PRICEWATERHOUSECOOPERS

The William and Flora Hewlett Foundation

Financial Statements
December 31, 2008 and 2007

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers LLP
Three Embarcadero Center
San Francisco CA 94111-4004
Telephone (415) 498 5000
Facsimile (415) 498 7100

Report of Independent Auditors

To The Board of Directors of The William and Flora Hewlett Foundation:

In our opinion, the accompanying statement of financial position and the related statements of activities, changes in net assets and cash flows present fairly, in all material respects, the financial position of The William and Flora Hewlett Foundation (the "Foundation") at December 31, 2008 and 2007, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Foundation's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audit of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

April 10, 2009

The William and Flora Hewlett Foundation
Statements of Financial Position
December 31, 2008 and 2007
(dollars in thousands)

	December 31, 2008	December 31, 2007
Assets		
Cash	$ 4,824	$ 5,820
Investments, at fair value (Notes 3 and 4)	6,156,392	9,195,759
Collateral under securities lending agreement	80,019	22,721
Prepaid expenses and other assets	4,170	2,496
Receivable	12,330	25,660
Fixed assets, net of accumulated depreciation and amortization	31,300	32,461
	$ 6,289,035	$ 9,284,917
Liabilities and Net Assets		
Accounts payable and accrued liabilities	$ 16,218	$ 30,925
Line of credit	40,000	90,000
Accrued post-retirement health care benefit	4,009	3,135
Payable under securities lending agreement	80,019	22,721
Deferred and federal excise tax payable	-	21,438
Grants payable (Note 8)	260,330	242,786
Gifts payable, net of discount (Note 9)	447,860	86,221
Total liabilities	848,436	497,226
Commitments (Note 3)		
Unrestricted net assets	5,423,342	8,759,347
Temporarily restricted net assets	17,257	28,344
Total net assets	5,440,599	8,787,691
	$ 6,289,035	$ 9,284,917

See accompanying notes to the financial statements.

The William and Flora Hewlett Foundation
Statements of Activities and Changes in Net Assets
Years Ended December 31, 2008 and 2007
(dollars in thousands)

	Year Ended December 31, 2008	2007
Unrestricted Net Assets:		
Net investment revenues:		
Interest, dividends and other	$ 104,454	$ 198,893
(Loss) gain on investment portfolio	(2,622,196)	1,131,314
Investment management expense	(31,135)	(27,977)
Net investment (loss) income	(2,548,877)	1,302,230
Tax expense on net investment (loss) income (Note 11)	(3,088)	(28,497)
Net investment (losses) revenues	(2,551,965)	1,273,733
Expenses:		
Grants and gift awarded, net of cancellations	(784,522)	(482,778)
Change in gift discount (Note 9)	28,360	9,779
Direct and other charitable activities	(14,599)	(12,346)
Administrative expenses	(24,514)	(21,799)
Total expenses	(795,275)	(507,144)
(Loss) income before net assets released from time restriction	(3,347,240)	766,589
Net assets released from time restriction	11,236	12,145
Change in unrestricted net assets	(3,336,004)	778,734
Temporarily Restricted Net Assets:		
Change in temporarily restricted net assets:		
Change in value	148	403
Net assets released from time restriction	(11,236)	(12,145)
Net change in temporarily restricted net assets	(11,088)	(11,742)
Change in total net assets	(3,347,092)	766,992
Net assets at beginning of year	8,787,691	8,020,699
Net assets at end of year	$ 5,440,599	$ 8,787,691

See accompanying notes to the financial statements.

The William and Flora Hewlett Foundation
Statements of Cash Flows
Years Ended December 31, 2008 and 2007
(dollars in thousands)

	Year Ended December 31, 2008	Year Ended December 31, 2007
Cash flows used in operating activities:		
Interest and dividends received	$ 123,970	$ 194,825
Cash paid for federal excise tax	(8,006)	(8,439)
Cash paid to suppliers and employees	(82,183)	(43,926)
Cash contributions paid	(11,205)	(12,145)
Grants and gifts paid	(376,979)	(426,195)
Net cash used in operating activities	(354,403)	(295,880)
Cash flows from investing activities:		
Purchases of fixed assets	(812)	(1,176)
Cash received from partnership distributions	388,947	413,735
Proceeds from sale of investments	47,578,796	23,632,749
Purchase of investments	(47,563,524)	(23,838,086)
Net cash from investing activities	403,407	207,222
Cash flows from financing activities:		
Cash received from line of credit	40,000	90,000
Cash paid on line of credit	(90,000)	-
Net cash (used) from financing activities	(50,000)	90,000
Net (decrease) increase in cash	(996)	1,342
Cash at beginning of year	5,820	4,478
Cash at end of year	$ 4,824	$ 5,820

See accompanying notes to the financial statements.

