 96801

Re: Kamehameha Schools/Bishop Estate Trust ("KSBE Trust"): Change of Place of Administration

Dear Mr. Aipa:

As we discussed previously, we are identifying issues that must be addressed before a decision to petition the court to move the administration of the KSBE Trust out of Hawaii can be made. Under H.R.S. § 560:7-305, the court may approve such a move if it will further the efficient administration of the trust. In addition, the move must not be contrary to the express or implied intent of the trust grantor, nor be to the detriment of the trust beneficiaries.

We believe there are several arguments to be made for a more efficient administration of the KSBE Trust in another jurisdiction. These arguments center on the potential interference with the efficient administration of the KSBE Trust by the Hawaii State Legislature, restrictions on alienation of property by trustees under Hawaiian law, and disadvantageous state tax treatment in Hawaii. In order to further develop these arguments, we need some additional information:

Deposition Exhibit No. 127
Deponent Wahee
Date 11-26-99

K028684

127

1. Bernice Pauahi Bishop's will contains a provision in Paragraph 13 requiring the filing of a report with the "Chief Justice of the Supreme Court, or other highest judicial officer in this country." (emphasis added) Paragraph 14 calls for the selection of trustees by a majority of the Justices of the Supreme Court. At the time of the execution of the will, Hawaii was an independent kingdom. The issue is the interpretation of the phrase "in this country" after Hawaii became a territory, then a state. Was there a particular decision by the Supreme Court, the Attorney General, or the KSBE trustees that "in this country" was interpreted to mean Hawaii?

2. H.R.S. § 554-4 provides that trustees are to file annual reports with the supervising court. The court may then refer the report to a master for review, if proper and necessary. We have received a copy of the master's report dated September 8, 1993. Under what authority does the master investigate and prepare his or her report on the KSBE Trust? Is the form of the report mandated by the Hawaiian Supreme Court, and may the form by shortened or simplified? Reference is made in the report we reviewed to the "Amended Order Establishing Minimum Guidelines For Future Masters and Instructing Trustees Concerning Future Annual Reports," dated July 12, 1989, as amended by Order dated June 8, 1992. These are documents of public record, and we would appreciate receiving copies of these as well.

3. Would you provide us with the statutory provision authorizing the Attorney General to act as parens patriae of Hawaiian charitable trusts.

4. We also need a detailed list of current assets held by the KSBE Trust. The list of assets (and particularly their location) may help buttress the argument that administration would be more efficient offshore because of tax considerations, for example. The breakdown should include assets by type such as real estate, marketable securities, and all investments. In particular, we need the location of each asset (in or out of Hawaii), and the percentage of that asset's value to total holdings. Also helpful for this argument would be copies of the most recent balance sheet and income statement.

5. It appears from review of the tax returns included in the 1993 master's report that the KSBE Trust is a 501(c)(3) charitable trust and public charity (not private foundation) for federal tax purposes. Would you please confirm its federal tax status, including whether it is treated as a corporation for federal tax purposes.

Thank you in advance for your assistance with these requests. Please contact me if you have any questions or concerns.

Sincerely yours,

Douglas Ochs Adler

cc: Gov. John D. Waihee

K028686

bcc: Denis J. Dwyer

NOTES FROM PH MTG: Adler, Aipa, Jervis, Waihee, Wong
March 22, 1995

TRANSFER OF DOMICILE

Looking at arguments that woulc make the case of beneficial transfer

Law not clear as to whether trust assets can be moved to a corporate entity en total without court approval

Bishop Museum; Midkiff are examples

As long as the intent of the trust, and trustees still held accountable, assets can be transferred without judicial consent

Argument would be easier if the corporate entity were set up first; also afford limited liability, although standard would be the same

School district encorporate as well(?)

If considered more prudent to go to the court, then more work would be needed

Different fact pattern for Museum

Info: types of assets so tax consequences can be established

If argument gets close, then details can get fleshed in (Gerry)

If can move from a trust to a corporation, then lateral move out of the state would be easier (Gerry)

If school and trust can be incorporated as one would be politically preferable (Gerry)

Generally, the trustees and the beneficiarires have to maintain a separate entity
How about the school being the member of the charitable corporation

There is a ruling regarding the beneficiary status of the school

There is precedent for transfer without consent, but the trust has gone to the court in the past; what is in the order set down by the court

When the for profits were set up, did the trust go back to the courts? Yes, out of caution; first check with IRS, IRS said go back to the courts to see if OK under will, then we'll take a look at it

128

If trustees are willing to transfer without court permission, could fashion a legal memorandum that would be within court guidelines; may be policy decision

May want to take the first step without court approval, then second with

To move to another jurisdiction after corporate entity is set up, would court approval be needed?

Scenario: get on firm ground to move to corporate entity, then move to another jurisdiction (without court approval?)

Doug: can be done

Would still have to research whether trustees would still have to be appointed by the court

Question on appointment by highest judicial officer in the country

Week of April 17 OK?

MEMORANDUM

TO: Suzanne Cartwright

FROM: Douglas O. Adler

RE: Bishop Estate/Relocation of Assets -- Weekly Status Report

DATE: April 14, 1995

On Monday, April 10, 1995, Sue Temkin and I met with Trustee Gerry Jervis, General Counsel Nathan Aipa, Governor Waihee, Denis Dwyer and Norma Wong. We reviewed the comprehensive information request that had been prepared the prior week. In addition, we discussed some of the underlying issues giving rise to the request to identify possible alternative sites for administration of the Trust's assets. As a result of the meeting several action items were identified:

1. Survey Trip. It was tentatively agreed that Ms. Temkin and I would make a survey trip to Honolulu to review various items at the offices of Mr. Aipa and, further, to meet with Bruce Graham. It is possible that we would meet with other KSBE staff as well. This trip has been tentatively scheduled for the week of May 8, pending confirmation from Mr. Aipa.

2. Research. Several areas were identified as requiring legal research. These include the following:

   a. The reasonableness of the Trustees' compensation under Section 501(c)(3) of the Internal Revenue Code.

   b. Whether there might be a 10th amendment or preemption issue with fespect to a state's right to establish compensation for Trustees versus IRS determination of reasonableness.

   c. Survey of other domiciles to determine if they would be more favorable.

   NY, DE, CA, HI TX

   d. Internal governance issues under corporate versus trust law.

   [illegible]

   e. Authority of the Master to review the internal workings of the Trust.

   f. Authority of the attorney general as parens patriae.

Upon conclusion of the survey trip and the legal research, a "White Paper" will be prepared.

K100054

Deposition Exhibit No. 129
Deposition of Waihee
Date 11-26-99

129

VERNER, LIIPFERT, BERNHARD, McPHERSON AND HAND
CHARTERED

HAWAII TIMES BUILDING
928 NUUANU AVENUE SUITE 400
HONOLULU HI 96817
(808) 566-0999
TELECOPIER (808) 566-0995

June 1, 1995

To: Nathan T. K. Aipa, Esq.

From: Norma Wong Norma Wong

Re: TRANSMITTAL OF DOCUMENTS

Enclosed are two documents for your review and further discussion:

(1) **"Trustee Compensation Issue - Executive Summary"** by Susan Temkin and Lawrence Cooper, which addresses the question of whether the doctrine of federal preemption applies to the Internal Revenue Service's review and any decision regarding the statutory compensation formula.
[TRS/General, KSBE Ref. No. N701, VL Ref. No. 5175.0001]

(2) **"Trustee Compensation Issue"** by Susan Temkin and Lawrence Cooper, which is the basis for the executive summary described above, and includes appropriate legal citations.
[TRS/General, KSBE Ref. No. N701, VL Ref. No. 5175.0001]

Please let me know if you and/or Gerry Jervis would like to discuss this issue in more detail with the attorneys, or require additional work on the matter.

Delivered to you this morning::

(3) **"Various Issues To Be Considered With Decision to Transfer Domicile of the KSBE Trust"**, which describes the various factors that are included in VL's analysis of the pros and cons of transferring domicile, and in evaluating the most favorable jurisdictions.
[TRS/General: Domicile Evaluation C95-2, KSBE Ref. No. N701, VL Ref No. 5175.0008]

VL is proceeding with a comprehensive analysis on the subject. This is an "outline" of subject matter addressed in the comprehensive analysis. The memo emphasizes that in order to make the analysis useful, we need guidance from the Trustees as to the relative importance of these factors. As we discussed, you'll set up a conference call with Bruce Graham, VL attorneys,

*Verner, Liipfert, Bernhard, McPherson and Hand Chartered is a law corporation with offices in Washington, D.C., Honolulu, Hawaii, McLean, Virginia, and in Houston and Austin, Texas. The named shareholders are not licensed to practice in Hawaii.

K028768

Deposition Exhibit No. 130
Deposition of Walker
Date 11-26-99

130

and yourself to discuss factors of importance to maintaining the integrity of the trust. Depending on the scope and nature of this discussion, it may be opportune to have a follow up call with Gerry Jervis to begin the prioritization process, just as far as relative importance to institutional needs - with the understanding that the Trustees as a whole will need to discuss priorities in the context of broader policies.

My secretary, Carol, will call your secretary on Monday with available time slots for the Graham conference call.

Also delivered to you this morning:

(4) **"Tax Exempt v. Taxable Status of KSBE Trust"** by Douglas Adler and Susan Temkin, which addresses the issue of whether KSBE can convert from tax-exempt to taxable status, and the pros and cons thereof.
[TRS/General: Institutional Status, C95-6, KSBE Ref. No. N701]

After you and Gerry Jervis have had a chance to review this memorandum, I suggest a conference call with the preparing attorneys to explore where we might go from here.

cc: Trustee Gerard Jervis
Governor John Waihee

MEMORANDUM

TO: Trustee Richard Wong
Trustee Oswald Stender
Trustee Lokelani Lindsey
Trustee Henry Peters
Trustee Gerard Jervis

FROM: John Waihee

RE: Analysis of The Impact of the Wall Street Journal Article

DATE: April 27, 1995

I suspect by now each of you has had the opportunity to review and discuss among yourselves Tuesday's Wall Street Journal article on Kamehameha Schools/Bishop Estate. From my view, the article revealed little new information that has not already been in the media here in Hawaii.

From the national perspective, however, we are beginning to see some expanded interest in KSBE and a further interest not only by the Internal Revenue Service, but by the Treasury Department and the U.S. Congress.

Today one of my partners, Lawrence Cooper, attended the first part of "Representing and Managing Tax-Exempt Organization", an annual two day continuing legal education program presented at Georgetown Law Center in Washington DC. The selected faculty for the program includes Treasury and IRS

VLDC01-35267.1

Deposition Exhibit No. 131
Deposition of WAihee
Date 11-26-99

131
P016108

officials, counsel to Congressional committees as well as distinguished exempt organization practitioners.

The first speaker was Michael Superata, Esq., counsel to the House Subcommittee on Oversight of the House Committee on Ways and Means. The title of his presentation was "Tax Policy and Exempt Organizations: A View From the Hill". Most of his presentation addressed legislation considered during the 103rd Congress regarding the imposition of intermediate sanctions against public charities (such provisions are similar to present law sanctions imposed on private foundations). Pursuant to last year's proposed legislation, sanctions would be imposed in cases of excessive salaries and benefits paid to certain disqualified persons with respect to a public charity. He noted that these provisions could be reintroduced during the 104th Congress.

In the course of his presentation, he also mentioned that he had read a Wall Street Journal article regarding the Bishop Estate and commented on his surprise in learning that the trustees of the Estate received over $900,000 in compensation. Although he clearly stated that he did not know the circumstances, the mention of the Bishop Estate article at the particular point in his presentation highlighted his concerns.

The second speaker was Catherine Livingston, Esq., Attorney-Advisor.- U.S. Treasury Dept. Office of Tax Policy. During her presentation on current matters before the IRS and Treasury, she noted that some guidance would be forthcoming on the Section 4941 self-dealing rules applicable to private foundations. One of the attendees asked whether the guidance on self-dealing would include any clarification of the Treasury and IRS positions on reasonable compensation. She responded that the attendee would have to review the guidance once it was released. It was Lawrence's impression that this non-answer suggests that the guidance will address reasonable compensation.

Based upon these developments, as well as our views expressed earlier, we would urge that contacts be made, not only with the Internal Revenue Service, but also, based upon what we learned today, with the Treasury Department. Additionally, contacts with the House Ways and Means Committee, Senate Finance Committee and the House and Senate Banking Committees should be considered. I believe that if a dialogue is initiated with these agencies and Congressional Committees, we will minimize the potential for conflict and the possible mischaracterization of the facts which may concern these entities by the Wall Street Journal, CNN or the Honolulu Advertiser reports. Without the initiation of a dialogue, the Estate's ability to provide both context and accuracy to the issues raised by the media will be diminished. Our concern is that KSBE will again be in the position of reacting to inquiries, only this time the inquiries will be from a much more serious source than the media.

This advice is not offered by way of attempting to supplant the ongoing relationship that the Estate has with Mark McConaghy. Although I have not talked with Mark, I believe that he will make the same suggestions. It is important, however, that these decisions be made quickly so that the Estate will be in a proactive position with each of these agencies and Committees and attempt to work with them, rather than responding to them.

Finally, Lawrence sent along the attached article which appeared in the April 1995 edition of The Exempt Organization Tax Review, and was handed out at today's Georgetown program. It contains a brief analysis of a private letter ruling (LTR 9505020) which the author was able to conclude was issued to the Bishop Estate. The author is concerned with the IRS failure to tax the real estate transactions described in the ruling. A copy of the analysis is attached for your reference.

Please let me know if you wish to discuss any of these matters further. I am prepared to work with you in any way that may be helpful to dealing with these developments.

VLDC01-35267.1

MEMORANDUM

TO: Dennis Dwyer

FROM: Lawrence Cooper

RE: CLE Program/Representing and Managing Tax-Exempt Organizations

DATE: April 27, 1995

Today I attended the first part of "Representing and Managing Tax-Exempt Organization, an annual two day continuing legal education program presented at Georgetown Law Center. The selected faculty for the program includes Treasury and IRS officials, counsel to Congressional committees as well as distinguished exempt organization practitioners.

The first speaker was Michael Superata, Esq., counsel to the House Subcommittee on Oversight, Committee on Ways and Means. The title of his presentation was "Tax Policy and Exempt Organizations: A View From the Hill". Most of his presentation addressed legislation considered during the 103rd Congress regarding the imposition of intermediate sanctions against public charities (such provisions are similar to present law sanctions imposed on private foundations). Pursuant to the proposed legislation, sanctions would be imposed in cases of excessive salaries and benefits paid to certain disqualified persons with respect to a public charity. He noted that these provisions could be reintroduced during the 104th Congress.

In the course of his presentation, he also mentioned that he had read a Wall Street Journal article regarding the Bishop Estate and commented on his surprise in learning that the trustees of the Estate received over $900,000 in compensation. Although he clearly stated that he did not know the circumstances, the mention of the Bishop Estate article at the particular point in his presentation highlighted his concerns.

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I also note that the April 1995 edition of The Exempt Organization Tax Review, which was handed out at the program, contains a brief analysis of a private letter ruling (LTR 9505020) which the author was able to conclude was issued to the Bishop Estate. The author seems to be a bit concerned with the IRS failure to tax the real estate transactions described in the ruling. A copy of the analysis is attached for your reference.

Notes of Discussion w/ L. Cooper Re GU Tax Exempt CLE
4/27/95

Tax Exempt - ABA Bruce Hoskins

1st Speaker Michael Schaham.
Atty w/ Holder SC on oversight
Intermediate Sanctions
Context of Exam. Be Bit much.
Aiming & Limited ally

Letter Ruling in November ruled favorably on unrelated bus.
transaction
In Tax Exempt Org. Review
Obvious Mis Conduct
Exempt Org Tax Review.

Treasury - Bruce Hopkins
Kathryn Livingston - Tax Policy
Smith Forbes
Self Dealing rules for Private Foundation. Put in Revenue Ruling.
Whether issue Unreasonable Compensation included
And arc read

Intermediate Sanction - Gen Basis of legis. History

PRIVILEGED AND CONFIDENTIAL
ATTORNEY-CLIENT COMMUNICATION

October 4, 1995

To: KSBE Trustees

From: John Waihee
Denis Dwyer
Norma Wong

Re: BACK UP POSITION

Our efforts in opposition to the interim sanctions legislation have thus far concentrated on the short-term; that is, removing the interim sanctions in their entirety from the proposed legislation. At this time, we are cautiously optimistic that we will be successful in the Senate. Whether or not this objective will prevail in conference remains to be seen. In addition, there are similar proposals that could advance this session if it appears that the current proposal won't pass, such as the Stark-Houghton bill, which are even more objectionable in their impacts. Should we prevail this session, it is unlikely that Congress will dismiss the matter in entirety. A reprieve for the moment may be just that - a reprieve.

It cannot be over-emphasized that our first objective is to remove the interim sanctions in their entirety from the proposed legislation. If this objective cannot be accomplished in entirety, and Congress is compelled politically to address the general issue of interim sanctions, we must consider ways to amend the current proposal in a way that will minimize adverse impacts to the institution.

Attached is a draft outline of proposed backup positions for those elements of the interim sanctions proposal that are the most agregious, which were developed in concert with Mark McConaghey and Mike Repass of Price Waterhouse.

Deposition Exhibit No. 132
Deposition of Waihee
Date 11-26-99

132

BACKUP POSITIONS
IN THE EVENT THE INTERIM SANCTIONS PROPOSAL SURVIVES

Introduction

The first objective is to remove the interim sanction provision in its entirety from the proposed legislation. If this objective cannot be accomplished and Congress is compelled politically to address the general issue of interim sanctions, we must consider ways to amend the current proposal. The following are suggestions of alternative positions for consideration.

"Safe Harbor"

Modify the scope, operational rules and contents of safe harbors.

