

In the opinion of McCorrison Miller Mukai MacKinnon, Bond Counsel, under existing law and assuming compliance with certain covenants and the accuracy of certain representations, interest on the 2003 Bonds is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations, although interest on the 2003 Bonds is included in the adjusted current earnings of certain corporations in computing their alternative minimum tax liability. Bond Counsel is of the further opinion that the 2003 Bonds and the income therefrom are exempt from taxation by the State of Hawaii or any political subdivision thereof, except for inheritance, transfer, estate and certain franchise taxes. Bond Counsel expresses no opinion regarding any other tax consequences related to the ownership or disposition of the 2003 Bonds or the accrual or receipt of interest thereon. See "TAX MATTERS" herein.

\$44,940,000
STATE OF HAWAII
Highway Revenue Bonds
Refunding Series 2003

Dated: Date of Delivery

Due: July 1, as shown on inside cover

The Refunding Series 2003 Bonds (the "2003 Bonds") are being issued for the purpose of providing funds to refund certain outstanding Highway Revenue Bonds of the State of Hawaii (the "State"). The 2003 Bonds are special limited obligations of the State, payable solely from and secured by the Pledged Funds under the Certificate as described herein, consisting principally of highway fuel license taxes, vehicle registration fees, vehicle weight taxes and rental motor vehicle and tour vehicle surcharge taxes, as more fully described in this Official Statement.

The 2003 Bonds are issuable in fully registered form and when initially issued will be registered in the name of Cede & Co., as nominee of The Depository Trust Company ("DTC"), New York, New York. So long as DTC or its nominee is the registered owner of the 2003 Bonds, purchases of the 2003 Bonds will be made in book-entry form only, through brokers and dealers who are, or who act through, DTC participants; beneficial owners of the 2003 Bonds will not receive physical delivery of Bond certificates; payment of the principal of and interest on the 2003 Bonds will be made directly to DTC or its nominee; and disbursement of such payments to DTC participants will be the responsibility of DTC and disbursement of such payments to the beneficial owners will be the responsibility of DTC participants (See "BOOK-ENTRY SYSTEM" herein). Purchases of the 2003 Bonds may be made in the denomination of \$5,000 or any integral multiple thereof.

Interest on the 2003 Bonds is payable on each January 1 and July 1 commencing July 1, 2003. The 2003 Bonds are not subject to optional redemption prior to maturity.

The 2003 Bonds do not constitute a general or moral obligation of the State nor a charge upon the general fund of the State. The full faith and credit of the State are not pledged to the payment of the principal of or interest on the 2003 Bonds.

The 2003 Bonds are being issued pursuant to the Certificate of the Director of Transportation Providing for the Issuance of State of Hawaii Highway Revenue Bonds, dated as of August 1, 1993, as supplemented.

The scheduled payment of principal of and interest on the 2003 Bonds maturing on July 1, 2005 bearing interest at 3.000% and on July 1 of the years 2006 through 2013, inclusive (the "Insured Bonds") when due will be guaranteed by an insurance policy issued concurrently with the delivery of the 2003 Insured Bonds by Financial Security Assurance Inc.



The scheduled payment of principal of and interest on the 2003 Bonds maturing on July 1, 2004 and July 1, 2005 bearing interest at 2.5000% (the "Uninsured Bonds") when due will not be guaranteed by the aforementioned insurance policy.

This cover page contains certain information for quick reference only. It is not a summary of this issue. Investors must read the entire Official Statement to obtain information essential to the making of an informed investment decision.

MATURITY SCHEDULE-See Inside Cover Page

The 2003 Bonds are offered when, as and if issued and received by the Underwriter, subject to prior sale or withdrawal or modification of the offer without notice, and to the approval of legality by McCorrison Miller Mukai MacKinnon LLP, Honolulu, Hawaii, Bond Counsel. Certain legal matters will be passed upon for the Underwriter by its counsel, Pillsbury Winthrop LLP, New York, New York. It is expected that the 2003 Bonds in definitive book-entry form will be available for delivery on or about April 15, 2003.

A.G. Edwards & Sons, Inc.