The William and Flora Hewlett Foundation
Statements of Cash Flows, continued
Years Ended December 31, 2008 and 2007
(dollars in thousands)

	Year Ended December 31, 2008	2007
Reconciliation of change in net assets to net cash used in operating activities:		
Change in total net assets	$ (3,347,092)	$ 766,992
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Depreciation and amortization on fixed assets	1,663	1,763
Loss on disposal of fixed assets	310	525
Change in value of gift payable	(28,360)	(9,779)
Net unrealized and realized loss (gain) on investments	2,622,196	(1,131,314)
(Decrease) increase in deferred and federal excise tax	(21,438)	3,047
Increase (decrease) in accrued post-retirement health care benefit	874	(485)
(Increase) decrease in value of receivable	(118)	38
Changes in operating assets and liabilities:		
Decrease (increase) in interest and dividends receivable	13,070	(4,055)
(Increase) decrease in prepaid expenses and other assets	(1,674)	1,421
Decrease in Gates and other receivable	13,330	4,426
(Decrease) increase in accounts payable and accrued liabilities	(14,707)	14,958
Increase in grants payable	17,544	49,059
Increase in gift payable	389,999	7,524
Net cash used in operating activities	$ (354,403)	$ (295,880)

See accompanying notes to the financial statements.

1. The Organization

The William and Flora Hewlett Foundation (the "Foundation") is a private foundation incorporated in 1966 as a non-profit charitable organization. The Foundation's grantmaking activities are concentrated in the program areas of education, environment, performing arts, population and global development. More detailed information regarding the Foundation's charitable activities can be obtained from the Foundation's website at www.hewlett.org.

2. Significant Accounting Policies

Basis of presentation

The accompanying financial statements have been prepared on the accrual basis of accounting.

Investments

Investments in stocks and bonds which are listed on national securities exchanges, quoted on NASDAQ or on the over-the-counter market are valued at the last reported sale price, or in the absence of a recorded sale, at the value between the most recent bid and asked prices. Futures, forwards, swaps and options which are traded on exchanges are valued at the last reported sale price or, if they are traded over-the-counter, at the most recent bid price. Index and credit swaps, which gain exposure to equities and fixed income securities in a leveraged form, are traded with a counterparty and are valued at each month end. Equity swaps are valued based on the last reported price of the relevant index or ETF. Fixed income swaps are valued at the last reported sale price, or in the absence of a recorded sale, at a value between the most recent bid and asked prices. Short-term investments are valued at amortized cost, which approximates market value. Since there is no readily available market for investments in limited partnerships, such investments are valued at amounts reported to the Foundation by the general partners of such entities. The investments of these limited partnerships, such as venture capital, buyout firms and real estate partnerships, include securities of companies that are not immediately liquid. Accordingly, their values are based upon guidelines established by the general partners. The valuations of the investments in limited partnerships are based upon the value determined by each partnership's general partner as of December 31. Management believes this method provides a reasonable estimate of fair value. These values may differ significantly from values that would have been used had a readily available market existed for such investments, and the differences could be material to the change in net assets of the Foundation.

Investment transactions are recorded on trade date. Realized gains and losses on sales of investments are determined on the specific identification basis.

Foreign currency amounts are translated into U.S. dollars based upon exchange rates as of December 31. Transactions in foreign currencies are translated into U.S. dollars at the exchange rate prevailing on the transaction date.

Cash equivalents consist of money market mutual funds and foreign currency held for investment purposes, with an original maturity when purchased of three months or less.

Cash

Cash consists of funds held in commercial interest-bearing accounts, for operating expenses.