- Change the standards that the IRS must meet to establish that the compensation determined in compliance with the safe harbor is nonetheless unreasonable:
    - Require that the presumption of compensatory reasonableness created by the safe harbor can only be negated by the IRS proving by of clear and convincing evidence (the highest standard of evidence necessary to rebut a presumption) that the compensation was unreasonable
- Create additional or alternative safe harbor provisions:
    - Create a safe harbor that is based upon compliance with the conditions of a state statute (See section below entitled "State or Judicial Action Creating Presumption of Reasonableness)
- Modify or replace existing safe harbor language
    - Make clear that compensation is reasonable if the compensation package is comparable to <u>either</u> tax-exempt or for-profit taxable organizations
    - Use of a "Business Judgment Rule" in determining reasonableness of compensation. For example, compensation would be considered reasonable if paid in good faith belief that it was reasonable and that the payment of such amounts was consistent with ordinary business care and

prudence. Such a standard is presently used in determining the reasonableness of compensation for purposes of certain private foundation provisions regarding taxable expenditures

- Expand which parties may provide independent review to include:
  - An Independent Committee
  - A Court of Competent Jurisdiction

- Specify the weight of factors in the safe harbor:
  - Use of nationally recognized compensation experts increases presumption of correctness
  - Use of two independent professional studies creates presumption of reasonableness of compensation
  - Insert affirmative statement that potential for exposure to liability for fiduciaries is a factor to be considered when determining the extent of "services" provided and therefore in turn the reasonableness of compensation

Penalties

- Lower from 25% to 5% the penalty imposed upon a disqualified person upon receipt of an excess benefit; the penalty then would be equal to 5% of the amount of the excess benefit

- Lower from 200% to 100% the penalty imposed if the person who receives the excess benefit does not return it or take corrective action; the penalty would then be equal to 100% of the amount of the excess benefit

__ State or Judicial Action Creating Presumption of Reasonableness

Background

The Joint Committee on Taxation's description of the legislative proposal on Intermediate Sanctions contains a footnote which assumes that a State or local legislative body or court of competent jurisdiction authorized or approved a particular compensation package paid to a disqualified person would not be determinative of the reasonableness of compensation paid for purposes of the penalties provided by the interim sanctions proposal.

- Modify Statutory and/or Committee Language:
  - Modify the legislative language and the description of the proposal to provide an affirmative statement that any amount paid up to or within the state formula is conclusively presumed reasonable compensation. The legislature should be considered an independent body.
  - As an alternative, footnote language should be excluded from any Senate Report language and the Conference Report should explain that the footnote was removed because the state law should be determinative (or be given substantial weight) as to the reasonableness of the compensation.

Create Exemption for Educational Institutions

- Exempt all educational institutions (schools, colleges and universities) from the interim sanctions proposals

ksbe2:backup1

Exit Tax

- Remove the "exit tax"

- Limit the application of the "exit tax" to terminations of exempt status that result from either willful, repeated excess benefit transactions or a willful and flagrant excess benefit transaction

Transition Period

- The interim sanction provisions shall only be effective for payments for services in cash, services and/or property or for investments entered into after January 1, 1996

- Make the effective date for the application of the intermediate sanctions to tax-exempt organizations the date that the Secretary issues final regulations or January 1, 1998, whichever is later

- Make the effective date until January 1, 1998 for the application of the interim sanctions provisions for organizations that have made a good faith effort to comply with the provisions of the safe harbor as of the date of the proposal's enactment.

- Include a binding contract exception, effective for contracts binding and entered into on or before the date that the Secretary issues final regulations or January 1, 1998, whichever is later

Disclosure, Reporting and Substantiation Requirements

- Remove the increased disclosure, reporting and substantiation requirements

- Alternatively, provide for less burdensome disclosure, reporting and substantiation requirements. For example, with respect to the substantiation of compensation that was not reported on Form W-2, language could be added that would provide that a failure to include compensation benefits on Form W-2 would not result in treatment of such benefits as prohibited excess benefits if the failure was inadvertent or the amount involved was no more than than some minimal amount.

Disclosure to States

- Prohibit any information transferred to the State and its representatives from being publicly disclosed and provide stiff penalties on individuals, personally, who violate this rule.

- Alternatively, prohibit any information transferred to the State and its representatives from being publicly disclosed and provide such officials would be required to comply with the same nondisclosure rules applicable to the IRS personnel or be subject to the same individual liability.

Advance Ruling

- Develop an advance ruling mechanism, by which the IRS would have to rule in advance on the reasonableness of the methodology used in determining compensation, the reasonableness of the compensation and the applicability of the safe harbor provision.

Appendix A

The factors and information that would be considered in determining the reasonableness of compensation turn on comparisons to individuals in comparable positions.

- geographic location
- required skills (technical, managerial, interpersonal)
- education and experience of candidate
- educational and experience requirements for the position
- scope of duties (investment, management, planning, etc.)
- time commitment requirements of position
- statutory standards
- consistency with ordinary business care and prudence standards
- compliance with statutory compensation formula limitations
- other relevant factors

ksbe2 backup1

3-10-98
Trustees Mtg

Mike
As part of the WASC committee, they are supposed to set aside time to meet with the trustees. This meeting is supposed to be arranged by the committee - IN ADVANCE - & check with the trustees through the chairman to decide on an appropriate time.
Oz said the Chair, who he met at the airport (they were on the same plane) asked him to meet with them & Oz said he would be happy to do it.

Nam
House Bill 2362 H.D.1

Kekoa - Song contest package will be falling together

Deposition Exhibit No. 133
Deposition of Lindsey
Date 12-4-99

3-17-98
TRUSTEES MTG

"I don't want to scold them but I want to give them a positive meeting"

Yuki
Closing Kamamalu & Kalama during the holidays - Thurs - Fri & Sat for electricians to resplice as part of the enhancing electrical ~~problems~~ capability

Rodney
· Discussing compensation plan. Wants to find out about what to do since the vote

Nam
C&C - Donna Kim wants to extend the time on Kaiwi due to Gov. correspondence.

3-17-98
Trustees Meeting

Nam (cont)
- Land Use issues that we are tracking
- Trustees Commissions still alive
- Bill tracking of DOE bills are given to personnel.

Kekoa
- Nibbles on Keauhou Beach from Big Island reporters
- Peterson Group questions.
- Mid Ocean questions.

[illegible]efer Korn - Ferry
Rodney is following up on one thing for speaker.

[illegible]efer.

4-6-98
TRUSTEES MTG

Nam

Decision making hearing.
Senate on Commission Bill.
Take out % percentages &
put in "reasonable compensation".
Formula by statute.
Thursday - bill ~~to~~ be decked
& sent to the house.

Lease to fee mandatory
conversion of commercial
property. Council will hear
this signed

4-14-98
Trustee Mtg

Mam

Trustee Compensation -
Senate has 'til Thursday to ~~hear~~ send the bill to the House.
They gutted the bill & put in "reasonable" compensati

COWORM

4-23-98
TRUSTEES MTG

Rockne

Info · 33 members inducted into NHS
· 4 more weeks of school.

Rodney
Nothing

Info Henry
LOOK FOR PROFILE
· Impressed by Tony Parish as depicted in a Profile
· written by a student.

Kekoa
Radio Ads -
Focus groups set up for getting feed back on the ads. Kekoa to come back on TUESDAY

Nam
Senate conferees on the Compensation Committee: BAKER - FUKUNAGA - CHUMBLEY - MATSUNAGA - McCARTNEY - ANDERSON

LLL 000006

5-5-98
TRUSTEE MTG

OK **Mike**
Nominee for Order of Keʻelikōlani
Pauahi — Martha Hohu

Yuki
Groundbreaking was successful
Communications did a hell of a job
given the short time frame.

Rodney
Nothing

Nathan
Executive Session

Nam
· Ed Case's "yanking the bill"
· Approval to buy a table
· for the Public School
Foundation. /

5-5-98
TRUSTEE MTGS

Benefits for Staff / KSBE & Kukui's participation in our retirement system. This includes all subs i.e. RHSCI. etc.

Agreed to discuss this in its entirety because there are a myriad of issues.

OJ - will bring to us the process they went through. "It took us 2 years."

[EXECUTIVE SESSION]

3 Issues

1. Update on an Audit
2. Long Term Commitments
3. Intermediate Sanctions

5-5-98
TRUSTEES MTG

Pule: Jerry
"FIND A PATH TO GET OUR INSTITUTION BACK on track"

Executive Session

Ed Case's Yanking of the Bill.
Heavy duty discussion
Power play in the House
(During the discussion - Oz looking at other documents - not participating

Agenda

Minutes - Aug. 23 DRAFT
Oz Stender presiding

Aug. 9 Minutes
Oz recommended that Daos live in the house rent free in exchange for services subject to legal review

5-5-98

TRUSTEES EXEC. SESSION

Trustees Approved This

Unanimous

- Valuation - do we do this? Trustees agreed to do on valuation ASAP.

- RHSCI - should do the valuation. Glenn to take the lead.

Business Purpose

To meet planned growth of KSBE Educational Programs.

Handout Page 3

Intermediate Sanctions Issue.

- Comprehensive Breefing to the Board of Trustees
- Fiduciary Handbook
- SCA Compensation Study
- Tax Compliance Workshop

LLL 000010

5-5-98
EXEC. SESSION

(Rodney) RETREAT ? in the near future.
~~to finalize~~ Nathan to finalize.
& also schedule a workshop.
Henry wants Nathan to come back to us on RICO.

Retroactive to Sept. 1995
Excessive Benefits
Disqualified Person
- Trustees
- PE's

Penalty Tax
- 25% - excessive penalty for person who did this!
- 10% - penalty on supervisors
Person must be repaid
- 200% - if not repaid

- Statue has an corrective clause
- Statue also talks about abatement.

5-14-98
TRUSTEES MTG

Rodney
June 9 - Peterson group to come back with preliminary findings

Nathan
Circulating the petition for the 112th. It has to be filed on 5-15-98

Nam
Legislature "signed + died" per Larry Price.
Governor has 45 days to ~~sign~~ take action. Sign - veto or let it become law without a signature.

Kekoa
I will work with Gil - Myron - Nathan to come up with a media release on 990's

LLL 000012

5-26-98

OPTIONS - COMPENSATION

- TAX EXEMPT vs Private Entity
  - What about TAX consequence if you do this? per Intermediate tax sanctions?
    How does this affect us.
- Plan to meet with SCA - Mark Mc~~Connaghy~~ - Mark - Bruce - outside trust lawyer.
- Advice on -
  - Do we take our full amount?
  - Can we "set aside" the amount we waive in case we need to reimburse the estate.
  - Can we

6-4-98
TRUSTEES MTG

Pule - Jerry

Minutes: approved 5/19; 5/26; 5/28

Agenda

OK 1. North Kona Lease Proposal

2. Intermediate Dormitory Renovation

Put in a bill to the courts for instructions on CIP projects.

Let's move from this town!!

Why are we getting so much negative press?

We are the only ones putting money in this town

JP – KSBEs contribution is the difference between "recession & depression."

6-4-98
TRUSTEES MTG

Approved [redacted] EXECUTIVE SESSION [redacted]

PROPOSED SUBSIDIARY REORGANIZATION PLAN

OK

De reorganization. of

3 CRITERIA

- Valid business purpose
- Valid continuity of business enterprise
- Valid " of shareholder interest

Discussion

① Did we ever consider changing the TRUST to a NON-PROFIT CORPORATION &

- Bishop Museum did this.
- * ~~Nathan will look into this and~~ NOT ~~come back to the board~~. We will form
- a non-profit in Delaware.

② Valuation

If we went through dereorganization – and it was challenged – Valuation determines how

LLL 000015

6-4-98
EXECUTIVE SESSION

much tax we should have paid in 1998.

Trustees approved going ahead with the dereorganization and valuation.

---

* Presentation by: Bruce - Nathan - Randy - Yuki - Paul and Rodney.
{ Proposed format for a Summary of KSBE Strategic Planning Activities 1993-1998

Dr. Ahr
Outline of a report (Handout)

E+Y - January 1994
- March 1994 - 1st Report
- Extensive strategic analysis stage.
- March '94 to October '94

7-23-98
EXECUTIVE SESSION

ASK A TRUST LAWYER

Colbert is a reporter to the court. The only thing that the court can see is what Colbert gives the judge. Filing under seal is false comfort. Anything filed under seal can be unsealed.

- Trustees would like to discuss this issue with Colbert on Wednesday.
These policies were ~~a~~ asked for by Matsubara.

- White Paper on Intermediate Sanctions - We will turn this over to Colbert

- Petersen Report will be filed tomorrow 7/24/98
Is this an open filing?
YES!

9-17-98
EXEC SESSION

Pat Yim - filed a petition to keep his work sealed (whatever is left)

↓ phone call from

<u>Int Sanctions</u>

$ 826888.00
74682.00
$ 901,570

~~901570~~
~~74682~~
~~826888~~

<u>Sue Templeton</u> (sp?)
The time was cut up to address:
- SAFE HARBOR
- STATE LAW FOOTNOTE
- COMPENSATION ISSUES
- Lobbying Disclosure Act — [redacted] $180,000
  6 mos -
- [redacted]

9-24-98
EXEC SESSION

14 The so called "Lead-Trustee" system has been abolished. A new estate CEO Based Management system will be instituted.

~~Responce~~
TODAY - meet w/ Kevin & Colbert

9/25/98 - 2:00pm - Meet w/ Hirai

9/29/98 - 9:00pm Responce to Kevin's filings Deadline

10/2/98 - Colbert's report - our report & Kevin's report.

10:00 AM

WANT Bruce to oppose this	Kevin - Interim removal
Wally to work on this	- Took commission on final disbursements

10-6-98
EXEC SESSION

Supplemental responses - 9-16-98

- Must have evidence in these hearings
- Int. Sanctions

Colbert thinks the whole $990,000 was used to defend trustees compensation

At a minimum we should say

a - Everything was done for other than compensation

b - only X amt was used for compensation

- Colbert wants ~~surcharges~~ placed on trustees.
- We have to prove we did not do this

Hamakua - Colbert's Issues

- Colbert is raising the issue of diversification

11-12-98
TRUSTEES MTG

Rodney - We must work w/
our secretaries.
Nov. — cut over to
new system will take
place.

NATHAN - said we will cover:
RFP for a Strategic Plan.
- Needs approval.

- Bruce has a proposal
for the Compensation
plan

- Miller & Chevalier

EXEC. SESSION

RFP -
Discussion:
Page 2 - item 3 on
diversification. This
should not include our law

LLL 000021

21

EXEC SESSION / 11-12-98 TRUSTEES MTG

Also discussed was:

- Process
- Who gets this report
- Approach & Process-paragraph 4 and Time Frame - Paragraph 9 on page 3
- Involvement of the Educational Firm.

Compensation

Federal law & state law addressing this.

Federal law prevails.

Fed Law - more specific.

#15 Stipulation Language says:

On or before 11-13-98 we must

DISQUALIFIED PERSONS

LLL 000022

EXEC SESSION 11-12-98

TIME TABLE FOR INT. SANCTIONS.
Should decide, by the middle of 1999, the rules & regs of Int. Sanctions
It is retroactive to Sept 1995.

Jan 1, 1999
• Reasonable compensation state law kicks in.
Major trust companies are taking the money they think is reasonable and be prepared to refund any of it later per the court.

• Eventually Int. Sanctions kicks in (around mid '99)
• Interim period -
Starts Jan 1, 1999.
What we have is SCA STUDY

EXEC SESSION 11-12-98

SCA Study may solve State problems but not Feds' sanction.

They repealed the schedule we used to ~~use~~ determine compensation.

Suggestion use Marketable Compensation

- Why wouldn't other trustees compensation i.e. Campbell Estate be part of "reasonableness"
- Court ordered us to have a study every 3 years re: compensation.

Federal Purposes -

Feds determine what is reasonable not state.

12-17-98

EXECUTIVE SESSION

Lokelani

Brought up two issues:

1- Judge ruled there was no attorney client privilege. Information gleaned by the AG can be used against in the interim and permanent removal.

2. Today - Randy Chang said S&P is concerned about:

- Hawaii's economy
- downturn in tourist & impact on RHSCI
- Legal action by the AG
- Legal action between trustees.

I asked Nathan if the

12-17-98

AG could remove us if the S+P rating goes down? He said yes.
I brought it up as part of my fiduciary duty.
Jerry responded about ~~to~~ how narrow the grey area is with regards to attorney client privilege so it doesn't mean the AG can use very much. He also indicated there were restrictions on what info she could use.

Re: S+P
No comment; dead silence!

12-17-98

Nathan

ok 1. Dec 16, 1998 letter to Nathan from Dickie. Subject - Mr. Cohen's Involvement in IRS Audit.

ok 2. Dec 16, 1998 - letter to Nathan from Dickie re: Colbert's duties as an agent of KSBE. Colbert had no problem. We will all abide by this - Nathan to formally notify Colbert.

ok 3. Nov. 16, 1998 To Trustees from Nathan re: KAA & KAPSF
Trustees response to AG.

12-17-98

ok 4. Dec. 16, 1998 memo to Trustees
* from Nathan
attached - Mark McConaghy's
re: meeting with Janet
Hughes in Seattle, Wa.
Proposes revocation

OK 5 Dec. 16, 1998
~~To Natha~~ TO: Dickie from
Nathan re: IRS Authorization

Dec 16, 1998
OK 6. To Trustees from Nathan
Motion for Immediate
Return of Personal Property

noted 7. Hand-Out
Peter Harris Expenses

8. Motion ~~of~~ for return ~~of~~ of KSBE's
records.

LLL 000028

12-17-98

<u>Compensation</u>.

- Stay within a range 3½ – 5½ per SCA Studies.

<u>Trustees</u> will stay with status quo.

<u>Meeting</u> – <u>Dec. 23, '98</u> 2:00 pm

LLL 000029

12-23-98

Hamakua
Concerned about how we did our due diligence

Int Sanctions
There was some element of trustee compensation - so maybe we should find out how much of this was

Trustee Compensation
- Filed in court
- BE is the biggest + best organized
- Other trusts may be looking for us to take the lead.

LLL 000030

12-23-98

- Not sure if the court is cognizant of the urgency of the situation. Feels we should have a status conference on this.

Strategic Plan
Court has to approve the R.F.P.

Mtg w/ ~~AG~~ Kevin - Colbert - Bruce to discuss

CEO Issue vs Strategic Plan

Should it be ~~[illegible]~~ postponed or should we have a CEO on an interim basis - strong management structure for an estate.

EXECUTIVE SESSION 1-14-99

Henry

- Falsifying Claims by the AG should be addressed.
  - how do we do this? can we?
  - how can you influence an election - when its pau?