Dated March 25, 2003

\$44,940,000
STATE OF HAWAII
Highway Revenue Bonds
Refunding Series 2003

MATURITY SCHEDULE

<u>Bond Component</u>	<u>Maturity Date</u>	<u>Principal</u>	<u>Interest</u>	<u>Yield</u>
Uninsured Serial Bonds:				
	7/1/2004	\$3,875,000	2.000%	1.250%
	7/1/2005	455,000	2.500%	1.670%
Insured Serial Bonds:				
	7/1/2005	3,505,000	3.000%	1.630%
	7/1/2006	4,025,000	2.500%	1.990%
	7/1/2007	2,245,000	2.500%	2.430%
	7/1/2007	1,930,000	4.500%	2.430%
	7/1/2008	2,310,000	3.000%	2.810%
	7/1/2008	2,000,000	4.500%	2.810%
	7/1/2009	1,200,000	3.125%	3.150%
	7/1/2009	3,280,000	5.000%	3.150%
	7/1/2010	750,000	3.500%	3.460%
	7/1/2010	4,000,000	4.500%	3.460%
	7/1/2011	4,900,000	4.500%	3.700%
	7/1/2012	5,105,000	5.000%	3.840%
	7/1/2013	1,360,000	4.000%	3.950%
	7/1/2013	4,000,000	5.250%	3.950%
		\$44,940,000		

No dealer, broker, salesman or other person has been authorized to give any information or to make any representations, other than those contained in this Official Statement, in connection with the offering of the 2003 Bonds described in this Official Statement, and, if given or made, such information or representations must not be relied upon as having been authorized by the State of Hawaii or the Underwriter. This Official Statement does not constitute an offer to sell the 2003 Bonds or a solicitation of an offer to buy by any person, nor shall there be any sale of the 2003 Bonds by any person, in any jurisdiction in which it is unlawful for such person to make such offer, solicitation or sale. The information set forth in this Official Statement has been furnished by the State and other sources which are believed to be reliable but it is not guaranteed as to accuracy or completeness, and is not to be construed as a representation, by the Underwriter. The information and expressions of opinion in this Official Statement are subject to change without notice and neither the delivery of the Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the State since the date of this Official Statement.

Other than with respect to information concerning Financial Security Assurance Inc. ("Financial Security") contained under the caption "INSURANCE," Appendix G - "SPECIMEN OF THE BOND INSURANCE POLICY" and Appendix H - "SPECIMEN OF THE DEBT SERVICE RESERVE INSURANCE POLICY" herein, none of the information in the Official Statement has been supplied or verified by Financial Security and Financial Security makes no representation or warranty, express or implied, as to (i) the accuracy or completeness of such information; (ii) the validity of the 2003 Bonds; or (iii) the tax exempt status of the interest on the 2003 Bonds.

IN CONNECTION WITH THIS OFFERING THE UNDERWRITER MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF THE 2003 BONDS OFFERED HEREBY AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

STATE OF HAWAII

Linda Lingle, Governor

James R. Aiona, Jr., Lieutenant Governor

DEPARTMENT OF TRANSPORTATION

Rodney K. Haraga, Director

Acting Deputy Director
Administrator, Airports Division
Administrator, Harbors Division
Administrator, Highways Division

Glenn M. Okimoto
Davis Yogi
Glenn M. Okimoto
Glenn M. Yasui

COMMISSION ON TRANSPORTATION

Willy Crozier, Chair
Lester Fushikoshi, Vice-Chair
Rudy Miranda
Norman K. Tsuji
James C. Pacopac
Kazu Hayashida

Jane N. Yamashiroya
Stephen E. Smith
David W. Rae
Alfred Wong
Kirk T. Tanaka
Harold K. Kageura

SPECIAL SERVICES

Department of Budget and Finance
of the State of Hawaii
Honolulu, Hawaii
Paying Agent and Registrar