Fixed Assets

Fixed assets are recorded at cost and depreciated using the straight-line basis over their estimated useful lives. The headquarters building and associated fixtures are generally depreciated using the straight-line basis over ten to fifty years. Furniture and computer and office equipment are depreciated over estimated useful lives of three to ten years.

Net Asset Classification

The Foundation's activities and related assets and liabilities are classified as unrestricted and temporarily restricted according to the terms of the various contributions. The Foundation has no permanently restricted net assets.

Unrestricted balances consist of funds undesignated and currently available for all Foundation activities. Temporarily restricted balances consist of funds available for support of the Foundation’s activities, which are expendable only for purposes specified by the donor or within a specified period.

The net assets included in the temporarily restricted class at December 31, 2008 relate to a donor-restricted contribution for which the requirements have not yet been met.

Grants

Grants are accrued when awarded by the Foundation.

Administrative Expenses

Administrative expenses represent those expenses incurred in managing programs funded by the Foundation. Expenses associated with managing programs funded by other organizations are reimbursed at the time they are incurred.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of changes in net assets during the reporting period. Actual results could differ from those estimates.

Reclassifications

Certain reclassifications have been made to the 2007 balances to conform to the 2008 presentation of tax expenses and investment assets. These reclassifications had no effect on the change in net assets in 2007 or total net assets at December 31, 2007.

(dollars in thousands)

Recent Accounting Pronouncements

In July 2006, FASB issued Financial Accounting Standards Board Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" (FIN 48), an interpretation of SFAS No. 109, "Accounting for Income Taxes". FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken in an organization's tax return. The Foundation adopted FIN 48 effective January 1, 2008. The Foundation believes that it has appropriate support for the excise tax positions taken and, as such, does not have any uncertain tax positions that result in a material impact on the Foundation's financial position or statement of activities.

In March 2008, FASB issued Statement of Financial Accounting Standards No. 161, "Disclosures about Derivative Instruments and Hedging Activities" (FAS 161), an amendment of FASB No. 133. FAS 161 requires enhanced disclosures to provide additional information regarding the accounting treatment for derivatives and hedging activities, the reasons the Foundation's managers invest using derivative instruments, and the effect derivatives have on the Foundation's financial statements. FAS 161 is effective for reporting periods beginning after November 15, 2008. The Foundation intends to adopt FAS 161 effective January 1, 2009 and does not believe the adoption of FAS 161 will materially impact the financial statement amounts, but will require additional disclosures.

3. Investments

The Foundation's investment portfolio, at December 31 consists of the following:

	2008	2007
Investments, at fair value		
Hewlett-Packard and Agilent common stock	$ 266,254	$ 445,565
Global equities	1,800,972	3,761,521
Private equities, real assets and absolute return	2,503,539	2,889,726
Fixed income	2,386,122	3,191,410
Net payable on forward fixed income transactions	(844,080)	(1,093,621)
Cash equivalents	164,646	141,882
Net payable from unsettled securities purchases and sales	(98,517)	(165,183)
Other	(22,544)	24,459
Total	$ 6,156,392	$ 9,195,759

The investment goal of the Foundation is to maintain or grow its asset size and spending power in real (inflation adjusted) terms with risk at a level appropriate to the Foundation's program objectives. The Foundation diversifies its investments among various financial instruments and asset categories, and uses multiple investment strategies. As a general practice, except for the Foundation's holdings in Hewlett-Packard and Agilent stock and certain index swaps, all financial assets of the Foundation are managed by external investment management firms selected by the Foundation. All financial assets of the Foundation are held in custody by a major commercial bank, except for assets invested with partnerships, commingled funds, the overlay swaps and call options, and the covered call program, which have separate arrangements related to their legal structure.

(dollars in thousands)

The majority of the Foundation's assets are invested in equities, which are listed on national exchanges, quoted on NASDAQ, or in the over-the-counter market; treasury and agency bonds of the U.S. government; and investment grade corporate bonds for which active trading markets exist. Net realized and unrealized gains and losses on investments are reflected in the Statements of Activities and Changes in Net Assets.

Global equities include those held directly by the Foundation and those held in commingled entities including partnerships and trusts. At December 31, 2008 and 2007, global equities held in partnerships and trusts were $817,431 and $1,448,262.