Hearing set for Jan. 26th

- Trustees voted 3-2 to file the motion as recommended by Mac on campaign spending and voted 3-2 to
- file the motion to return our documents.

Chart #1

EXECUTIVE SESSION 1-14-99

Nathan

Purpose for the mtg is to update the trustees on chronology of events, etc.

- Jan 4 1999 - Rec'd 5701's. (9" thick)

Response to IRS

1. 5701 Issue
   Bates #
   Potential Dollar Impact
   Relevant IDR's
2. Conflict Analysis
3. Summary of Services Position
4. Factual Errors/Inaccuracies/Omissions in Service's Position
5. Areas where clarifications is Needed from service

EXECUTIVE SESSION 1-14-99

6 Summary of KSBE's proposed response to service

7. Brief statement of relevant law

8. Outline of Factual Support for KSBE's position

9. Proposed treatment of issue at February mtg with service.

National Office

Should not be making law - they should be interpreting law. Therefore - they are looking factual data.

District Office believes firmly that it is discrimentory to accept only someone that has Hawaiian ethnicity

EXECUTIVE SESSION 1-14-99

- Should get a better hearing before the National Office than before the District Office.

- When there's an issue - ie what is public policy - IRS would listen to what the head legal officer of the state would say re: this. The AG - weighing in - made an issue in a separate case.

- Will AG give a letter of support in this environment?

- AG's position is that beneficiaries are students, alumni & others that went to KS.

- List will be given to us by Nathan on 1-15-99

Chart #2

Chronology 1-14-99

1. Jan 4, 1999 – 5701 s, issued by IRS rec'd at KSBE

2. Jan 20, 1999 – Target date for preliminary drafts of issue analysis

3. Jan. 26 & 27, 1999 – Mtg of KSBE team to work on format sheet analysis

4. Feb 4, 1999 – Mtg in Wash DC re: Admissions Policy

5. Feb 8-12, 1999 - Individual trustees with an oral outline of the tax implications on 5701s.

6. Feb 22, 23 & 24, 1999 – KSBE Team meets to discuss analysis of 5701 s.

7. March 3, 4 & 5, 1999 - Mtg in LA with IRS

LLL 000036

EXECUTIVE SESSION 1-14-99

8. Approximiately March 22, 1999: Final draft of responses to 5701s prepared by KSBE counsel & tax consultants

9. approximiately April 1, 1999 Individual trustees submit suggestions, comments & if appropriate, supplementation to draft ... about Mar. 22, 1999

10. Approximiately April 12, 1999 — ~~individual trustees~~ (30-45 days after the mtg w/ IRS) KSBE's written response to the 5701s is due.

11. approx mid-May, 1999 - 30-60 days after IRS receipt of KSBE's written responses. IRS may issue (Revenue Agents Reports.)

12. Administrative & Judicial Avenues of Review

1-14-99

Henry
- AG had a political target & she politicized it. They changed it forever.
- attorneys want to put closure to this but the AG wants to charge us with all of the conflicts - & is looking ~~any~~ every way you can.

Jerry
How does this process impact Intermediate Sanctions?
Yes! The intermediate sanctions would come down to each individual separately. Mark thinks it would be divide by 5

Excess Compensation - affects all trustees.
Must have absolute coordination

1-14-99

Unanimioty - if it applies individually to all trustees its a common issue. If its a common issue than its an estate issue and we can take an coordinated effort instead of a individual effort.

Intermediate Sanctions is retroactive to Sept. 1995

* The service was influenced by all the articles that appeared in the newspaper. They investigated them & many of them turned out to be more fact than fiction.

1-14-99

Excess Compensation

Subsidiary Drop Downs

Do we look to our insurance carriers for relief?

What is Primary & Numbers

~~400,000~~ 400 million.

Audited Financial Statements

approved subject to Art Tokin's responding to the paragraph on the separate sheet on

(1) Internal Revenue Service Audit

(2) PHC - which is also included on Page B-27 under Subsequent Events

EXECUTIVE SESSION 1-14-99

This may take a couple of years -- this is a whole process that we have to go through.

This process - McConaghy -

AIPA -

8C

- UBIT - adjustment 70 mil
- Excess Compensation X
- Primary Purpose X
- Private Inurements X
- " Benefits X
- Admissions Policy X
- Excess Taxes
- Employee Taxes -

X= Revocation

- Is private inurment cutoff 9-95? No!
- The service has it all

Revocation - per

1-14-99

COLBERT

Colbert doesn't like this process.

→ He doesn't feel that Nathan + McConaghy would not be independent. He feels that trustees may influence Nathan/Mark. Must convince Colbert that we have enough insulation in place for Colbert to feel comfortable.

→ Problem that Colbert will talk about is that fiduciaries must be represented by another fiduciary when the existing trustees are in conflict.

→

1-14-99

If Colbert doesn't believe that you folks are not insulated enough — Colbert could look - monitor

Current orders - allow the Master to get periodic reports.

Rule 29 Colbert

Rule 42 - Exception

1-14-99

Colbert

Its not my preference to go to the court & ask for some process.

Nathan & Mark said there was a conflict of interest.

"You told me... Nathan... that you wanted to handle this ~~[illegible]~~ with your staff

You are not the fiduciary - you are not the one to be charged with the fiduciary duty

If you are not concerned about these issues - than you 5 should go to the court and should step down. It should not

1-14-99

be me, Calbert said, to take it to the court.
Henry said - just because someone says we are in conflict - are you in conflict.
~~Jerry~~ - proposed Calbert monitoring, auditing, having unfettered access to the process. Calbert didn't like the idea.

Calbert also asked why we are threatened by having alternative fiduciary trustees named & put in place.

We should go to the courts & telling the courts we should be out.
NOTE: I left at 7:30pm

1-20-99

Why should the trustees be removed ----

- Is there an actual conflict?
- Mark & Nathan declared a conflict...... on Thursday 1-14-99 -

Nathan said there is definitely a conflict; there are varying degrees of conflict as it applies to individual trustees and its global.

How did Nathan determine there is an actual conflict

1-20-99

Nathan

- Trustees are the ones to determine conflict

- Proposed sanctions of the IRS are adverse to the estate

    - Unreasonable Compensation
    - Private Inurement
    - Private Benefits
    - Primary Process
    - Admissions Policy

- Unreasonable Compensation
  Too much money. Should be 90-110,000. Chairman 2x as much.
- Private Inurement
  Inside benefits

1-20-99

• Private Benefits

Giving contracts to benefit outsiders.

• Primary Purpose

Arms Length Issues.

Trustees did not keep an arms length.

Primary Purpose

• ~~[illegible]~~

# of students served & contrast it with the amount of money earned show a Business purposes.

What is the Core argument underlying the 5701's?

Tying Threads

4-22-99
Trustees Mtg

Oz - Dickie - Loke * (Henry & Jerry recused)
EXECUTIVE SESSION
· PBOC - Conversion to State Bank Charter
· Colleen Wong - re: Board Meeting
of PBOC x

· If they convert their charter
we can still own 24.5%
but can only

Oz recommended Option 3. We all
agreed. We will go with Option
3

Rodney
3/31/99 - We stipulated
that we would have
a CEO in place.
- We filed a petition
with the court asking
for: 1)
2)
3) 90 day extension

I 4-22-99.
EXECUTIVE SESSION

- Our petition will be heard on 4-30-99
- Clock is running now.
- Rodney wants to know if he goes ahead.

Henry
Explained Holders' testimony re: Management Audit.
- Colbert Matsumoto engaged Arthur Anderson not KSBE.
- Hypothetically - Colbert could have given Arthur Anderson the direction to have a CEO Arthur Anderson would have done exactly as Colbert wanted regardless of if the institution needed a CEO or not.

4-22-99

EXECUTIVE SESSION

Meet with Bruce Graham regarding

~~Thursday~~ - Deferral of the CEO issue until the plan (the Strategic Plan) is completed.

Schwartz Coming on MONDAY - Rodney to talk to Korn Ferry re: CEO job description.

- Keaukaha School -

· Oz wants a couple of more weeks to review the items listed on page 6 of 6

Jerry & Oz & Claire team went to meet with Mr Mehieu & his staff.

Oz asked Michael to assign somebody to do this and Michael assigned Claire.

4-27-99

EXECUTIVE SESSION

Special Purpose Trustee Panel
April 17, 1999 -

Mike Hare - when they discussed ~~[illegible]~~ the admissions policy the District & National Office involved met jointly to discuss the issue. It was called a Comprehensive Global. Everyone felt this was good.

Now - we are involved with revocation of exempt status per 5701's.
We now have

5701's in final form
agents report follow
Appeals put in - ligitation

4-27-99

STANDARD PROCESS
5701's finalized
Discussions
~~Issues~~ Issuance of a Revenue Agents
Report (RAR)
- Administrative Steps
- Finals appeals step
- Litigation.

Comprehensive Global

- Removal of 5 of Us
(does not indicate
  - Differences between what
Diane & Mark are saying
  - What Carol Taylor is
writing up
- Screening & Selection of Trustees.
- KSBE all subs will be at
the table
- Governance reforms

52-A

4-27-99

- Unreasonable Compensation paid to trustees - excessive - excessiveness will stop.
- IRS - has been let to believe there is threatened or diversion of assets.

Special Panel
- Lacks authority to affect actions.
- Lacking authority - cannot comply with positions
- Will step down if they have no authority

Chevalier

Is it in the best interests of the estate to go through the Comprehensive Approach or the Standard Approach.

4-27-99
EXECUTIVE MEETING

Probate Court will have to hear this.

- This is a report not a petition

(*) Henry asked about the process for Admissions Policy
- District was going to issue a TAM
- 5701's came down in mass.
- District Office said - We were discriminatory
- We appealed to National Office.

It is clear - IRS has taken the position of the AG → and it has taken 5 years to complete the audit.

4-27-99
EXECUTIVE SESSION

They go from 5701's to final settlements without ERAR's, RAR's

They are trying to interfere with the estate - the will - the judicial process

Jerry
- I'm not sure why I have to resign - what is the basis for our resignation.
- We need a process in place to get to a resolution
- Permanent removal.... from all positions held.

4-27-9[illegible]
EXECUTIVE SES[illegible]

"Process is underway" ...
(Jerry says - this process is underway & we are going through a process.

Lohe - What about Intermediate Sanctions? How does this impact us? Why is the IRS going from

— Who was at the mtg on 4/17/97

— Was National Office there?

— Giving the restraints - get clarification or modification from the courts

— This is first the sentence then the evidence - ~~then~~ and a unsure ending

4-27-99

"I'm not going to talk to you until you resign & adhere until you agree to all 6 conditions.

What is it that supports the IRS Revocation until you do all of these things.

They have not talked about the ~~a~~ merits of the resolution — what says that the resolution is in the best interest of this estate.

Intermediate Sanctions is
· Revocation plus sanctions.
· Letter Mr. Cohen wrote – he pointed out – if

4-27-99

everytime the IRS says
we have a problem as a board
we ~~[illegible]~~ are put in CONFLICT.
IRS makes a statement
against a major trust
This is an object lesson
To be a lesson to all others.
Puts the
Special Purpose Panel Trustees
in a terrible position.

This is a fundamental due process
issue —

Darren Pai called Ron Sakamoto
& asked why all 5 should
be removed. What did the
IRS say in the document.

4-27-99
EXECUTIVE SESSION

ILS Threatened to revoke
Unless you do such & such
' what is unreasonable
compensation?
' Other particulars that
indicate wrong doing
. Stepdown because this
is what they want.

Getting to the court with
a statement about what
one or more of us think
→ Communication to the
court – we should file
something to the court.

Suggestions
' Call the panel
'
'
'
.

4-29-99
EXECUTIVE SESSION

What were you told that -
leads you to believe we
should step down.

Who was said at the mtg?
What " said in more details

We need the authority to talk
to staff & find out
what was happening

Bruce

→ Panel can give us authority
to go to the staff to
get information.

→ Mike Hare says meet with
the Panel to ask them for
information.

→ He suggests we get something
to the court ASAP -

4-27-99
EXECUTIVE SESSION

Bruce suggested:
- ~~Talked~~ Talk to ~~Kihune~~ Kihune
- Bruce — to draft a letter for the chair.

Cohen
Retained by the estate to do estate work + he may be counsel by the order
Setting him aside —
you may want to talk to other counsel

Rice vs. Cayetano
Caveat re: administration process. Nathan wants an amicus brief filed with regards to this to minimize impact.
Recommendation: Carter Phillips to file the amicus.

Chumbley
Chun
Inouye
Lenin
Matt
Sakamoto
Taniguchi
Slom
Bunda
Iwase
Ihara

4-29-99

TRUSTEES EXECUTIVE SESSION

Discussion:

1. Oz's Filing

Oz will step down if National Office will not revoke the tax exempt status & will settle all issues

2. Compensation Issue

Will accept $600,000 as a salary!

Whatever probate court sets - if he is overpaid - he will reimburse.

Recieved $300,000 for the year

Oz asked for 5701's. He got it today!!!

LLL 000063

4-29-99

EXECUTIVE SESSION

DISCUSSION: MASTERS REPORT

Same agency that had to apologize to the American people for its abusive tactics!

Same agency that accused us of discrimination .... and threatened us with revocation of tax exempt status

EXECUTIVE SESSION (4-29-99

Other problems: $\boxed{5701's}$
• Milton Holt issues
• Travel Issues
• Penalties.

Jerry
• Asking us to resign in a "blind"; we don't know why they are asking us to resign — IT'S EXTORTION!!

Henry
Right now - the burden of proof is on the IRS.

We need our day in court.

Jerry
Two things in law:
• Process and procedure
• Merits

4-28-99

OJ's filing — is an attempt at negotiation
... he will resign if etc, etc.

(*) What ~~can~~ is it the IRS can or cannot do to us under these circumstances

Question (A)

Possibility — Verner Liipfert
(1) go to the IRS - ASAP and go to the General Counsel of the IRS so we can get some information re: this

(2) If Verner-Liipfert is conflicted out — then they go to a tax firm that is reputable & ~~have~~ has access to the General Counsel of IRS & do this above

4-29-99

Re:
Also - did or does the power shift to the panel or does it stay with ~~xxx~~ the incumbent trustees.

Op.
"This is ~~the~~ a legitimate tax expense.

Dickie
Have McCarriston take the lead with this as our local representative to coordinate this with the tax experts, etc.
Jerry said this is more important than any other things. So he agrees with McCarriston doing this.

4-29-99

McCarriston - look at whether ~~or~~ not the special panel, per the order, is liable if they make the wrong decisions

Ques B

McCarriston - Look at compensation issue.

Agreed to all of the above & to send ~~[illegible]~~ someone to the IRS ASAP.

Oz said - he has differences w/ McCarriston on his (Oz's) own pleadings However - he has no problems w/ ~~the~~ McCarristons

4-29-99

handling this issue

- Op also feels that there should be no problem with a conflict by Werner Liepfest.
- Jerry

This board needs information on the process!

Dass C — It makes a big difference on whether they can ~~to~~ pull the revocation "tomorrow" or does it take 6 months? ~~Is~~ Is there some other process they must to do this? What is the process

NOTE:

Calhert was not at the April 19, 1999.

- Calhert left out the preliminaries that caused

4-29-99

the ~~IRS~~ to say it "has suspended communication with us".

"Conflict Issue may have to be looked at ..."

Jerry
Was Carroll Taylor at the meeting with the IRS?
NO. So the information from ~~the~~ Calbert & Carroll Taylor ~~the~~ was second hand.

Trustees decided:
• Bruce Graham & McCarriston will work with each other to ~~prep~~ prepare the document to file

4-29-99

BRUCE GRAHAM

Colbert recommends:

(1) Recommends that the court cause to be issued and served upon each Trustee to show cause.

(2) Order the hearing to be held before May 10, 1999

The Judge has already done the #1 & #2 above.

Colbert ~~states~~ ~~regurgitates~~ regurgitates the Panels report.

Bruce's dilemmas —
He has attended some of the Panel's meetings & will have a hard time writing a report if he cannot put on paper

4-29-99

Bruce - continued
what he knows and/or discussed with the panel.

Deadline to file.
9:00 Am
Tuesday morning.

On Tuesday - we must present to the court
+ evidence that the tax status is not in jeopardy because we didn't do any thing OR The IRS cannot require resignation.

* Two Questions
Can the IRS do this?
Do they have the power?
Under what circumstances?

EXECUTIVE SESSION 4-29-99

The IRS may be wound up because Brewster was.

Need to get into a process.

* If we don't resign or get removed bef the 10th — is it fatal?

* Do you belong in Fed court or state court?
If in Fed court can we get a restraining order.
Carroll did not file the document "under seal"

Estate damaged because the attorney for the special panel did not seal the report properly.

4-30-99

+ The I.R.S. wants to be the trustees of the Bishop Estate. The master wants to be the

+ Get someone in the Senate to say - we wanted to get ~~rid of her~~ reduce the compensation so the trustees cannot

+ Get someone to take this ~~of~~ to describe this as a ~~a~~ "one" Hawaiian institution vs the greedy - political - merchant street.

+ Get savvy tax people ~~so we~~ dont hand

4-30-99

Someone ~~otet~~ ought to sit down & say - The IRS wanted a part of our 9.S. monies.
- The KAA was appr

Change the character of the

① Bronster is an inquisition
She went beyond the pale
She was rejected by the 9th certificate.
" " " " "
Senate.

② Attack by a bunch of people to dismantle the one unique Hawaiian Trust.

Get 5%

(3) Start an investigation by the Senate to bring in her communication with the IRS
- She helped the IRS to ~~go~~ do her dirty work & caused judge to appoint a panel -

(4) ~~Show~~ that IRS is mad because of KAA
This is what the IRS is after
~~The want to tax the QS investigated~~

~~Make~~ She's burning us in the middle of the school & doesn't care about the school

Get key Senators to
tell them they are going
to use the poor ~~using~~
Hawi'n people by ~~making~~
a unique Hawi'n institution
as the example for the
heavy handedness of
the Ort Sanctions

Savannah Ralla

LLL 000077

5-4-99
TRUSTEES MTG

Pule: Oz

Agenda

1. New Swimming Pool Position
WITHDRAWN

2. Lease - 6.5 acres for Coffee Cultivation in Keei South Kona

3. Gold Bond Bldg
Rent Renegotiation at 130.00 per sq. ft

4. New lease to Kaiser at Hawaii Kai
$2.40 a sq. ft.

5. Issuance of a New Lease to Shimizu dba All About Me
Newtown Square -

LLL 000078

73

5-4-99

6. Lease to BBJ dba Patty's & Ray-Z General Store.

Randy
Historic Foundation
Mothey Lindsey to give the Opening Remarks.

Mike
Yuki } nothing
Rodney

Alika - sine die

Kekoa
Goldman - starting at $53.00 a share → $73.00
$477,000

Charles Reed Bishop Trust 5-4-99

EXECUTIVE SESSION

Charles Reed Bishop Trust

1. 0% to 5% per yr.
2. Indicate expenses & contributions of $850,000 or 6.6% spending rate
   $500,000 Bishop Museum
   250,000 ~~Maunaal~~ Maunaala.
3. Long term maintenance plan

4. Note: the museum staff will in various programs, provide these services & others for KS ~~the~~ students

Action Needed #1 — Reword/define #1 better.

#6 - Talk to Bruce Graham - re: Plug this into the Master acting or go to the court separately.

5-4-99

Charles Reed Trust - cont)

#5. Exhibit B - proposal of use of funds & addressed other items re: the trust

#6 Preserve a balance of 5.6 mil instead of $500,000 per the Will of CR Bishop because the endowment has grown to 10 mil.

<u>Minutes</u>

Adopted minutes of Feb 9, 1999 Mar. 2, 1999 & March 11, 1999

Concern raised re: should we waive our Commissions.

5-4-99

KSBE
EXECUTIVE SESSION

- Policy re: residential life tenancies.
- Trustees approved the recommendation that the trustees not approve a life tenancy policy based on the age of lessees.

Governance

- Internal Auditor
  Trustees approved the beginning of a search for an internal auditor — EXPEDITE
- External Auditor

5-4-99

EXECUTIVE SESSION

Q "Its too bad we are going through all of this - but the IRS is going to do this to us.
They are going to take us out on:
- Excessive Compensation
-

Henry
Its good that we earn commissions and not a ~~sa~~ salary.

None of this is fair - they keep on doing it to us.

5-5-99

12 Noon - any affadavits

- IRS Threat is the real ballgame.

- If the judge finds Imminent Danger to the estate.

1. EXCESSIVE compensation

2. Does what the panel reported add up to imminent threat of harm?

Judge has to be persuaded that

Can the IRS do this? Can they do it? Do they have the power to do it?

If they have the power
~~Carry they~~?

Would they really sink
the estate & damage
the estate

Successful fight - plays
into imminent harm.

IRS has not said if
the trustees go - the
estate is safe.

If these trustees go - your
TAX EXEMPT STATUS IS
SAFE.
They said - we don't want
to talk to these trustees
so make them go away.

5-6-99

EXECUTIVE SESSION

OK ① Request authority to buy back the leased-fee in subject residential property at a foreclosure auction on May 26, 1999.

OK ② Gwinnett Center
Sale of 99 acres plus
NOTE: We do not own Gwinnett but ~~have~~ are the lender.

OK ③ CEO Issue
• I brought up GIL TAM
Ideally we all want to go through the process – But the court refused to grant us an extension of time – 90 days – last Friday – per Judge Chang.

5-6-99

EXECUTIVE SESSION

On Tuesday we decided on an ~~The~~ alternative process was to go to the courts yesterday 5-5-99 & ask for two weeks to pick someone. This could not be done because it was not the ~~platform~~ arena for this request. It was a Status Conference.

Therefore - since we ~~were~~ are not in compliance - it was agreed 4-1 to be in compliance prior to the court date 5-7-99

Gil Tam was always considered as a possible candidate

He knows KSBE

Worked w/ us before

5-6-99

EXECUTIVE SESSION

Competent in strategic planning.

He would be an interim CEO until such time as the strategic plan was completed.

At that time - we would go through the RFP/Korn Ferry route to select a permanent CEO.

Salary - $300,000 per yr.

NO percentages

NO golden parachute

He would get all the normal benefits other ~~employees~~ principal executives get.

Vote 4-1 in

Tuesday, Feb. 17, 1998

To: Honorable Brian Y. Yamane, Vice Chair
House Judiciary Committee
State of Hawai'i

From: LeRoy K. Akamine
3469 Kahawalu Drive
Honolulu, Hawai'i 96817

Re: Support of HB. NO. 2362, 2587 & 3007
Relating To Charitable Trusts

I am in support of any measure that would seek to adjust the compensation of trustees of an estate of a charitable trust if such adjustments shall result in compensation paid to said trustees not to be excessive.

I am especially supportive of the provisions in HB No. 2587 and 3007 that disallows income from the sale of the fee interest under any leasehold property or on income received from lessees for payment of real property taxes on leasehold property.

These measures to adjust or cap trustees compensation will increase the amount of trust income available to serve the beneficiaries of a charitable trust, such as the Kamehameha Schools Bishop Estate.

Mahalo,
LeRoy K. Akamine

LeRoy K. Akamine
Graduate Kamehameha Schools
(R) 595-49464

Deposition Exhibit No. 134
Deposition of Lindsey
Date 12-4-99

LLL 000089

KAMEHAMEHA SCHOOLS BERNICE PAUAHI BISHOP ESTATE

April 9, 1998

The Honorable Avery B. Chumbley, Co-Chair
The Honorable Matthew M. Matsunaga, Co-Chair
and Members of the Committee on Judiciary

The Honorable Rosalyn H. Baker, Co-Chair
The Honorable Carol Fukunaga, Co-Chair
and Members of the Committee on Ways and Means

Hawaii State Capitol Room 211
415 South Beretania Street
Honolulu, Hawai'i 96813

Re. H.B. No. 2362, Proposed Senate Draft 1 Relating to Charitable Trusts

Dear Chairpersons and Committee Members:

H.B. No. 2362, Proposed S.D. 1, Relating to Charitable Trusts, addresses the issue of trustee compensation for charitable trusts. The issue of trustee compensation is a highly complex one and extremely controversial when it deals with the commissions of a singular trust --- a private, self-sustaining, Hawaiian Ali'i trust.

Kamehameha Schools Bishop Estate (KSBE) requires no government funds to run its schools for Hawaiian children. In fact, last year alone, KSBE spent more than $120 million on its educational mission. That's $120 million the State of Hawai'i did not have to spend on education.

The five-member board of trustees established under the Will of Ke Ali'i Pauahi Bishop is governed by its provisions and receives a commission based on a formula established by law. In the early 1990's, based on a court order, the first of a series of studies on KSBE's trustee compensation was conducted by three nationally-renowned compensation firms. While each firm used a different approach, all three concluded that KSBE's trustee commissions were well within the range of compensation using national comparables.

567 SOUTH KING STREET HONOLULU, HAWAI'I 96813 TELEPHONE (808) 523-6200 FAX (808) 523-6365

It is also interesting to note that these studies show that of the states ~~that~~ statutorily address trustee compensation, the overwhelming majority -- 80% -- ~~do~~ not discriminate between charitable and non-charitable trusts. Trustees in these states are treated evenly, equally and fairly under the law.

In testimony presented before the House Judiciary Committee on H.B. No. 2362, Relating to Charitable Trusts, Mr. Gary Hourihan, Chairman and CEO of Strategic Compensation Associates stated:

> "It is my strong professional opinion that any legislation pertaining to the compensation of the Trustees of Kamehameha Schools Bishop Estate (KSBE) must take into consideration the unique aspects of KSBE compared to other charitable trusts. Specifically:
>
> - KSBE is self-funding and does not rely on charitable contributions to sustain its operations
> - KSBE encompasses both a major operating entity (Kamehameha Schools) and an extremely large investment portfolio. In contrast, the vast majority of other foundations and trusts are significantly smaller and do not have a separate operating arm. Also, in those limited cases where a separate operating entity exists, it typically is managed by a different board or trustee group
> - Unlike the typical foundation or trust, the KSBE Trustees take a proactive role in investment decisions as opposed to merely monitoring the performance of professional money managers. Moreover, the fact that most of KSBE's investments are in real estate adds a further layer of complexity.
> - KSBE is subject to a much higher level of public scrutiny than the typical foundation or trust.
>
> In my professional opinion, reasonable counterparts to the role of the Trustees exist in both the public and private sectors. These include the senior managers and directors of organizations that combine investment management and operating responsibility, such as real estate developers and real estate-oriented banks. It also includes the investment and administrative arms of selected educational institutions, such as Princeton, Harvard, Duke, Texas, and Stanford, where the endowment is large and proactively managed.

Testimony re: H.B. 2362, S.D.1
April 9, 1998
Page 3

> The KSBE Trustees have taken the appropriate and rational step of maintaining their compensation within reasonable limits supported by a thorough and professional analysis of the amount typically earned by those with comparable responsibilities..." (Submitted February 17, 1998 to the House Judiciary Committee).

It seems clear that to determine what is fair requires an understanding of the complex compensation and legal issues involved to be conducted in an environment free from the emotionally-charged, politically motivated and media-hyped climate which currently exists.

Thank you for this opportunity to comment on H.B. 2362, S.D. 1.

Sincerely,

Henry H. Peters
Treasurer
Board of Trustees

STAND. COM. REP. NO. 3258

Honolulu, Hawaii

APR 09, 1998

RE: H.B. No. 2362
H.D. 1
S.D. 1

Honorable Norman Mizuguchi
President of the Senate
Nineteenth State Legislature
Regular Session of 1998
State of Hawaii

Sir:

Your Committees on Judiciary and Ways and Means, to which was referred H.B. No. 2362, H.D. 1, entitled:

"A BILL FOR AN ACT RELATING TO CHARITABLE TRUSTS,"

beg leave to report as follows:

The purpose of this bill, as received by your Committees, is to create a task force to study compensation for trustees of charitable trust.

Your Committees find that charitable trusts are established to benefit the public at-large, and, therefore, government oversight is appropriate with regard to monitoring their operations to ensure they are financially and institutionally sound. As such, there are a limited number of charitable trusts in which a broad sector of Hawaii's population has an interest as either a beneficiary or as a relative of a beneficiary. Therefore, your Committees agree that there is a compelling state interest to ensure that these charitable trusts are being managed in the beneficiaries' best interests.

Your Committees further find that as policy-makers, the Legislature needs to balance its responsibility between protecting the public interest and not unduly restricting the operations of a charitable trust. In this regard, your Committees note that the federal government provides some direction about trustees' compensation through the federal Intermediate Sanctions Law. Through this law, the Internal

Revenue Service has established regulations to determine reasonableness of trustee compensation.

Upon further consideration, your Committees have amended this measure by deleting its substance and inserting the provisions of S.B. 3037 S.D.1, which was previously passed out by your Committee. This measure repeals the existing statutory schedule for trustee commissions, and inserts language that trustee-compensation should be limited to an amount that is reasonable under the circumstances. This measure further adds a provision that this Act shall apply to both existing and new trusts, provided that any provision in existing trust agreements regarding trustee compensation shall supersede this Act.

As affirmed by the records of votes of the members of your Committees on Judiciary and Ways and Means that are attached to this report, your Committees are in accord with the intent and purpose of H.B. No. 2362, H.D. 1, as amended herein, and recommend that it pass Second Reading in the form attached hereto as H.B. No. 2362, H.D. 1, S.D. 1, and be placed on the calendar for Third Reading.

Respectfully submitted on behalf of the members of the Committees on Judiciary and Ways and Means,

Rosalyn H Baker
ROSALYN BAKER, Co-Chair

Avery B Chumbley
AVERY B. CHUMBLEY, Co-Chair

Carol Fukunaga
CAROL FUKUNAGA, Co-Chair

Matt Matsunaga
MATT MATSUNAGA, Co-Chair

The Senate
Nineteenth Legislature
State of Hawaii

Record of Votes of the Committee on Judiciary

Measure:	Committee Referral:	Date:
HB 2362 HD1	JDC/WAM	April 9, 1998

☐ The committee is reconsidering its previous decision on this measure.

The Recommendation is to:

☐ Pass, unamended ☑ Pass, with amendments
☐ Hold ☐ Recommit
☐ Advise and Consent ☐ Not Advise and Consent
☐ Advise and Consent with Exception

Code	Members	Ayes	Ayes(WR)	Nays	Excused
104	CHUMBLEY, Avery (C)	✓			
115	MATSUNAGA, Matt (C)	✓			
103	BUNDA, Robert	✓			
110	IHARA, Les, Jr.				✓
117	MCCARTNEY, Mike	✓			
119	SAKAMOTO, Norman				✓
101	ANDERSON, Whitney				✓
	TOTAL	4	0	0	3

Recommendation: ☑ Adopted ☐ Not Adopted

Chair's or Designee's Signature:
Matt Matsunaga

Distribution:
Original - Committee Yellow - Clerk's Office Pink - Drafting Agency

LLL 000095

The Senate
Nineteenth Legislature
State of Hawaii

Record of Votes of the Committee on Ways and Means

Measure:	Committee Referral:	Date:
HB 2362 HD1	JDC / WAM	4-9-98

☐ The committee is reconsidering its previous decision on this measure.

The Recommendation is to:

- ☐ Pass, unamended
- ☑ Pass, with amendments
- ☐ Hold
- ☐ Recommit
- ☐ Advise and Consent
- ☐ Not Advise and Consent
- ☐ Advise and Consent with Exception

Code	Members	Ayes	Ayes(WR)	Nays	Excused
102	BAKER, Rosalyn H. (C)	✓			
107	FUKUNAGA, Carol (C)	✓			
105	CHUN OAKLAND, Suzanne	✓			
106	FERNANDES SALLING, Lehua	✓			
109	IGE, Marshall	✓			
110	IHARA, Les, Jr.				✓
111	IWASE, Randy	✓			
113	KAWAMOTO, Cal	✓			
114	LEVIN, Andrew	✓			
117	MCCARTNEY, Mike				✓
122	TAM, Rod				✓
124	TANIGUCHI, Brian	✓			
101	ANDERSON, Whitney				✓
	TOTAL	9			4

Recommendation: ☑ Adopted ☐ Not Adopted

Chair's or Designee's Signature: Carol Fukunaga

Distribution:
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LLL 000096

HOUSE OF REPRESENTATIVES
NINETEENTH LEGISLATURE, 1998
STATE OF HAWAII

H.B. NO. 2362 H.D. 1 S.D. 1

A BILL FOR AN ACT

RELATING TO CHARITABLE TRUSTS.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:

SECTION 1. 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.

SECTION 2. Section 607-20, Hawaii Revised Statutes, is amended to read as follows:

"**§607-20 Charitable trusts, special provision.** (a) Notwithstanding any other provisions, in the case of [an estate of] a charitable trust, the [commissions] compensation of the trustees shall be limited to [the following schedule of percentages on all moneys received in the nature of revenue or income of the estate, such as rents, interests, and general profits: ten per cent on the first $1,000; seven per cent on the next $4,000; five per cent on the next $100,000; three per cent on the next $100,000; and two per cent on all over $205,000. This schedule of percentages shall be applied not oftener than once a year. The trustees shall also be entitled to just and reasonable allowances for bookkeeping, clerical, and special services and expenses incidental thereto.] an amount that is reasonable under the circumstances.

(b) This section shall apply [as well to future accounting in existing estates as to new estates.] to existing and new charitable trusts established after the effective date of this Act; provided that any provisions in existing trust agreements regarding trustees compensation shall supersede this section."

SECTION 3. Statutory material to be repealed is bracketed. New statutory material is underscored.

SECTION 4. This Act shall take effect on January 1, 1999.

REPORT TITLE:
Charitable trusts.

DESCRIPTION:
Establishes reasonable standard of compensation for trustees of charitable trusts. (SD1)

file

HOUSE OF REPRESENTATIVES

STATE OF HAWAII
STATE CAPITOL
HONOLULU, HAWAII 96813

RECEIVED MAY 0 4 1998

MEMORANDUM

TO: Majority Leader Okamura

FROM: Rep. Case Ed Case

DATE: May 5, 1998

RE: HB 2362 HD1 SD1 (Charitable Trustee Compensation): Agreement to Senate Draft

At the appropriate point today, I and other colleagues will offer motions, the effect of which is to obtain House agreement to the Senate's amendments to the above bill and final passage of the bill. This memo is to explain this effort to you and our colleagues, to obtain your confirmation of the appropriate motions and timing, and to request your support.

As you know, charitable trustee compensation has been a major controversy for many years, but especially over the last year. In short, compensation of charitable trustees is currently established according to a set statutory percentage of gross revenues (HRS 607-20); there is no Probate Court discretion to adjust compensation up or down to reflect general trustee compensation standards or specific trust or trustee performance.

At the House hearing on this bill, the testimony confirmed that the Probate Court, in comparable circumstances, applies a "reasonable compensation" standard which essentially reflects these discretionary factors. A diverse group of testifiers, including a Bishop Estate trustee, the Estate's national compensation expert, the Attorney General's office, and representatives of beneficiary groups, agreed that this approach was appropriate for charitable trustee compensation. Nonetheless, the House proposed to "study" this issue.

The Senate version (copy of SD1 attached) alters the statutory compensation payable to charitable trustees to an amount that is "reasonable under the circumstances." Under general trust law and procedure, the actual amount would be approved by the Probate Court upon application by the trustees with input from other parties with legal standing. The general standards to be applied are familiar aspects of trust law, and could result in highly compensated trustees if justified and approved.

This approach is supported by the Governor and Attorney General in addition to beneficiary groups including Na Pua a Ke Ali'i Pauahi. The "Broken Trust" authors have also made the points (see attached) that "reasonable compensation" is already required by the common law of trusts, the federal intermediate sanctions law, and tax law in related areas.

There is, in fact, nothing left to study and we should get this inevitable result over with. I therefore again ask you to confirm the necessary procedures for bringing this issue to a floor vote today, and I ask for our colleagues' support.

Thank you.

cc: House Colleagues

April 29, 1998

To: All Interested Parties
From: Broken Trust authors
Re: Legislation Regarding the Compensation of Trustees of Charitable Trusts

Summary of our position. We believe that compensation of trustees of charitable trusts should be set at amounts that are "reasonable under the circumstances." However, we recognize the concern of others that the absence of a specific cap might set the stage for costly litigation each year to determine what is reasonable. In an attempt to address this concern, we suggest the following:

Absent a contrary provision in the governing document, trustees of charitable trusts will set the level of their own compensation. However, compensation paid to any particular trustee must always be reasonable under the circumstances, and compensation higher than the salary of the Chief Justice of the Hawaii Supreme Court must be approved by the probate court, using this same standard. In situations where compensation is set by the probate court, the trustees will be able to participate in any related hearing, or even appeal the court's order, but only at their own expense.