The loss or gain on the Foundation's investment portfolio for the years ended December 31, 2008 and 2007 consists of the following:

	2008	2007
Net realized (loss) / gain	$ (208,286)	$ 669,230
Net unrealized (loss) / gain	(2,413,910)	462,084
	$ (2,622,196)	$1,131,314

Approximately 41 percent of the Foundation's investments at December 31, 2008 were invested with various limited partnerships that invest in the securities of companies that are not immediately liquid, such as venture capital and buyout firms, and in real estate limited partnerships or private REITs that have investments in various types of properties. As of December 31, 2008 the Foundation is committed to contribute approximately $2,297,708 in additional capital in future years to various partnerships.

Investment securities are exposed to various risks, such as changes in interest rates or credit ratings and market fluctuations. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is possible that the value of the Foundation's investments and total net assets balance could fluctuate materially.

Legal, tax and regulatory changes could occur during the term of the Foundation's fund investments. The regulatory environment for private equity and hedge funds is evolving, and changes in the regulation of these funds may adversely affect the value of investments held by the Foundation. The Foundation believes that the effect of any future regulatory change on the Foundation's assets would not be substantial.

The Foundation maintains a custody account with its primary custodian, The Bank of New York Mellon Corporation (BNY Mellon). Although the Foundation monitors BNY Mellon and believes that it is an appropriate custodian, there is no guarantee that BNY Mellon, or any other custodian that the Foundation may use from time to time, will not become insolvent. The Foundation believes that, in the event of the insolvency of its custodian, some of the Foundation's assets may be unavailable for a period of time, but that it would ultimately have full recovery of its assets.

The investments of the Foundation include a variety of financial instruments involving contractual commitments for future settlements, including futures, swaps, forwards and options which are exchange traded or are executed over-the-counter. Some investment managers retained by the Foundation have been authorized to use certain financial derivative instruments in a manner set forth by either the Foundation's written investment policy, specific manager guidelines or partnership/fund agreement documents. Specifically, financial derivative instruments may be used for the following purposes: (1) currency forward contracts and options may be used to hedge nondollar exposure in foreign investments, or to take positions in managed currency portfolios; (2) futures and swap contracts may be used to rebalance asset categories within the portfolio or to manage market exposures in managed portfolios; and (3) futures contracts, swaps and options may be used to hedge or leverage positions in managed portfolios. Financial derivative instruments are recorded at fair value in the Statements of Financial Position with changes in fair value reflected in the Statements of Activities and Changes in Net Assets.

The total value of investments pledged with respect to options and futures contracts at December 31, 2008 and 2007 was $22,067 and $14,884, respectively. The value of restricted cash held at brokers as collateral for variation margin at December 31, 2008 and 2007 was $22,282 and $10,941 respectively.

Certain of the Foundation's managers purchase or sell fixed income securities on a delayed delivery or forward settled basis. These transactions involve a commitment by the Foundation to purchase or sell securities for a predetermined price or yield, with payment and delivery taking place beyond the customary settlement period, from about 1 to 3 months. When purchasing a security on a delayed delivery basis, the Foundation assumes the rights and risks of ownership of the security, including the risk of price and yield fluctuations, and reflects such fluctuations in its net assets. The manager may dispose of or renegotiate a delayed delivery transaction after it is entered into, and may sell the securities before they are delivered, which may result in a capital gain or loss. At December 31, 2008 and 2007 the net liability for these forward purchases and sales was $844,080 and $1,093,621 respectively.

Premiums received with respect to open options contracts at December 31, 2008 and 2007 were $13,640 and $5,908, respectively.

Other investment assets of $(22,544) and $24,459 at December 31, 2008 and 2007, respectively, consist of receivables for interest and dividends and certain derivatives held at fair market value. At December 31, 2008 and 2007 these derivatives included swap contracts, futures contracts, foreign exchange contracts, covered call options and put and call options, as shown in the table on the following page.

In the opinion of the Foundation's management, the use of financial derivative instruments in its investment program is appropriate and customary for the investment strategies employed. Using those instruments reduces certain investment risks and may add value to the portfolio. The instruments themselves, however, do involve investment and counterparty risk in amounts greater than what are reflected in the Foundation's financial statements. Management does not anticipate that losses, if any, from such instruments would materially affect the financial position of the Foundation.