As a practical matter, this approach ensures that the compensation of Bishop Estate trustees always will be set by the probate court rather than by a statutory formula or by the trustees themselves. Our expectation is that the court will retain an expert on compensation planning to advise it. Presumably, the court also will schedule a hearing and give the trustees, AG and perhaps other interested parties an opportunity to make suggestions, but it will be the court that makes the determination. It shouldn't take much time or be inordinately expensive. The trustees will have standing, but because their interests and those of the beneficiaries will be in conflict on this issue, it only makes sense to require them to spend their own money when arguing for higher compensation. This is similar to what happens now when an interested party questions the reasonableness of compensation paid to the personal representative of a decedent's estate. In order for the court's finding to be reversed, the trustees would have to convince the appellate court that the probate court was "clearly erroneous." This would be difficult in any event, but virtually impossible when the probate court bases its decision on input from an outside expert.

The rest of this memo consists of background information and possible language for use in the statute and legislative history.

Reasonable compensation already is required by the common law of trusts. The common law of trusts has for centuries prohibited trustees from paying themselves more than reasonable compensation. Even in a state like Hawaii that has a statutory formula which sets a maximum, trustees still must limit their compensation to a reasonable amount. Consider, for example, this quote from comment b of the Restatement of Trusts, Section 242: "In some states

LLL 000102

the statutes provide that the trustee shall receive not more than certain fixed percentages, in which case the trustee is entitled to such compensation as the court deems just and reasonable, not exceeding the statutory percentages." "Just and reasonable" is another way of saying reasonable under the circumstances.

It also is clear that reasonableness under the law is based not only on the nature of the job itself, but on the market value of the services of the individual whose compensation is in question. In other words, the fact that people hired to manage $10 billion of assets might routinely be paid a million dollars or more in compensation, doesn't mean that a million dollars is reasonable compensation regardless of the credentials and performance of the individual whose compensation is in question. It is neither just nor reasonable to pay a level of compensation based on the credentials and performance of persons other than the individual actually receiving the compensation.

The same Restatement comment notes that "in many states there is no statutory provision with reference to compensation of trustees. In such states the trustee is entitled to receive the fair value of his services, and the amount of the compensation and the time or times at which the trustees is entitled to receive it are subject to allowance or approval by the court." In other words, many states already rely solely on the common law in this area and it envisions court involvement.

That comment goes on to describe guidelines for determining a reasonable amount: "Among the circumstances to be considered in determining the amount of compensation are (1) the amount and character of the trust property, (2) the extent of the risk and responsibility of the trustee, (3) the character of the services rendered by the trustee, (4) the degree of difficulty in administering the trust, (5) the skill and success of the trustee in administering the trust, and (6) the statutory rates of compensation for executors and administrators." Again, we see that reasonableness is based on more than just the job itself. Credentials and performance are important factors in determining what is reasonable. Also, the common law assumes a link between the rules for determining compensation of fiduciaries. You'll recall that in Hawaii, the statutory rate of compensation for executors and administrators is whatever is reasonable under the circumstances.

Comment c of Restatement 242 talks about trustees of trusts that involve business activity. Again, it limits compensation to amounts that are reasonable under the circumstances: "In the absence of a statute providing a definite rule fixing the amount of (such a) trustee's compensation, he is entitled to the fair value of his services in carrying on the business." Fair value generally is considered synonymous with reasonable under the circumstances. (Recall that Hawaii's current law does not fix the amount of compensation, it merely establishes a maximum.)

Comment l of the same Restatement indicates that co-trustees ordinarily are entitled to the same amount of compensation, "unless one has rendered greater services than the other or others, in which case the compensation will be divided among them in accordance with the relative value of their services as determined by the court." In other words, the compensation must be related to the relative value of each trustee's services.

It's worth noting that the Restatement envisions active court involvement in the determination or approval of what's reasonable.

Reasonable compensation is required under federal intermediate sanctions law. This relatively new law (July, 1996) provides for sanctions that can be imposed by the IRS on trustees of charitable trusts (among others) who receive "excess benefits." While the legislative history makes clear that "an individual need not accept reduced compensation merely because he or she renders services to a tax-exempt organization, as opposed to a taxable, organization," it clearly includes in the definition of excess benefit, any compensation (direct or indirect) that is in excess of what would be reasonable under the circumstances.

As stated in Hopkins and Tesdahl's Intermediate Sanctions: Curbing Nonprofit Abuse, "The process for determining reasonable compensation is much like that for appraising an item of property: it is an evaluation and application of generally recognized factors that have a bearing on computation of value. It is an exercise of comparing a mix of variables that also pertains to the compensation of others."

The Treasury Department has not yet issued regulations for the intermediate sanctions law, but extensive legislative history does exist and is expected to form the backbone of the regulations. This history stresses "appropriate data as to comparability" are to be assessed, and that these data include factors such as "written offers from similar institutions competing for the services of the individual involved." In other words, while amounts paid to people hired to do similar jobs is a relevant factor, the determination of reasonableness requires a close look at the value of each specific individual's services.

In an attempt to lessen the amount of uncertainty over what is or isn't reasonable under any particular set of circumstances, the legislative history of intermediate sanctions law includes a rebuttable presumption as to reasonableness, which is itself a criterion for determining whether compensation is excessive. In a nutshell, it involves approval of the compensation by an independent party not under the control of the individuals whose compensation is under question. We see some similarity between this and our suggested approach of having the probate court appoint an outside expert to help it determine what is reasonable under the circumstances.

Reasonable compensation is required by tax law in related areas. For more than 80 years, the tax law has allowed a deduction to businesses for compensation paid to employees only up to amounts that are "reasonable."

Because reasonableness varies with the circumstances and is a question of fact rather than law, it will surprise no one to hear that many cases have been litigated over these 80 plus years.

However, the number of cases has declined, in part due to established guidelines which include factors such as what comparable organizations would be willing to pay in compensation to that same individual. This determination, of course, is best made by a compensation expert familiar with the credentials and performance of the person whose compensation is being reviewed, as well as the nature of the job held by that individual and "the market" for such services.

It makes sense to involve the probate court and use the reasonableness standard. As noted above, the common law of trusts has for centuries involved the probate court in the determination or approval of trustee compensation. For reasons unknown to us, the probate court in Hawaii has not taken the initiative to closely scrutinize the level of compensation paid to trustees of charitable trusts, and for equally unknown reasons, the state Attorney General has never asked the court to do so. The approach we are suggesting would give charities the freedom to set their own level of compensation at a relatively high level (the amount of the Chief Justice's salary) without the court necessarily getting involved. It also would allow for a greater level of compensation as long as the court found it to be reasonable under the circumstances. In such cases, the court's determination could reflect the assistance of an outside expert and not involve the time and expense inherent in an adversarial proceeding. Of course, the trustees or the AG could appeal the court's determination, but an appellate court would have to affirm the lower court's finding unless it was "clearly erroneous." The reasonableness standard and the guidelines almost certain to be utilized by the outside expert would be very similar, if not identical, to those provided for by trust case law under the common law and tax case law under the internal revenue code, including the legislative history of intermediate sanctions law.

Possible language for the statute: "Notwithstanding any other provisions, and except as expressly provided by the governing document, in the case of a charitable trust, the compensation of each trustee shall be limited to an amount that is reasonable under the circumstances, and shall not exceed the salary of the Chief Justice of the Hawaii Supreme Court unless a court with original jurisdiction over probate matters specifically determines such higher amount to be reasonable under the circumstances."

Possible legislative history: "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 or even limited by statutory formula to an amount that might bear little or no relationship to the fair value of their services. Trustees who do receive compensation from a charitable trust already have a common law fiduciary duty to make sure such compensation is not in excess of what is reasonable under the circumstances. Such circumstances include, for example, not just the job description but also the credentials and performance of that particular trustee. Compensation to a trustee of a charitable trust cannot exceed what that particular trustee's services are worth in the local market. In addition to this common law duty, trustees of charitable trusts are subject to penalty under federal intermediate sanctions law if they allow their compensation to exceed what is reasonable under the circumstances. Since the common law and federal intermediate sanctions law require that trustees limit their compensation to amounts that are reasonable, the statutory law of Hawaii should be consistent. In cases where trustees determine reasonable compensation to be no higher than the salary of the Chief Justice of the Hawaii Supreme Court, amounts set by the trustees will be presumed reasonable and may be paid without court involvement, unless challenged by the state Attorney General. In all other cases, compensation set by anyone other than the probate court shall be presumed unreasonable. In instances where one or more trustees of a charitable trust fail to set compensation at or below the salary of the Chief Justice, compensation shall be set by the probate court. It is anticipated that the court will determine reasonable compensation for any particular trustee only after having sought input from an independent compensation expert who will be selected by and report directly to the court, but whose fee will be paid by the charitable trust. In such cases, because the personal interests of the trustees may be in conflict with those of trust beneficiaries, the cost of any effort on behalf of the trustees to influence the court or appeal its decision must be borne by the trustees and not the trust. The Attorney General, whose job is to protect the interests of the beneficiaries, will be entitled to reimbursement from the trust for any costs incurred in representing those interests. Thus, the purposes of this bill are to codify the duty of trustees not to accept compensation above what is reasonable under the circumstances; provide that reasonable compensation generally will be set by the trustees; and determine the level beyond which compensation must be set, if at all, by the probate court rather than affected trustees."

HOUSE OF REPRESENTATIVES
NINETEENTH LEGISLATURE, 1998
STATE OF HAWAII

H.B. NO. 2362 H.D. 1 S.D. 1

A BILL FOR AN ACT

RELATING TO CHARITABLE TRUSTS.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:

SECTION 1. 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.

SECTION 2. Section 607-20, Hawaii Revised Statutes, is amended to read as follows:

"§607-20 **Charitable trusts, special provision.** (a) Notwithstanding any other provisions, in the case of [an estate of] a charitable trust, the [commissions] compensation of the trustees shall be limited to [the following schedule of percentages on all moneys received in the nature of revenue or income of the estate, such as rents, interests, and general profits: ten per cent on the first $1,000; seven per cent on the next $4,000; five per cent on the next $100,000; three per cent on the next $100,000; and two per cent on all over $205,000. This schedule of percentages shall be applied not oftener than once a year. The trustees shall also be entitled to just and reasonable allowances for bookkeeping, clerical, and special services and expenses incidental thereto.] an amount that is reasonable under the circumstances.

(b) This section shall apply [as well to future accounting in existing estates as to new estates.] to existing and new charitable trusts established after the effective date of this Act; provided that any provisions in existing trust agreements regarding trustees compensation shall supersede this section."

SECTION 3. Statutory material to be repealed is bracketed. New statutory material is underscored.

SECTION 4. This Act shall take effect on January 1, 1999.

REPORT TITLE:
Charitable trusts.

DESCRIPTION:
Establishes reasonable standard of compensation for trustees of charitable trusts. (SD1)

HB2362 SD1

LLL 000110

Testimony

To: Brian Yamane/FAX: 586-8519
Chairman, pro tem, Judiciary Committee
House of Representatives

Re: House Bills 2362, 2587 and 3007
Relating to Charitable Trust

The widespread urgency felt by the entire community of both Hawaiians and non-Hawaiians on the subject of excessive trustee commissions paid to trustees of some charitable trusts is clearly demonstrated by the introduction of not one but four different bills introduced in the house, three of which are being heard tonight.

It is the excessive commission's of some charitable trusts which have created a large part of the current controversy. Much of the controversy will be remedied when individuals no longer seek trusteeships of charitable trusts for monetary gain but will do so out of respect and dedication for the institution and for the honor of serving the high purpose of the charitable trust.

I would prefer that trustees of charitable trusts serve without compensation. Harvard University which is a multi-billion dollar trust comparable or larger than our Bishop Estate Trust, seeks and gets the finest individuals to serve on their Harvard board of trustees completely pro bono. Those trustees serve as policy makers and they hire the

LLL 000111

very best CEOs to handle the direct administration of Harvard and its investment of assets.

The current statute which is the subject of all 3 bills, TRS 607-20 does not require any payment to trustees of charitable trusts. It merely sets a maximum or limit on compensation trustees can request the Probate Trust to authorize.

The problem today is that for generations, trustees ask the court for the highest commissions allowable under the law, not necessarily because its reasonable or justified, but simply because its allowable. And remarkably, the courts have granted the maximum. The courts have never asked for justification, but has merely asked for a written description of the methodology used to calculate the commissions.

If the commissions were not so "available", perhaps trustees would not fight so vigorously every reasonable effort to find and identify the truth.

However, a cap would clearly mean that political manipulations for lucrative trusteeships of wealthy charitable trusts would largely subside.

Trustees would be selected on the basis of their qualifications and not on the basis of their political connections.

Trustee policy-making could then focus on education or some other identifiable charitable purpose while competent and qualified CEOs would carryout the trustees' policies, manage the growth and quality of the institution and manage the trustees assets for maximum stability, return and perpetuity.

In part, we favor H.B. 3007 because it offers a realistic solution for all charitable trusts.

In part, we also favor H.B. 2362 because it would require trustees of the richest and poorest trusts to come to the court on equal footing and present their full rationale for reasonable commissions justifyably earned. (It also might permit trustees to ask the court for even higher commissions than they have in the past.)

In short, the bills, if properly combined, may offer the best solution for the trustee compensation issue.

Mahalo for your attention and the opportunity to address you.

Beadie Kanahele Dawson

File

HB NO. 2362, HD1, SD1 RELATING TO CHARITABLE TRUSTS

SENATE CONFERENCE VERSION:

607-20 Charitable trusts, special provision. (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 trustees compensation shall supersede this section."

HOUSE COMMENT:

- **ENDLESS, FRIVOLOUS LAWSUITS**

First of all, even those who are advocating new proposed language, which are the same people who supported the above Senate version of this bill, admit that there are serious problems with the current Senate language which set trustee compensation as "reasonable" and could expose charitable trusts to endless and frivolous lawsuits.

PROPOSED LANGUAGE OFFERED BY NA PUA KE ALII, RANDY ROTH AND COMPANY, THE GOVERNOR AND ATTORNEY GENERAL

"Absent a contrary provision in the governing document, Trustees of charitable trusts will set the level of their own compensation. However, compensation paid to any particular trustee must always be reasonable under the circumstances and compensation higher than the salary of the Chief Justice of the Hawaii Supreme Court must be approved by the Probate Court, using this same standard. In situations where compensation is set by the Probate Court, the trustees will be able to participate in any related hearing or even appeal the court's order, but only at their own expense."

HOUSE COMMENTS:

- **ARBITRARY, FLAWED---HOUSE POSITION REINFORCED**

Now comes this hastily drafted "proposed amendment" to the Senate proposal which they now claim will resolve the possible harm to the trust which could have resulted from the Senate's conference version. ("Broken Trust" authors memorandum dated April 28,1998:"...we recognize the concern...that the absence of a specific cap might set the stage for costly litigation each year to determine what is reasonable..."). So right now, the Senate version that's before this conference committee is admittedly flawed because applying a "reasonable" standard to trustee compensation could expose the trust to increased litigation. The House takes little comfort in these assurances that the Senate's original position which could have caused harm to the trust is O.K. now. The House believes that the very act of offering this "eleventh hour" amendment (because the Senate's original proposal could have placed the trust in endless litigation and cost the trust untold dollars in legal fees) in fact dramatically and strongly emphasizes the need to have a task force look into the complex issues involving trustee compensation.

- **COMPENSATION EXPERTS SAY CAPPING IS NOT RATIONAL**

Capping trustee compensation at the state's Chief Justice salary and defining that as the automatic cut off point as to what is "reasonable" not only makes no logical sense but compensation experts agree that such a cap is not rational. The House has heard from local and national compensation experts who have said that there is no justifiable basis for tying trustee compensation to the salary of any state worker, whether it's the governor, chief justice of any other public employee.

- **UNFAIR**

Other bills offered by the Attorney General this session would have lowered the Chief Justice's salary. Tying the Chief Justice's salary to trustee compensation would "politicize" every salary adjustment made to the chief justice's pay. Would a raise for the Chief Justice become a raise for the trustees? Is this fair to the Judiciary and the Chief Justice? Is this fair to trusts and trustees?

- **PROBATE COURT ALREADY HAS EXPERTS REVIEWING TRUSTEE COMPENSATION**

The House has received information that the Probate Court has ordered and both the court and the Attorney General's Office have already received expert compensation analysis regarding Bishop Estate trustees commissions done by at least three different national compensation firms. All three firms have concluded that current levels of compensation for the trustees of Bishop Estate fall within an acceptable and justifiable national range for companies of similar size and executives of comparable duties and responsibilities. What expert witnesses or testimony do we have that would justify passing a law to cap trustees pay at a level arbitrarily suggested by a few? Again, the House position to gather the facts and make decisions based on those facts, appears to be the only truly reasonable thing to do.

- **FEDERAL INTERMEDIATE SANCTIONS LAW**

Those who advocate the Senate position and the latest changes, frequently refer to the federal Intermediate Sanctions Law as the basis for changing Hawaii's current statutory formula for trustee compensation. However, the House is aware of the fact that the Internal Revenue Service is currently drafting guidelines, rules and regulations to implement the federal law. The federal law will supersede any state law. Since no federal rules and regulations have been adopted, The House position is that there is a need to consider the federal requirements prior to acting on state statute. Again, the House proposal for a task force which would consider factors such as the federal legislation is the more prudent position. It makes no sense to pass something which may need to be changed again because it conflicts with federal law. The IRS has tentatively set late summer or early fall for the release of their rules and regs on the Intermediate Sanctions law.

- **PROTECTING TRUST ASSETS**

Included in the recent proposed amendment is the suggestion that the trust pay for legal costs of the Attorney General with regard to any challenges involving reasonable compensation, regardless of whether the AG wins or loses on those challenges. Such requirements raise concern regarding the use of trust assets.