Fair values of the Foundation's derivative financial instruments at December 31, 2008 and 2007 are summarized in the following table. This table excludes exposures relating to derivatives held indirectly through commingled funds.

Derivative Financial Instruments		**December 31** **2008** Fair Value (in thousands)		**2007** Fair Value (in thousands)
- Equity contracts:				
Futures and swap contracts				
Assets	$	2,809	$	190
Put and call options:				
(Liabilities) / Assets	$	(7,814)	$	698
Covered call options:				
Liabilities	$	(221)	$	(1,145)
- Fixed income contracts:				
Futures and swap contracts				
Liabilities	$	(2,253)	$	(6,723)
Put and call options:				
Liabilities	$	(2,121)	$	(667)
Forward net purchases and sales				
Liabilities	$	(844,080)	$	(1,093,621)
- Foreign currency contracts:				
Forward contracts				
Unrealized gain on currency contracts	$	9,926	$	40,100
Unrealized loss on currency contracts	$	(22,980)	$	(23,618)

The Foundation may engage in securities lending. During the term of the loan, the Foundation continues to receive any dividends, or amounts equivalent thereto, on the loaned securities. The loans are secured by collateral whose par value is at least equal to the market value of the loaned securities. The collateral is adjusted daily based on current market values. Investment of this collateral is in accordance with specified guidelines, and the collateral is marked to market daily. Cash collateral received for securities on loan has been invested in the BNY Mellon GSL DBT II Collateral Fund ("DBT II"), a collateral investment pool managed by the securities lending agent. Income generated from the investment of cash collateral, net of negotiated rebate fees paid to borrowers and transaction costs, is divided 75/25 between the Foundation and the securities lending agent. The Foundation's share of this securities lending income is disclosed as stock loan income in the Statement of Activities and Changes in Net Assets. Loans are subject to termination at the option of the borrower or the Foundation. Upon termination of the loan, the borrower returns to the lender securities identical to the loaned securities. The Foundation bears the risk of delay in recovery of, or even loss of rights in, the securities loaned should the borrower of the securities fail financially. The Foundation also bears the risk of loss in the event the securities purchased with cash collateral depreciate in value.

At December 31, 2008 and 2007, the market value of securities on loan was $76,474 and $21,430 respectively. In connection therewith, the Foundation received cash collateral of $80,019 and $22,721 respectively, which has been invested. As of December 31, 2008, the fair value of the Foundation's collateral holdings was $75,087. The Foundation recorded an unrealized loss of $4,783 related to the decrease in fair value of its holdings in the collateral investments. In September 2008, the Foundation's proportionate holdings in the DBT II collateral pool were placed in a separately managed liquidating trust and are managed on behalf of the Foundation by the securities lending agent.

As of December 31, 2008 and 2007, the Foundation earned $1,227 and $1,090, respectively, in securities lending income.

At December 31, 2008, the Foundation's net receivable from unsettled securities purchases and sales includes a receivable from brokers of $1,495,349 and a payable to brokers of $1,593,866. At December 31, 2007, the net receivable from unsettled securities purchases and sales included a receivable from brokers of $462,826 and a payable to brokers of $628,009.

The Foundation held 5.1 million shares of Hewlett-Packard Company ("Hewlett-Packard") stock with a market price of $36.29 per share at December 31, 2008. At December 31, 2007, the Foundation held 5.3 million shares with a market price of $50.48 per share. The Foundation held 4.8 million shares of Agilent Company ("Agilent") stock with a market price of $15.63 per share at December 31, 2008. At December 31, 2007, the Foundation held 4.8 million shares of Agilent stock with a market price of $36.74.

The Foundation's investment managers enter into credit default swaps, generally to simulate long and short bond positions that are either unavailable or considered to be less attractively priced in the bond market. The Foundation managers use these swaps to reduce risk where the Foundation has exposure to the issuer, or to take an active long or short position with respect to the likelihood of an event of default. The reference obligation of the swap can be a single issuer, a "basket" of issuers, or an index. The underlying referenced assets are typically corporate debt, sovereign debt and asset backed securities.

The buyer of a credit default swap is generally obligated to pay the seller a periodic stream of payments over the term of the contract in return for a contingent payment upon the occurrence of a credit event with respect to an underlying reference obligation. If a credit event occurs, the seller typically must pay the contingent payment to the buyer, which is typically the par value (full notional value) of the reference obligation, though the actual payment may be mitigated by terms of the International Swaps and Derivative Agreement ("ISDA"), allowing for netting arrangements and collateral.

(dollars in thousands)

The contingent payment may be a cash settlement or a physical delivery of the reference obligation in return for payment of the face amount of the obligation. If the Foundation's investment manager is a buyer and no credit event occurs, the Foundation may lose its investment and recover nothing. However, if a credit event occurs, the buyer typically receives full notional value for a reference obligation that may have little or no value. As a seller, the Foundation receives a fixed rate of income throughout the term of the contract, which typically is between one month and five years, provided that no credit event occurs. If a credit event occurs, the seller may be obligated to pay the buyer an amount up to the full notional value of the reference obligation.

As of December 31, 2008, the Foundation is the buyer ("receiving protection") on a total notional amount of $41,643 and is the seller ("providing protection") on a total notional amount of $284,903. The notional amounts of the swaps are not recorded in the financial statements; however the notional amount does approximate the maximum potential amount of future payments that the Foundation could be required to make if the Foundation were the seller of protection and a credit event were to occur. Those credit default swaps for which the Foundation is providing protection at December 31, 2008 are summarized as follows:

Written Credit Derivative Contracts	**Single Name Credit Default Swaps**		**Credit Default Swap Index**		
Reference Asset:	**Corporate Debt**	**Sovereign Debt**	**Asset Backed Securities**	**Corporate Debt**	**Total**
Fair value of written credit derivatives	$ (2,583)	$ (449)	$ (6,085)	$ (3,277)	$ (12,394)
Maximum potential amount of future payments	$ 111,300	$ 13,200	$ 19,060	$ 141,343	$284,903
Recourse provisions with 3rd parties to recover any amounts paid under the credit derivative				$ 13,743	$ 13,743

Maximum Potential Amount of Future Payments By Contract Term

	0-12 months	**1-5 years**	**5-10 years**	**Over 10 years**	**Total**
Current rating on underlying :					
AAA		$ 86,765	$ 13,281	$ 19,060	$ 119,106
AA		20,527			20,527
A		32,600	20,000		52,600
BBB		70,238	6,832		77,070
<BBB		15,600			15,600
Total	-	$ 225,730	$ 40,113	$ 19,060	$ 284,903

(dollars in thousands)

4. Valuation of Investments - SFAS 157

In September 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* ("SFAS 157"), which is effective for the Foundation's fiscal year beginning January 1, 2008. SFAS 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. The new standard provides a consistent definition of fair value which focuses on an exit price between market participants in an orderly transaction as prescribed by SFAS 157. The standard also prioritizes, within the measurement of fair value, the use of market-based information over entity-specific information and establishes a three-level hierarchy for fair value measurements based on the transparency of information used in the valuation of an asset or liability as of the measurement date.

Investments measured and reported at fair value are classified and disclosed in one of the following categories:

Level I – Quoted prices are available in active markets for identical investments as of the reporting date. The type of investments in Level I include listed equities held in the name of the Foundation, and exclude listed equities and other securities held indirectly through commingled funds.

Level II – Pricing inputs, including broker quotes, are generally those other than exchange quoted prices in active markets, which are either directly or indirectly observable as of the reporting date, and fair value is determined through the use of models or other valuation methodologies.

Level III – Pricing inputs are unobservable for the investment and includes situations where there is little, if any, market activity for the investment. The inputs into the determination of fair value require significant management judgment or estimation. Investments that are included in this category generally include privately held investments and partnership interests.