- **LIABILITY AND FAIRNESS**

Currently, Trustees are personally liable for their actions. Arbitrarily capping trustees compensation because some people say that's reasonable, yet leaving trustees personally liable appears inherently unfair.

The Honorable Terrence W. H. Tom, Chair
and Members of the Committee on Judiciary
Hawaii State House of Representatives
Hawaii State Capitol Room 325
415 South Beretania Street
Honolulu, Hawai'i 96813

Re: H.B. No. 2362 Relating to Charitable Trusts

H.B. No. 2587 Relating to Charitable Trusts

H.B. No. 3007 Relating to Charitable Trusts

Submitted by:

Gary C. Hourihan
Chairman and CEO of Strategic Compensation Associates

633 West 5th Street, Suite 3650
Los Angeles, California 90071
(213) 488-8570

Deposition Exhibit No. 135
Deposition of Lindsey
Date 12-4-99

LLL 000117

It is my strong professional opinion that any legislation pertaining to the compensation of the Trustees of Kamehameha Schools Bishop Estate (KSBE) must take into consideration the unique aspects of KSBE compared to other charitable trusts. Specifically:

- KSBE is self-funding and does not rely on charitable contributions to sustain its operations

- KSBE encompasses both a major operating entity (Kamehameha Schools) and an extremely large ($8 billion to $10 billion) investment portfolio. In contrast, the vast majority of other foundations and trusts are significantly smaller and do not have a separate operating arm. Also, in those limited cases where a separate operating entity exists, it typically is managed by a different board or trustee group

- Unlike the typical foundation or trust, the KSBE Trustees take a proactive role in key investment decisions as opposed to merely monitoring the performance of professional money managers. Moreover, the fact that most of KSBE's investments are in real estate adds a further layer of complexity.

- KSBE is subject to a much higher level of public scrutiny than the typical foundation or trust

Due to the uniqueness of KSBE, any legislation that ties Trustee compensation to the pay levels of designated public officials becomes extremely difficult to justify. Rather, appropriate and fair compensation for the Trustees is a complicated issue that needs to take into account their specific role and responsibilities.

In my professional opinion, reasonable counterparts to the role of the Trustees exist in both the public and private sectors. These include the senior managers and directors of organizations that combine investment management and operating responsibility, such as real estate developers and real estate-oriented banks. It also includes the investment and administrative arms of selected educational institutions, such as Princeton, Harvard, Duke, Texas, and Stanford, where the endowment is large and proactively managed.

The KSBE Trustees have taken the appropriate and rational step of maintaining their compensation within reasonable limits supported by a thorough and professional analysis of the amount typically earned by those with comparable responsibilities. Legislation that overrides this process by artificially linking their compensation to individuals with vastly different roles is difficult to support.

GARY C. HOURIHAN

SCA Consulting
633 West 5th Street, Suite 3650
Los Angeles, California 90071
(213) 488-8570

Education:

B.A., Princeton University, 1970

M.B.A., University of Chicago, 1972

License en Economique Applique, Universite de Louvain, Belgium, 1972

Employment:

Co-founder and President, SCA Consulting, Los Angeles, California, 1984 - present

Vice President, Booz, Allen & Hamilton, San Francisco, California, 1979 - 1984

Unit Manager, Hewitt Associates, Lincolnshire, Illinois, 1977 - 1979

Regional Vice President, Citibank Brussels, Brussels, Belgium, 1974 - 1977

International Planning Group, Citicorp, New York, New York, 1972 - 1974

Honors and Awards:

Deans List, Princeton University; University of Chicago

International Business Fellowship, University of Chicago

Who's Who In Leading American Executives

Professional Activities:

Past Speaker:

American Compensation Association
American Program Bureau
American Society of Corporate Secretaries
Conference Board
Directors' College at Stanford University
Hospital Financial Management Association
International Forum

Past Speaker: (Continued)

LOMA Human Resource Forum
PROSHARE (London)
University of St. Gallen (Switzerland) - Business Forum

<u>Articles/Quotes</u>:

The Atlanta Constitution
The Corporate Board
Boardroom Reports
Crane's New York Business
Directors and Boards
Investor's Daily
Los Angeles Business Journal
The Los Angeles Times
Management Review
Orange County Register
USA Today
The Wall Street Journal

Strategic Compensation Associates

Creating value
through performance measurement
and compensation design. . .

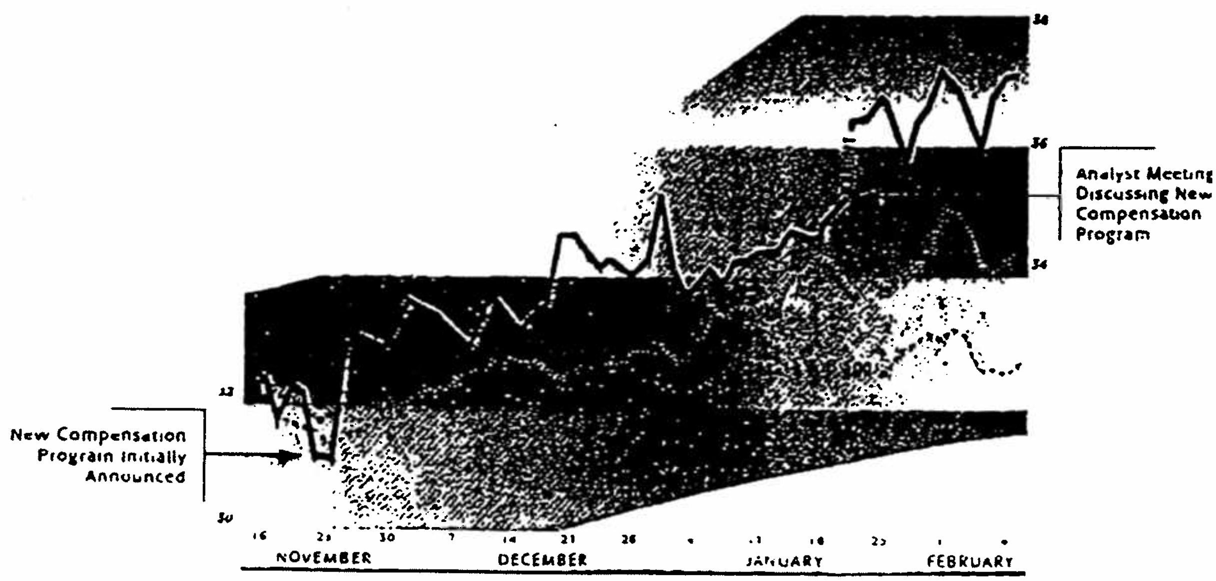
Strategic Compensation Associates (SCA) is an international consulting firm dedicated to designing compensation strategies and programs that focus participants on achieving business objectives and creating shareholder value. SCA is one of the largest and most highly respected firms in its field and a recognized leader in developing innovative, performance-based compensation plans. We serve our clients through five full service offices in Los Angeles, New York, Chicago, London, and Mexico City.

Our Approach

SCA'S APPROACH IS BASED ON FIVE GUIDING PRINCIPLES:

- We view compensation as a powerful (and often underutilized) strategic management tool that can influence and focus behavior and contribute significantly to the creation of shareholder value
- A well thought-out compensation strategy forms the basis for an effective total pay program
- A compensation strategy must recognize and respond to each company's unique culture, organizational structure, business strategy, and value-creation process
- Compensation, and executive compensation in particular, is best aligned with shareholder interests when a meaningful portion of pay is "at risk" through performance-based incentives
- "At risk" compensation should be linked to performance criteria that are measurable, provide "line-of-sight" focus, and are closely related to increasing shareholder value

SUPPORTING A VALUE-CREATING STRATEGY THROUGH COMPENSATION PROGRAM DESIGN



INDEXED TO CLIENT'S SHARE PRICE (DAILY CLOSE)

We differentiate ourselves in four important ways

1 We approach compensation planning from an integrated perspective with the goal of reinforcing business strategy and the decisions that build shareholder value.

At the heart of our approach is an in-depth understanding of the client's market dynamics, business strategy, organization, and the processes by which shareholder value is created. This understanding allows us to make informed recommendations regarding the key components of the reward system, including performance measurement, performance goals, risk, and pay opportunity.

2 Our staff combines the strategic, financial, organizational, and compensation expertise required to design and implement strategically-driven compensation programs.

SCA's consultants are among the most highly skilled and educated in our field. Prior to joining SCA, many were partners or senior consultants within the most prestigious management consulting firms. Each was selected on the basis of an outstanding academic record, strong problem-solving skills, a broad business perspective, and the ability to deal effectively with senior executives and Boards of Directors on complex issues.

3 We tailor innovative solutions to each client's particular strategy, organization, and value-creation process.

We avoid "off-the-shelf" solutions in favor of advice based on a thorough understanding of a client's business, culture, markets, and value-creation process. This understanding is gained through a process that combines interviews with management and the Board of Directors, a thorough review of business strategies, analysis of financial and stock price performance and the factors that drive shareholder value, assessment of competitive pay practices, and analysis of potential accounting, cost, and regulatory issues. Based on this input, we design pay programs customized to each client's needs.

INTRODUCING VALUE-BASED MEASUREMENT

After internally developing a value-based planning model, a major financial institution retained SCA to refine the model and integrate the resulting value-based measurement process into the Company's incentive program

To this end, SCA worked with a task force comprised of senior representatives from the client's strategic planning, finance, and human resource organizations. As an initial step, SCA assisted in identifying and resolving technical issues associated with the value model, such as treatment of transactions unique to the client's business. SCA then helped the task force translate the value-based measurement process into alternative incentive concepts. Finally, SCA modeled the implications of these alternatives under various assumptions to develop appropriate relationships between payout and performance

The process resulted in the successful implementation of a new incentive concept that rewards for sustained value creation as measured by the client's value-based planning model, but with goals calibrated against an external market benchmark. Key to the success of the process was SCA's knowledge of both value-based planning techniques and compensation strategy and design

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4 We recognize that consistently high quality work is the foundation of our continued success.

Our commitment to superior quality is demonstrated in numerous ways, including:

- Rigorous analysis to support our recommendations
- Significant, "hands-on" involvement by our partners and senior staff in each assignment
- A "one firm" philosophy which ensures that our approach to client work is consistent across our various offices
- An extremely strong record for implementation of our recommendations among our clients
- A superior level of responsiveness to client needs and time constraints

SCA'S INTEGRATED APPROACH

Our Services

TOTAL COMPENSATION STRATEGY

The foundation of an effective total pay program is a compensation strategy that is consistent with and reinforces a company's business strategy, culture, and market characteristics. Such a strategy provides a "blueprint" for addressing and resolving key compensation issues, including pay opportunity, compensation risk (i.e., the role of incentives), performance measurement, and goal-setting. SCA's tailored, business-oriented approach to compensation issues ensures that the compensation strategies we develop appropriately reflect the unique characteristics of each client.

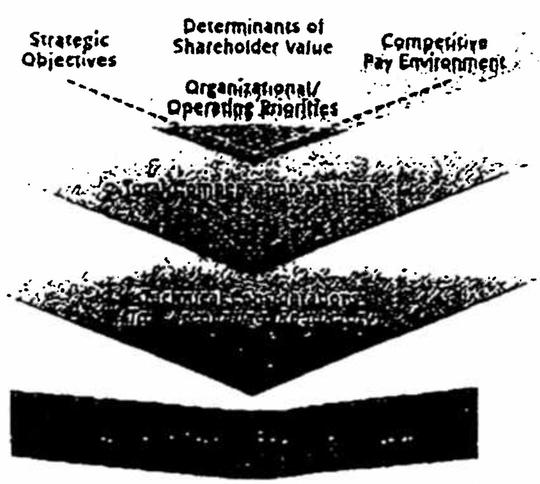
BUSINESS UNIT COMPENSATION

Strategic differences among business units often make a single, company-wide compensation program inappropriate. For example, the approach to compensation risk and performance measurement within a mature, cash generating unit is far different from the approach needed in a newer, high growth business. SCA has extensive experience developing compensation strategies and approaches to performance measurement that respond to the unique requirements of a particular business unit while remaining sensitive to overall company-wide considerations.

COMPETITIVE PAY ANALYSIS

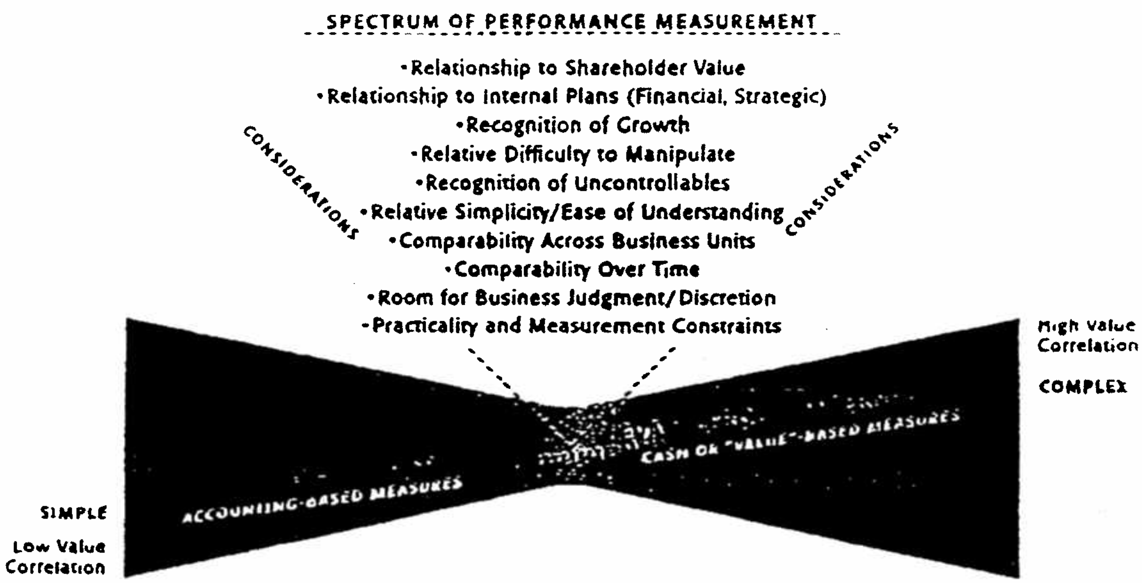
Reliable competitive compensation data is a requirement in the development of any compensation program. In cases where existing survey data are either too general or unavailable, SCA has extensive experience assisting clients in the development of appropriate peer groups and the collection and analysis of private survey data.

DEVELOPMENT OF COMPENSATION STRATEGY AND PROGRAM DESIGN



PERFORMANCE MEASUREMENT AND INCENTIVE PLAN DESIGN

Performance measurement and goal-setting are the foundation of an effective incentive plan. Measures must reflect controllable contributions and be directly linked to the creation of shareholder value. In turn, performance goals must provide a reasonable balance between realistic potential for achievement and the requirement to create incremental value. SCA's consultants are skilled in the techniques needed to identify critical performance measures and to assess the difficulty inherent in performance goals We also have an in-depth understanding of the various cash and value-based measurement models, such as Economic Value Added (EVA), and the issues associated with applying such models to incentive plan design. These skills and knowledge allow us to develop incentive performance measures and related goals that are directly compatible with each client's culture and value-creation process.



COMPENSATION WITHIN PRIVATELY HELD FIRMS

The unique aspects of private ownership raise a number of intriguing compensation issues. Among these is the challenge of developing programs that can compete effectively with equity incentives offered by publicly-traded competitors. SCA has worked with many privately-held organizations to design phantom equity plans that closely replicate the opportunity associated with actual ownership.

BOARD OF DIRECTORS' COMPENSATION

Board of Director compensation practices have changed dramatically in response to the increasing complexity and liability associated with Board membership. In many companies, equity incentives, retirement plans, and other non-cash compensation programs now form a significant portion of outside director compensation. SCA has worked with numerous Boards to develop innovative director compensation programs that reflect the unique challenges of Board membership while remaining sensitive to shareholder concerns.

CREATING VALUE AT THE BUSINESS UNIT LEVEL

[illegible] value creation process for the IPP was different from that of the utility, the Company was interested in developing a pay program tailored to its own unique requirements.

SCA assisted in the development of a new compensation strategy and program for the subsidiary firm. We identified key steps in the value creation process for IPPs, developed a way to quantify value at the business unit level, determined the historical and prospective growth in value for the subsidiary, and assessed competitive compensation levels among IPPs. Given these analyses, we recommended a total compensation strategy and specific pay programs, including a salary [illegible] we also recommended some linkage of the subsidiary executives to the parent through participation in the parent's long-term incentive plan.

To date, the program has been highly successful in focusing participants on enhancing value at the business unit level, aligning subsidiary interests with those of the parent, and attracting and retaining key talent. Prospectively, the long-term incentive plan is expected to generate significant payouts if substantial value in the subsidiary is created, and no payment if the Company has not at least achieved a threshold return on its investment.

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SALES COMPENSATION

The complex relationships among volume, profitability, and individual motivation make the development of effective sales compensation programs particularly challenging. At the same time, effective sales incentive programs can be a powerful means of implementing corporate strategy, playing a critical role in new product introductions, shifts in product mix, and customer service and support. SCA's approach to sales compensation is to perform a rigorous series of analyses to capture the critical elements of business, marketing, and sales and service strategy. We identify key measures of sales success, including customer satisfaction, type and difficulty of sale, and underlying economics of each sale, evaluating each across individuals, regions, and account types. This work defines sales force roles and accountabilities, which together form the basis of an effective sales incentive program.

STRATEGIC SALARY ADMINISTRATION

While incentive compensation is the heart of most performance-based pay programs, the introduction of a salary administration and job evaluation system built around a company's key success factors offers a potentially powerful tool to extend performance-based pay throughout an organization. In contrast to traditional salary systems built around individual span of control, a strategic salary system links salary and position-in-range to individual skills and factors that drive the creation of shareholder value. SCA has helped numerous clients revise their thinking about salary administration and the important role it can play in the value creation process.

[illegible]

[illegible] risk and carried a sense of entitlement by relying heavily on grants of restricted stock. The Company wished to introduce a strong performance orientation and sense of individual accountability, while minimizing the level of dislocation inherent in such a significant change to existing compensation practices.

SCA worked with both Company management and the Compensation Committee to assess the performance potential and key value drivers of the business as well as the cultural implications of introducing greater risk and focus into the compensation program. This process involved extensive management and Committee discussions aimed at [illegible] measurement that linked incentive compensation payments more directly to the creation of incremental value.