The following table summarizes the valuation of the Foundation's investments by the SFAS 157 fair value hierarchy levels as of December 31, 2008:

		Alternative Assets			
	Equities & Fixed Income	Private Equity	Real Assets	Absolute Return	Total Investment Assets
Level I	$ 214,146				$ 214,146
Level II	1,283,643				1,283,643
Level III	2,155,064	923,735	879,023	700,781	4,658,603
	$ 3,652,853	$ 923,735	$ 879,023	$700,781	$ 6,156,392

(dollars in thousands)

Level 1 includes equities and fixed income held by the Foundation, and these are also offset by certain items including outstanding payables and receivables at year end; once netted, these sum to $214,146.

The following table summarizes the Foundation's level III reconciliation by the SFAS 157 standards as of December 31, 2008:

		Level III
Investments, at fair value		
Balance at December 31, 2007	$	5,839,397
Total net realized appreciation included in net income		81,444
Total net unrealized (loss) included in net income		(1,707,937)
Purchases of portfolio investments		4,944,207
Proceeds from sales, redemptions, and distributions		(4,886,853)
Transfer in and/or out of Level III		388,345
Balance at December 31, 2008	$	4,658,603

The amount of total losses for the period included in the statement of activities attributable to the change in unrealized losses relating to assets still held at the reporting date is ($491,196).

5. Receivable

In 2006 the Foundation entered into an agreement with the Bill and Melinda Gates Foundation to administer a program charged with improving quality education in developing countries. In addition to reimbursing associated administrative expenses, the Bill and Melinda Gates Foundation pledged $40,000 over five years to the William and Flora Hewlett Foundation to do grant-making in this area; this contribution was reported as a change in temporarily restricted net assets during 2006. $4,340 of this pledge was received during 2007, and $13,330 was received during 2008. $12,330 is reported as a receivable at December 31, 2008.

The Foundation is the residuary beneficiary of the Hewlett Marital Trust. As of December 31, 2008, the assets which the Foundation is entitled to receive are not material and cannot be reasonably estimated.

(dollars in thousands)

6. Fixed Assets

Fixed assets consist of the following at December 31, 2008 and 2007:

	2008	2007
Building, land lease and land improvements	$ 34,190	$ 34,277
Furniture and fixtures	5,262	4,654
Computer and office equipment	2,147	3,274
	41,599	42,205
Less accumulated depreciation and amortization	(10,299)	(9,744)
	$ 31,300	$ 32,461

7. Postretirement Healthcare Benefit

The Foundation adopted Statement No. 158 of the Financial Accounting Standards Board, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" and recognizes the accumulated liability for its postretirement healthcare benefit obligation, effective January 1, 2007.

The changes in postretirement healthcare benefit obligation, plan assets, and the amounts recognized in the financial statements are as follows:

	2008	2007
Change in postretirement healthcare benefit obligation (APBO):		
Postretirement benefit obligation as of January 1	$ 3,135	$ 2,928
Service cost	487	465
Interest cost	228	192
Actuarial loss (gain)	195	(423)
Benefits paid by employer	(36)	(27)
Accrued postretirement benefit cost as of December 31	$ 4,009	$ 3,135

By Foundation policy, the postretirement healthcare benefit plan is not funded.

Change in plan assets:		
Fair value of plan assets as of January 1	$ -	$ -
Actual return on plan assets	-	-
Company contributions	36	27
Participants contributions	-	-
Benefits paid	(36)	(27)
Fair value of plan assets as of December 31	$ -	$ -

(dollars in thousands)

	2008	2007
Amount recognized in Statement of Financial Position as of December 31:		
Accrued postretirement healthcare benefit cost	$ 4,009	$ 3,135
Assets	-	-
Net amount recognized	$ 4,009	$ 3,135
Amounts included in unrestricted net assets:		
Unrecognized prior service cost	$ -	$ -
Unrecognized net gain	(743)	(1,059)
Net gain included in unrestricted net assets	$ (743)	$ (1,059)
Net periodic postretirement healthcare benefit cost:		
Service cost	$ 487	$ 465
Interest cost	228	192
Expected return on plan assets		
Amortization of prior service cost		
Amortization of unrecognized net gain	(120)	(57)
Net periodic postretirement healthcare benefit cost:	595	600
Other changes recognized in unrestricted net assets:		
Net loss (gain)	315	(366)
Prior service cost	-	-
Amortization of prior service cost	-	-
Total recognized in unrestricted net assets	315	(366)
Total recognized net periodic benefit cost and unrestricted net assets	$ 910	$ 234

The prior service costs and net actuarial gain expected to be amortized from change in net assets to net periodic benefit expense over the next fiscal year are as follows:

Net actuarial gain	$ (49)
Prior service cost	-

Actuarial Assumptions:

The weighted average discount rate assumptions used for the Post Retirement Health Benefit plan are shown below:

Discount rate to determine benefit obligations	6.00%	6.50%
Discount rate to determine the net periodic benefit cost	6.50%	5.75%

(dollars in thousands)

To determine the accumulated postretirement healthcare benefit obligation as of December 31, 2008, an 11% annual rate of increase in per capita costs of covered health care was assumed for 2008-2009, declining gradually to 6% by 2013 and remaining at this rate thereafter.

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. Increasing the health care cost trend rate by 1% in each future year would increase the accumulated postretirement healthcare benefit obligation by $706, and the aggregate annual service and interest cost by $151. Decreasing the health care cost trend rate by 1% in each future year would decrease the accumulated postretirement healthcare benefit obligation by $574, and the aggregate annual service and interest cost by $121.

Expected contributions:

The Foundation expects to contribute $43 in postretirement healthcare benefits during the fiscal year ending December 31, 2009.

Expected benefit payments:

The following benefit payments, which reflect expected future service, are expected to be paid for the fiscal years ending December 31:

Fiscal Year	Expected Benefit Payments
2009	$ 43
2010	67
2011	82
2012	133
2013	175
2014-2018 (aggregate)	1,660

8. Grants Payable

Grant requests are recorded as grants payable when they are awarded. Some of the grants are payable in installments, generally over a two or three-year period. Grants authorized but unpaid at December 31, 2008 are payable as follows:

Year Payable	Amount
2009	$ 200,267
2010	36,063
2011 and thereafter	24,000
	$ 260,330

(dollars in thousands)

9. Gifts Payable

The Foundation made a commitment of $113,000 in August of 2007 to University of California, Berkeley, over seven years, for a challenge grant to endow 100 faculty chairs and for the creation of an in-house investment company. The obligation was discounted to a net present value as of December 31, 2008 using a discount rate of 4.26 %. Payments of $10,000 and $17,000 were made in 2008 and 2007, respectively.

The Foundation made a commitment of $461,095 in July of 2008 to ClimateWorks Foundation for an initiative to mitigate global climate change. This obligation is expected to be paid over a period of five years and was discounted to a net present value as of December 31, 2008 using a discount rate of 3.19%. Payment of $61,095 on this grant was made in 2008.
The total gifts payable at December 31, 2008, net of discount, is as follows:

	2008	2007
Gifts payable	$ 486,000	$ 96,000
Less unamortized discount	(38,140)	(9,779)
Gift payable, net of discount	$ 447,860	$ 86,221

10. Credit Facility

The Foundation has a collateralized revolving line of credit ("LOC") of $90,000 with BNY Mellon. This LOC note does not have an expiration date. At December 31, 2008 and 2007 the outstanding principal balance on the line of credit was $40,000 and $90,000, respectively. The interest rate on the LOC is variable and is indexed to the one month London Interbank Offered Rate ("Libor").

11. Federal Excise and Unrelated Business Income Tax

The William and Flora Hewlett Foundation is a private foundation and qualifies as a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code and corresponding California provisions. Private foundations are subject to a federal excise tax on net investment income and may reduce their federal excise tax rate from 2% to 1% by exceeding a certain payout target for the year. The Foundation qualified for the 1% tax rate in 2008. Each year, current federal excise tax is levied on interest and dividend income and net realized gains of the Foundation; net investment losses do not reduce investment income. At December 31, 2008 and 2007, deferred federal excise tax is provided at 1.5% and 1.33%, respectively, which is the average effective rate expected to be paid on unrealized gains on investments. The income from certain investments is subject to unrelated business income tax.

(dollars in thousands)

The expense for federal excise tax is as follows:

	2008	2007
Current	$ 5,302	$ 7,900
Deferred	(20,643)	3,047
	$ (15,341)	$ 10,947

The expense for unrelated business income tax is as follows:

	2008	2007
	$ 18,429	$ 17,555