The process resulted in the implementation of both a new value-based approach to performance measurement and a new risk-oriented compensation program based on this approach. Management acceptance of the new program was achieved by a combination of ongoing management involvement, open communication, and realistic value-creation goals that reflect the capabilities of the Company and its various business units. The new program has been cited by institutional investors as a reason for their purchasing the Company's stock.

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INTERNATIONAL COMPENSATION ISSUES

The increasingly global nature of the world economy places a premium on developing compensation strategies and programs that convey consistent messages across different locations. At the same time, such strategies and programs must take into consideration the culture, tax and regulatory climate, and compensation practices within each country. SCA's consultants have successfully addressed multinational compensation issues in Europe, Canada, Latin America, Australia, and the former Soviet Union and have an in-depth knowledge of the complexities inherent in global compensation projects. We address international compensation issues in our U.S. offices as well as in our offices in London and Mexico City.

TECHNICAL AND LITIGATION SUPPORT

Compensation programs face increasing scrutiny by external investors and regulatory agencies. In turn, changes in tax laws, accounting rules, and disclosure requirements resulting from this scrutiny directly affect compensation program design. SCA keeps current on all important regulatory, tax, and accounting issues affecting compensation and advises clients how best to respond to such issues. We also have assisted both shareholders and management as an expert witness and in developing the analytic support needed to resolve disputes arising from inquiries into compensation practices.

EXECUTIVE EMPLOYMENT AGREEMENTS

Proxy disclosure requirements and investor concerns over executive compensation practices dictate that executive employment agreements be particularly well thought out. SCA has worked with numerous organizations to structure and negotiate executive employment and change-of-control agreements that balance the needs of management with shareholder interests, while addressing complex technical considerations.

INTRODUCING A PERFORMANCE-FOCUSED BONUS PLAN IN A DIVERSIFIED MEXICAN COMPANY

A large, privately-held Mexican company with a diversified portfolio of businesses asked SCA to develop a bonus plan that would motivate business unit managers and corporate staff to achieve rapid growth and profitability.

To develop this plan, SCA reviewed each business unit's strategy and financial impact on overall Company results. SCA then identified key performance measures for the different businesses based on each unit's unique financial and strategic imperatives, including market share penetration for a high growth unit, gross margin for a service business, and volume and sales turnover in a slow growing division. These measures formed the basis for the largest component of award opportunity under the new plan.

In addition to the unit-specific measurement process, SCA developed a framework to reinforce other corporate priorities, including short-term improvement in revenue and profits, cooperation among the business units, and a "one-company" culture.

Following approval of the plan, SCA developed a user-friendly PC-based model that ensured a smooth implementation and serves as an ongoing administrative tool.

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Our Clients

SCA's clients include numerous top *Fortune* firms as well as many smaller publicly-traded and privately-held organizations. Since our formation in 1984, we have served over 500 different clients in the United States, Europe, Canada, Latin America, Australia, and the former Soviet Union to address and successfully resolve a wide variety of compensation issues.

We are particularly proud of the fact that the vast majority of our client assignments result in long-standing relationships. In addition, direct referrals from satisfied clients and Board members represent a significant portion of our inquiry stream.

"Dow is undergoing a continuing process to improve how the Company thinks about and manages for value. As part of this process, we worked with SCA to review and revise how Dow measures performance and rewards managers. SCA brought their unique and innovative perspective to Dow—an understanding of both the principles of value-based management and the practicalities of effective compensation plan design"

JAMES HAZEL
Director,
Global Compensation & Benefits
Dow Chemical Company

"Over the past four years, we have increased the performance orientation of our management compensation programs and have linked these programs directly to our new value-based measurement process. SCA helped us significantly in these endeavors. In particular, their expertise in performance measurement techniques and incentive plan design proved invaluable in translating Times Mirror's approach to value-based measurement into workable incentive concepts that reward directly for creating value for our shareholders"

JAMES SIMPSON
Senior Vice President,
Human Resources
Times Mirror Corporation

"In a challenging assignment involving a major U.S. acquisition, SCA helped bring life to the ideal of aligning management incentives with National Power's business strategy. SCA's creativity, tireless effort, and sensitivity to organizational issues enabled us to craft a tailored program balancing participants' desire for an entrepreneurial plan with National Power's performance requirements. Throughout the assignment, SCA always provided high quality advice and met the most challenging deadlines."

STEPHEN PERKINS
Head of Human Resources
National Power International

"Illinois Central undertook an enormous task to recraft every part of our management compensation program—and we wanted to complete the task in record time. SCA provided expertise and careful attention and helped us create what many analysts are calling the premier compensation program in the U.S. transportation industry"

JAMES HARRELL
Vice President,
Human Resources
Illinois Central

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Our Joint Venture Partners

SCA is an independent partnership that has affiliations with Korn/Ferry International, the world's largest executive search organization and Mullin Consulting, Inc., a leader in the design, security, and funding of executive benefit programs. Our affiliation with these organizations provides SCA with an extensive international network, access to world-wide compensation trends, and the opportunity to offer a wide range of consulting services.

KORN/FERRY INTERNATIONAL
serves its clients through 58 offices in key business centers in North America, Latin America, Europe, and the Asia/Pacific region. The firm specializes in recruiting senior level executives, assessing the capabilities of management teams, and addressing issues associated with organization structure and the decision-making processes.

MULLIN CONSULTING, INC.
specializes in the design and funding of innovative benefit programs for executives, including deferral plans, supplemental retirement programs, and special survivor and disability plans. The firm also is recognized for its leading-edge solutions to the security issues inherent in nonqualified benefit plans

BUILDING AN OWNERSHIP MENTALITY WITH A BROAD-BASED EQUITY PLAN

One of the largest direct retailing companies in the U.S. was undergoing a major restructuring, requiring a refinancing of the Company and divestiture of all non-core businesses.

SCA worked with the Company to develop a broad-based equity plan. Key objectives of the plan were to promote an ownership mentality, encourage a performance orientation, and enhance retention of key employees. To carry out the assignment, SCA conducted financial and stock price analyses to test the upside potential inherent in the Company's restructuring plan, conducted interviews and participatory meetings to determine perceptions of various approaches to plan design, modeled the cash flow, tax, and accounting implications of qualified and non-qualified alternatives, and developed specific recommendations on plan design.

Based on our work, the Company adopted a discounted stock purchase plan, offering the employees a 40% discount on the purchase of Company stock held for at least three years. We assisted the Company in fully implementing this plan by working with legal counsel on the development of plan documents, drafting employee communication material, and developing a communications strategy.

The program has been a dramatic success. Since its introduction, over 65% of employees are participating in the new plan and the stock has more than doubled in price

RESOLUTION TO CAP PAYMENTS TO BISHOP ESTATE TRUSTEES

WHEREAS, the Estate of Princess Bernice Pauahi Bishop was established to be used for the benefit of Hawaiian children; and

WHEREAS, only the cream of the crop comprising less than 15% of the Hawaiian keiki o ka aina are allowed entry into the Kamehameha schools; and

WHEREAS, there is a crying need for the expansion of Kamehameha school programs on Oahu, the neighbor islands and especially in areas such as Nanakuli, Miloli'i, Waimanalo and Hauula where the plight of Hawaiian children should be uplifted; and

WHEREAS, the Bishop Estate is chartered as a charitable trust under Hawaii State Law, and is subject to legal exemptions and privileges as a charitable trust; and

WHEREAS, many charitable trusts do not pay or allow their trustees to receive funds for the operation of such trusts since they are in effect carrying out a community service; and

WHEREAS, Bishop Estate trustees, whose salaries are in excess of $900,000 each year, are taking for themselves those funds desperately needed for the benefit of Hawaiian children and for the expansion of the Kamehameha schools; and

WHEREAS, such an expansion of the Kamehameha schools would resonate with the Princess's legacy since it would allow for a larger percentage of Hawaii's Hawaiian keiki to be included in the benevolent intent of Princess Bernice Puahi Bishop; and

WHEREAS, Bishop Estate trustees will have little moral credence in the community and the judicial system with their charges against Kuapa isle residents who are being characterized as "stealing our land" when Bishop Estate trustees with their inordinate salaries are in effect stealing much of the money intended for our Hawaiian keiki o ka aina; and

WHEREAS, the exorbitant fees paid to these trustees tend to have a corrupting influence on would-be future trustees, their families, friends, and associates; now, therefore

BE IT RESOLVED that the Democratic Party of Hawaii calls for the adoption of legislation to place a cap on the fees paid to each of the Bishop Estate trustees that would not exceed the current annual salary of the Governor of the State of Hawaii; and

BE IT FURTHER RESOLVED that copies of this resolution be forwarded to all members of the State Legislature.

Offered by Liana Petranek, Alfred Akana, and Ibrahim Aoude

CTE: GOVERNMENT OPERATIONS **RESO#: GOV.41**

Deposition Exhibit No. 136
Deposition of Lindsey
Date 12-4-99

RESOLUTION TO LIMIT PERCENTAGE OF MONEY SPENT BY NON-PROFIT ORGANIZATIONS ON ADMINISTRATION AND SALARIES

WHEREAS, non-profit organizations should maximize the percentage of money that is directly spent on programs to help improve the living conditions of Hawaii's people; and

WHEREAS, non-profit organizations should therefore minimize the amount spent on administration and salaries; and

WHEREAS, offering high compensation to non-profit trustees is inappropriate to the notion of public service; and

WHEREAS, the trustees of large landed estates in Hawaii have benefited greatly from the large general increase in the price of land in Hawaii by using an outmoded formula for trustee compensation; and

WHEREAS, this increased compensation directly reduces the amount that can be spent on programs to benefit the people of Hawaii; and

WHEREAS, this increased compensation is not commensurate with actual trustee duties, which consist largely of deciding among options worked out by professional staff; and

WHEREAS, Congressional investigations into the problem of excessive non-profit salaries have resulted in the suggestion that no salaries at national non-profit organizations should exceed that of the President of the United States; now, therefore

BE IT RESOLVED, that the Democratic Party resolves that trustee compensation for Hawaii non-profit organizations should be limited by law to the same salary as the Governor of the State of Hawaii.

Offered by Liana Petranak

CTE: GOVERNMENT OPERATIONS **RESO#: GOV.42**

File

We, the undersigned member delegates of the Government Operations Committee, file this minority report opposing the passage, of Resolution #41: "Resolution to Cap Payments to Bishop Estate Trustees."

We oppose the attempt of the Democratic Party to intrude government into the business of a private trust.

In particular, we oppose the specific targeting of this one trust. This resolution discriminates solely against a Hawaiian institution and its board of Hawaiian trustees.

While we take no position on the subject of commissions of the Bishop Estate Trustees, we do take issue with the fact that this resolution proposes that the legislature take action to target solely the Kamehameha Schools Bishop Estate.

We believe that this resolution is contrary to the anti-discrimination tenets found in the affirmative action position of the Democratic Party.

In addition, this resolution is filled with inaccuracies regarding Kamehameha Schools' students, programs and policies.

This resolution is inappropriate, inaccurate and unacceptable in its bias against a Hawaiian organization and its board of trustees and, because of its blatant bias, is unconstitutional and contrary to the laws of equal protection. We urge that this resolution be defeated and filed and that this report be accepted.

Arthur K. De Luis, Jr.

Linda Rosehill

Maurice Oshiro

John Williamson

Clifford LaBoy

Sesnita Moepone

RECEIVED
KSBE
TRUSTEES OFFICE

APR 23 11 02 AM '99

KAMEHAMEHA SCHOOLS BERNICE PAUAHI BISHOP ESTATE

GOVERNMENT RELATIONS DEPARTMENT
567 SOUTH KING STREET, SUITE 100 HONOLULU, HAWAI'I 96813
TELEPHONE (808) 523-6364 FAX (808) 523-6365

To:	Trustee, Henry Peters	Dr. Michael Chun
	Trustee, Richard Wong	Rodney Park
	Trustee, Oswald Stender	Nathan Aipa
	Trustee, Lokelani Lindsey	Yukio Takemoto
	Trustee, Gerard Jervis	Randall Chang
From:	Alika Thompson	
Date:	April 28, 1999	
Re:	GM145: MARGERY S. BRONSTER, GUBERNATORIAL NOMINEE AS ATTORNEY GENERAL	

Attached is Governors Message no. 145 for your information.

AT:gj

139

Exhibit No. Lindsey
Date 12-4-99

LLL 000136

STAND. COM. REP. NO. 1805

Honolulu, Hawaii

April 27, 1999

RE: GOV. MSG. NO. 145

Honorable Norman Mizuguchi
President of the Senate
Twentieth State Legislature
Regular Session of 1999
State of Hawaii

Sir:

Your Committee on Judiciary, to which was referred Governor's Message No. 145, submitting for study and consideration the nomination of:

MARGERY S. BRONSTER, gubernatorial nominee as Attorney General, for a term to expire December 2, 2002,

begs leave to report as follows:

Upon review of the resume and other background information submitted by the nominee, your Committee finds that Margery Bronster holds an A.B. degree in Chinese Language and Literature and History from Brown University, and a J.D. degree from the Columbia University School of Law. Ms. Bronster has practiced law with a New York firm and, for six years, with the Honolulu firm of Carlsmith Ball Wichman Murray Case & Ichiki. Ms. Bronster has served as Attorney General since January 1995, and is now nominated for a second term.

Testimony in support of the nominee was submitted by the Attorney General of Mississippi, the Hawaii State Commission on the Status of Women, the Department of the Prosecuting Attorney for the City and County of Honolulu, the Department of the Prosecuting Attorney for the County of Maui, the Office of the Prosecuting Attorney for the County of Hawaii, the Honolulu Police Department, the Maui Police Department, the Kauai Police Department, the Hawaii Police Department, the Domestic Violence Clearinghouse and Legal Hotline, the Sex Abuse Treatment Center, the Hilo Medical Center, the Kamehameha Alumni Association of the Northern California region, the Hawaii Carpenters Union, the

The Senate
Twentieth Legislature
State of Hawaii

Record of Votes of the Committee on Judiciary

Measure:	Committee Referral:	Date:
GM 145	JDC	4/16/99

☐ The committee is reconsidering its previous decision on this measure.

The Recommendation is to:

- ☐ Pass, unamended
- ☐ Pass, with amendments
- ☐ Hold
- ☐ Recommit
- ☒ Advise and Consent
- ☐ Not Advise and Consent
- ☐ Advise and Consent with Exception

Code	Members	Ayes	Ayes(WR)	Nays	Excused
103	CHUMBLEY, Avery B. (C)	X			
116	MATSUNAGA, Matt (C)	X			
105	CHUN OAKLAND, Suzanne	X			
110	IHARA, Les, Jr.	X			
120	SAKAMOTO, Norman				X
123	TANAKA, Joe		X		
100	ANDERSON, Whitney		X		
TOTAL		4	2	0	1

Recommendation: ☒ Adopted ☐ Not Adopted

Chair's or Designee's Signature:

Distribution:
Original - Committee   Yellow - Clerk's Office   Pink - Drafting Agency

LLL 000138

3

E+Y File

KAMEHAMEHA SCHOOLS BISHOP ESTATE
Trustees Office

To: Trustees

From: Lokelani Lindsey Lokelani

Date: January 26, 1995

Re: Wexler Group, Hecht, Spencer & Associates, Inc.

Per the request from Chairman Wong, attached for your review are the request for extension of contract from the Wexler Group and the proposal from Hecht, Spencer & Associates, Inc. These materials are being provided for our discussion today.

Deposition Exhibit No. 138
Deposition of Lindsey
Date 12-4-99

LLL 000139

October 14, 1994

Mr. Myron B. Thompson
Chairman
Board of Trustees
Kamehameha Schools/The Bishop Estate
567 South King Street
Suite 200
Honolulu, Hawaii 96813

Dear Mr. Thompson:

This letter, when signed by you and returned to us, will constitute an amendment to and extension of the letter of agreement dated April 14, 1994, pursuant to which Kamehameha Schools/The Bishop Estate ("The Bishop Estate" or "you") has retained The Wexler Group, a unit of Hill and Knowlton, Inc., ("The Wexler Group" or "we"), as consultants for the purpose of providing government affairs advice and strategic counsel on issues before Congress and the Executive Branch, including legislation providing Native American organizations with authority to repurchase lands taken by eminent domain.

This agreement shall be effective as of November 1, 1994, and will remain in effect through October 31, 1995, subject to the right of either party to cancel this agreement upon 30 days' written notice.

In consideration of The Wexler Group's provision of government relations services and of making our time available, The Bishop Estate will pay The Wexler Group a retainer fee of $15,000 per month.

All other terms and conditions in the letter of agreement dated April 14, 1994, between The Bishop Estate and The Wexler Group shall remain binding.

The Wexler Group is pleased to continue to be a part of your governmental affairs activities and looks forward to continuing to serve Kamehameha Schools/The Bishop Estate.

Sincerely,

Anne Wexler
Chairman

AGREED:

Kamehameha Schools/The Bishop Estate

BY: ______________________________
Mr. Myron B. Thompson DATE:
Chairman, Board of Trustees
[AUTHORIZED SIGNATURE]

101394/DWS/sns

HECHT, SPENCER & ASSOCIATES, INC.

RECEIVED
KS/BE
TRUSTEES OFFICE

JAN 9 5 04 PM '95

January 6, 1995

Mrs. Lokelani Lindsey
Trustee
Kamehameha Schools Bernice Pauahi Bishop Estate
567 South King Street, Suite 301
Honolulu, Hawaii 96813

Dear Mrs. Lindsey:

As a follow-up to our December 14, 1994, meeting in Los Angeles with Dickie Wong, Henry Peters, Dennis Walsh and you, this letter will outline how Hecht, Spencer & Associates proposes to assist Kamehameha Schools/Bishop Estate (KSBE) in identifying and realizing their goals in Washington, D.C. Initially, we believe it is imperative that the Trustees agree on the importance of educating Congress and the Clinton Administration and be willing to dedicate the necessary time and resources in obtaining this goal. Your specific goals with respect to Washington can evolve over the course of time; however, we do believe the commitment to spread the positive news of KSBE is something that should not be delayed.

We understand that Hawaii's Congressional delegation, led by Senator Inouye, has for the most part been very supportive of KSBE over the years. They need to remain the essential ingredient in informing the rest of Washington about the positive aspects of KSBE. After developing and reviewing our plan, we should approach the delegation (initially, Senator Inouye) and ask for their reaction. The next step would be to ask them to take a leadership role in helping KSBE implement the plan. Your interest in making positive change will impact their commitment to your cause. The more allies you have in Washington, the easier it is to accomplish your goals there.

499 South Capitol Street, S.W. Suite 507 Washington, D.C. 20003 (202) 554-2881

The three major issues we see affecting KSBE in Washington are funding, IRS-related measures and Title VI. These areas have been successfully monitored up to this point. However, with the recent CNN piece and the attack on funding from some in the last Congress, we believe it is essential to begin some major education in Washington. Our goal would be to inform all members, but we need to insure that we make a major impact on those legislators who are vital to your interests. By targeting the proper committees, you can be actively involved in any attempts to legislate on issues that affect KSBE.

With respect to funding, we believe that there will be a strong effort in the House to strip the funding. This was done last year, and Senator Inouye was very skillful in working out successful language, first in the Senate and then in Congress. We feel the Trustees need to make a decision about how they want to address this issue (i.e., fight it at every stage, watch from the sideline, work for compromise, find another implementer, etc.), and then use that decision as the foundation for educating and exposing Congress to the school. This is the highest profile issue for Congress, so the way in which the Trustees decide to address this issue will likely dictate the PR battle that ensues from both camps. We discussed this at length during our December meeting, and consensus then was also to get agreement on a decision from all Trustees.

While government funding is the issue that will be most readily identified with KSBE, the IRS situation is what we believe will be most important to the school in the years ahead. Because of the school's unique situation and tremendous success, you have been watched closely over the years. Undoubtedly, this will continue and possibly increase as more exposure comes to the school (e.g., CNN piece). In this vein, it is important that there be closer tracking in Washington, both on the Hill and in the Administration, on issues affecting how the IRS views KSBE. You have done an excellent job in working with those who audit and oversee you on the local level, but we believe it is important to expand your efforts to the federal level, as necessary.

Finally, there have been some discrimination claims leveled against the school recently, specifically violations of Title VI. The school has responded in the proper manner, but again, we think it is important to observe this issue from a Washington perspective because claims may increase as the school becomes more visible.

KSBE has reacted favorably to questions regarding all of these matters as they have come up in Hawaii. We suggest that your story now be presented to Washington. This will give you another voice as potential stories appear as well as place you in a stronger position in Hawaii. The Trustees need to make some decisions, primarily about handling the government funding situation. When we have your decisions and proposed plans, we will implement an education process, as follows:

I. Goals and Objectives
   A. Trustees meet and formulate plan
   B. Review and alteration with Senator Inouye
   C. Discuss with rest of Hawaiian delegation

II. Educate
   A. Hecht, Spencer targets and contacts key members and committees
   B. Trustees (or representatives) come to Washington for major educational initiative
      1. Social function (possible luau) with Hawaiian delegation serving as co-hosts
      2. Individual meetings with appropriate members
      3. Possible address to education-based organization

C. Work with area school graduates and other interested organizations to increase project awareness

D. Arrange for appropriate Legislators, and Administration officials and staff to visit school

III. Monitor

A. Keep abreast and report any legislation affecting KSBE

B. Work with members and staff to positively affect any legislation

IV. Review

A. Status report on strategic plan
   1. Identify problem areas
   2. Pass on suggestions

B. Evaluate success of education

C. Decide on continuing education process or modifying

This is a thumbnail sketch of our proposal to KSBE. We can expand further on the details and add dates as targets if the Trustees feel comfortable with the plan. We would ask for a one year agreement in the amount of $180,000.00, payable in twelve (12) monthly installments.

Please review this proposal with all Trustees, and don't hesitate to call if you have any questions or wish to discuss it further. We look forward to the opportunity of working with KSBE.

Best regards,

Stuart K. Spencer

Stuart K. Spencer

SKS:jrs

10-31-94
TRUSTEES RETREAT

TAB 5 - Develop a training module on KSBE history.

Alternative #3

Decision
- HSI to conduct inservice workshops to all employees.
- ~~Should involve subsidiaries~~ to insure a high quality of instruction delivered in a consistent dependable manner by the same instructor
- Required for all employees.
- 1995-96 School Year
- Integrate Hawaiian Values.
- Kaipo + one other to do this.

- Approved the budget of $25,000.00
- Implemented in 95-96 school year.

Staff report to come in ASAP. by end of November

TAB 6 - Develop and Implement a Semester course on KSBE histor

Grades 9-10 → HAWN CULTURE is required for all students.
Grades 7-8 - A part of ~~the~~ Hawaiian culture
Grades 11-12 → Class is being used for KB histor,
- Total class hours 125 hours

Decision: To develop a 135 hours of content on KSBE history from 7-12

Deposition Exhibit No. 139
Deposition of Lindsey
Date 12-4-99

LLL 000146

TAB 7-8 ESTABLISHING TEACHING LOADS FOR ALL KS PROGRAMS - KES - KIS - KSS

1. Decision - On Exhibit C - Change the summar of SAT scores to the accepted practic of reporting stanine scales.

2. ~~Prop~~ Accepting the report of minimum of 10 & maximum of 20

3. ~~Proposal~~ Recommendation 1:14 teacher-pupil ratio. Mike to come back with impact on the program/classrooms etc. of this recommendation by NOV 30th

TAB 9

1. Prepare Study of Restructuring - Reorganizati or Organization of the total Education Program. Due by the last retreat.

Dr. Ahr - Decision

1. Financial PROJECTIONS for each program
2. 10 yr. period
3. 100% - Current funding
   150% - Current + 1/2
   200% - double
   250% - double + 1/2

LLL 000147

10-31-94
Trustees Retreat

TAB 10 - Elisa

Develop an approach to recognize all persons who participate in KSBE - funded educational programs as alumni of KS.

Approved: these people would be known as KSBE Ohana

TAB 13 - Elisa

- Develop strategies for management's participation in government, community and service organization.
- Start at SR-24
- Oz volunteered to work with Elisa to come up with a proposal.

TAB 12: Accept current study of compensation & benefits & conduct follow-up studies at least biennially

- 4% per year for the next 4 yrs.
- Collapse steps — to ?
- Longevity - every 3 years

Policy Decisions:

~~Recommend~~: Proposals

- If a ~~teacher~~ educator goes on sabbatical they pay for their own tuition, etc.
- If an educator gets a degree outside of their area - then they will not
- Develop an administrative salary step/class chart -

LLL 000148

10-31
TRUSTE[illegible]

Longevity
Retirement - one time plan
Include in proposals.

Lobbying - We will not lobby

LLL 000149

LAW OFFICES
VERNER, LIIPFERT, BERNHARD, McPHERSON AND HAND
Chartered
901 - 15th Street N.W., Suite 700
Washington, D.C. 20005-2301
(202) 371-6000

Telex: 1561792 VERLIP UT
Telecopier: (202) 371-6279

TELECOPIER COVER PAGE

DATE: November 2, 1995

TO: Ernella Kam

COMPANY NAME:

FROM: Norma Wong

ORIGINATOR'S TEL.#.: 808/566-0999

TELECOPIER NO.: 808/536-6895

TOTAL NO. OF PAGES: 10
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CONFIRMATION TEL.

CLIENT/MATTER NO.: 05175-0016

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SPACE FOR ADDITIONAL MESSAGE

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FOR ASSISTANCE CALL TELECOPIER OPERATOR AT (202) 371-6245

Exhibit No. 140
Lindsey
12-4-99

PRIVILEGED AND CONFIDENTIAL
ATTORNEY-CLIENT COMMUNICATION

November 2, 1995

To: KSBE Trustees

From: Mark McConaghey
Denis Dwyer

Re: DRAFT FALL BACK POSITION

Attached is a draft fall back position, with pages numbered in the order of the priority of each item. Plain language explanations of each item will be faxed to arrive by 7:00 a.m. Honolulu time. Page numbers refer to the page numbers legislative bill; footnote numbers refer to the committee report.

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ATTORNEY-CLIENT COMMUNICATION

EXEMPT ALL EDUCATIONAL INSTITUTIONS.

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ATTORNEY-CLIENT COMMUNICATION

STATUTORY LANGUAGE

TAXABLE STANDARD

In determining whether excess benefits are reasonable, the tests and standards developed by the Internal Revenue Service and the courts under section 162 for taxable organizations shall apply to the determination of reasonableness of excess benefits for tax-exempt organizations.

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STATUTORY LANGUAGE

Insert as (c)(3)

SAFE HARBORS

For purposes of determining the reasonableness of any excess benefit under this section, the parties to a transaction can rely upon the reasonableness of a compensatory arrangement with a disqualified person if such arrangement was reviewed and authorized by an independent board or entity (or an independent committee authorized by the board or entity) that:

(1) obtained and relied upon appropriate data as to comparability (e.g., compensation paid by similarly situated taxable organizations for functionally comparable positions; the location of the organization, including the availability of similar specialties in the geographic area; independent compensation surveys by nationally recognized independent firms; or actual written offers from similar institutions competing for the services of the disqualified person); and

(2) adequately documented the basis for its determination (e.g., the record includes an evaluation of the individual whose compensation was being established and the basis for determining that the individual's compensation was reasonable in light of that evaluation and data); and

(3) was composed entirely of--

(i) individuals unrelated to and not subject to the control of the disqualified person(s) involved in the arrangement; or

(ii) members of a state or local judicial body.

Note: Delete Footnote 33

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ATTORNEY-CLIENT COMMUNICATION

STATUTORY LANGUAGE

SAFE HARBOR

Insert as (c)(3)

FALLBACK STATUTORY SAFE HARBOR LANGUAGE

For purposes of this section, a good faith determination by an applicable tax-exempt organization that the value of the consideration (including the performance of services) received equals or exceeds the economic benefit provided shall be controlling unless the Secretary establishes otherwise by clear and convincing evidence.

Note: Delete Footnote 33

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STATUTORY LANGUAGE - REMOVE EXIT TAX

Remove section's provision (g) entitled "TREATMENT OF PREVIOUSLY EXEMPT ORGANIZATIONS", and renumber following subsections.

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<u>ATTORNEY-CLIENT COMMUNICATION</u>

STATUTORY LANGUAGE - MODIFY EXIT TAX

Modify section's provision (g) entitled "TREATMENT OF PREVIOUSLY EXEMPT ORGANIZATIONS"

Add new section (g)(5) to read:

(5) Limitation.--Subsection (g)(1)(B)(i) shall only apply if there is willful and repeated or willful and flagrant and continuing excess benefit transactions

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STATUTORY LANGUAGE - MODIFY EXIT TAX TO ABATEMENT TAX

Subsection (g)(3) is amended by adding at the end thereof the following:

"The Secretary shall abate any unpaid portion of the assessment of any tax imposed by paragraph 2 or any liability in respect thereof, if the attorney general of the state in which the organization is domiciled notifies the Secretary that appropriate action has been taken to correct any excess benefit transaction."

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STATUTORY LANGUAGE - TRANSITION RULE FOR EXIT TAX

Any organization that desires to terminate its tax-exempt status can do so voluntarily until January 1, 1997.

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CONFERENCE REPORT MODIFICATION TO FOOTNOTE 33

The fact that a State or local legislative or agency body may have authorized or approved of a particular compensation package paid to a disqualified person would ~~not~~ be determinative of the reasonableness of compensation paid for purposes of the excise tax penalties provided for by the proposal. Similarly, such authorization or approval would ~~not~~ be determinative of whether a revenue sharing arrangement violates the private inurement proscription.

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CONFERENCE REPORT POSSIBLE MODIFICATIONS

"independent board or entity" language in conference change "approved" to "reviewed and authorized"

AND

Delete the footnote 33 regarding the applicability of state law for determining reasonableness of excess benefit

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STATUTORY LANGUAGE - GOOD FAITH DETERMINATION

Subsection (C)(1)(A) is amended by adding at the end thereof a new sentence, to read as follows:

"The preceding sentence shall not apply to the treatment of any benefit that was made in good faith by such organization."

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ATTORNEY-CLIENT COMMUNICATION

STATUTORY LANGUAGE - JOINT AND SEVERAL LIABILITY

Paragraph (1) of subsection (d) is amended to read as follows:

(1) JOINT AND SEVERAL LABILITY - If more than 1 person is liable for any tax imposed by subsection (a) or subsection (b), all such persons shall be jointly and severally liable for such tax except for the tax imposed under subsections (a)(1) and (b) with respect to compensation for services.

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STATUTORY LANGUAGE - EFFECTIVE DATE

Make the effective date for the application of the intermediate sanctions to tax-exempt organizations the date that the Secretary issues final regulations or the taxable year beginning after December 31, 1997, whichever is later.

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ATTORNEY-CLIENT COMMUNICATION

ADVERTISEMENT
Page 218:

Conference report language footnote 41:

In the case where an advertisement is not a solicitation for funds or contributions, this provision is not intended to require any such statement to be made more than once every six months.

file

VERNER, LIIPFERT, BERNHARD, MCPHERSON AND HAND
CHARTERED

901-15TH STREET, N.W.
WASHINGTON, D.C. 20005-2301
(202) 371-6000
TELECOPIER: (202) 371-6279

PRIVILEGED AND CONFIDENTIAL
ATTORNEY-CLIENT COMMUNICATION

March 23, 1995

MEMORANDUM

To: Trustee Gerry Jervis
Trustee Lokelani Lindsey

From: John Waihee
Sue Temkin

Re: Possible Tax Issues Raised By Additional Questions to KSBE From the Wall Street Journal Dated March 20, 1995

We have reviewed the additional follow-up questions posed to KSBE from the Wall Street Journal. The questions raise various areas of concern regarding allegations of private inurement and unrelated business income. Because of our limited knowledge of relevant factual information, it is not possible at this point in time for us to identify all potential issues.

Private Inurement

Generally, exempt organizations must be organized and operated for charitable and other exempt purposes, dedicating their resources to public benefit as opposed to private interests. The transfer of an exempt organization's financial resources to or for the benefit of an individual by virtue of such individual's relationship with the organization (an "insider") can possibly result in

Deposition Exhibit No. 141
Deposition of Lindsey
Date 2-4-99

private inurement. If private inurement exists, the Internal Revenue Service ("IRS") has the power to revoke the organization's exempt status.

"Insiders" are typically considered to be the organization's trustees, officers, founders, their families and friends. Nonetheless, the IRS has taken the position that any person performing services for an exempt organization can be an insider, such as an employee. Examples of possible private inurement may include but are no way limited to:

(1) Unreasonable and excessive compensation

(2) Unreasonable rental charges

(3) Loan arrangements which are not financially advantageous to the exempt organization or in furtherance of its exempt purposes (i.e. interest free loans)

(4) Favorable investments with and benefits conferred upon business organizations in which an insider has some ownership interest (the IRS is particularly sensitive to networks, affiliations and relationships between the exempt organization and insiders, the manipulation of these arrangements and large direct financial benefits)

Potential private inurement issues are raised by Freedman's questions numbered 4, 5, 8, 11, 13, 23, 24, 26, 28 and 29. The various guaranty arrangements referenced throughout these questions may raise private inurement issues to the extent they relate to insiders upon whom a private benefit has been conferred.

Unrelated Business Income

While a tax exempt organization is permitted to engage in a limited amount of commercial activities, the organization may be subject to an unrelated business income tax ("UBIT") on the income generated from these activities. Moreover, if such commercial activities constitute a substantial part of the organization's total activities, the organization's tax exempt status may be in jeopardy.

Generally, tax exempt organizations can carry on certain passive investment activities without the imposition of UBIT. Certain types of income may be excluded from the definition of UBIT including passive income such as dividends, interest, payments with respect to securities, loans, rental of real estate and gains from the disposition of property. With respect to gains and losses from the sale or disposition of property, the exempt organizations must avoid any characterization of the sales activities as the regular conduct of a trade or business to remain within this exclusion.

Issues involving UBIT are raised by questions numbered 8, 12, 19, 20, 21 and 27.

Potential Attribution of Unrelated Business Income

Where commercial activities become substantial, the tax exempt organization may create a for-profit subsidiary and transfer the assets used for the commercial activities to such entity. The separate existence of the subsidiary should be observed if the subsidiary is established for a bona fide business purpose and the parent, or its officers or representatives, are not involved in the day to day management of the subsidiary. Overlapping officers, trustees and directors sometimes indicate too much control. This could result in a failure to respect the separate corporate existence of the subsidiary. If the corporate subsidiary's existence is ignored, all of the subsidiary's commercial activities may be attributed to the parent. If this happens and the subsidiary's commercial activities are considered a substantial part of the exempt organization's activities, the exempt organization's status can be in jeopardy.

Other issues may arise when funds are transferred between these related organizations. Care must be taken to ensure that the tax exempt organization's funds do not pass through the for-profit entity and benefit private individuals. All arrangements and contracts between the entities should be treated arms length, supported by adequate consideration, properly documented and accounted for by the organizations.

Issues of potential attribution of commercial activities may be raised by questions numbered 8, 12, and 27.

Potential Governmental Inquiry

Questions numbered 4, 21, 22 and 23 appear to be questioning whether special treatment has been received by KSBE from Congress or the Department of Treasury. Both Congress and the Department of Treasury have been reconsidering the current guidelines governing tax exempt organizations and the ability of tax exempt organizations to compete with taxable entities. Negative publicity could prompt a renewed interest in reforming the rules applicable to tax exempt organizations.

It is possible that other questions raise additional concerns. However, our information base prevents us from providing additional analysis of those questions.

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

D. SAKIMOTO
CLERK

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 STIPULATIONS CONCERNING MASTER'S RECOMMENDATIONS (109th, 110th, and 111th ANNUAL ACCOUNTS) and ORDER 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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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 ~~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 112^{th} 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 112^{th} 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 Regulariy 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 <u>Appropriate Performance Measures.</u>

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: <u>Investment Policies Shall Be Reviewed.</u>

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 <u>Strengthened.</u>

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 <u>Properly Documented.</u>

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 <u>Instituted.</u>**

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:

colleen k. hira

Judge of the Above-Entitled Court

SEAL FIRST CIRCUIT COURT STATE OF HAWAII