McCorriston Miller Mukai MacKinnon LLP
Honolulu, Hawaii
Bond Counsel

The Bank of New York
Escrow Agent

Table of Contents

	<u>Page</u>
INTRODUCTION	1
PLAN OF FINANCE.....	2
Refunding.....	2
Discharge of State’s Obligation upon Refunding.....	3
THE 2003 BONDS	3
General.....	3
Authority for Issuance	4
BOOK-ENTRY SYSTEM.....	4
DTC and its Participants.....	4
Purchase of Ownership Interests	5
Notices and Other Communications.....	5
Principal and Interest Payments	5
Discontinuance of Book-Entry System; Replacement Bonds	5
Use of Certain Terms in Other Sections of the Official Statement.....	6
DTC and Book-Entry Information	6
ESTIMATED SOURCES AND USES OF THE PROCEEDS OF THE 2003 BONDS	7
SECURITY FOR THE BONDS.....	8
General.....	8
Pledge of Revenues	8
Highway Senior Debt Service Reserve Subaccount.....	10
Funds and Accounts and Application of Revenues	10
Additional Bonds and Refunding Bonds.....	11
INSURANCE.....	11
Bond Insurance Policy	12
Financial Security Assurance Inc.	12
Debt Service Reserve Fund Policy	12
REVENUE SOURCES.....	13
State Highway Fund.....	13
Sources of Revenues and Pledged User Taxes.....	13
Historical Revenues.....	14
THE DEPARTMENT OF TRANSPORTATION	15
Department Organization	15
Department Management	16
Management Personnel	16
Employees	17
CAPITAL IMPROVEMENT PROGRAM.....	17
General.....	17
Plan of Finance.....	18
DEBT SERVICE COVERAGE.....	19
Projected Revenues	19
Debt Service Requirements for the Bonds	20
Historic and Projected Debt Service Coverage	20
Reimbursable General Obligation Bonds.....	22
LITIGATION.....	23
TAX MATTERS.....	23
CERTAIN LEGAL MATTERS.....	24
RATINGS	24
ESCROW VERIFICATION.....	25
UNDERWRITING	25
CONTINUING DISCLOSURE.....	25
FINANCIAL STATEMENTS	26
MISCELLANEOUS	26

- APPENDIX A: SUMMARY OF CERTAIN PROVISIONS OF THE CERTIFICATE
- APPENDIX B: ADDITIONAL INFORMATION RELATING TO REVENUE SOURCES, THE STATE HIGHWAY SYSTEM AND THE HAWAII DEPARTMENT OF TRANSPORTATION
- APPENDIX C: THE STATE OF HAWAII

- APPENDIX D: AUDITED FINANCIAL STATEMENTS OF THE HIGHWAYS DIVISION FOR FISCAL YEAR ENDED JUNE 30, 2002
- APPENDIX E: PROPOSED FORM OF OPINION OF BOND COUNSEL
- APPENDIX F: PROPOSED FORM OF CONTINUING DISCLOSURE CERTIFICATE
- APPENDIX G: SPECIMEN OF THE MUNICIPAL BOND INSURANCE POLICY
- APPENDIX H: SPECIMEN OF THE MUNICIPAL BOND DEBT SERVICE RESERVE INSURANCE POLICY

OFFICIAL STATEMENT

\$44,940,000

STATE OF HAWAII

Highway Revenue Bonds Refunding Series 2003

INTRODUCTION

This Official Statement, which includes the cover page and appendices (the "Official Statement"), provides information with respect to the issuance and sale by the State of Hawaii (the "State") of \$44,940,000 principal amount of State of Hawaii Highway Revenue Bonds, Refunding Series 2003 (the "2003 Bonds"). Capitalized terms not otherwise defined in this Official Statement shall have the respective meanings given to such terms in Appendix A "SUMMARY OF CERTAIN PROVISIONS OF THE CERTIFICATE - Definitions of Certain Terms."

The State will issue the 2003 Bonds pursuant to the Constitution, the laws of the State and the Certificate of the Director of Transportation Providing for the Issuance of State of Hawaii Highway Revenue Bonds dated as of August 1, 1993, as heretofore supplemented and as further supplemented by a Sixth Supplemental Certificate of the Director of Transportation Providing for the Issuance of State of Hawaii Highway Revenue Bonds, Refunding Series 2003, dated as of March 25, 2003 (collectively, the "Certificate"). See "THE 2003 BONDS" for a description of the 2003 Bonds. Under the Certificate, the State has previously issued its Highway Revenue Bonds, Series 1993 (the "1993 Bonds"), currently outstanding in the aggregate principal amount of \$48,820,000, its Highway Revenue Bonds, Series 1996 (the "1996 Bonds"), currently outstanding in the aggregate principal amount of \$34,635,000, its Highway Revenue Bonds, Series 1998 (the "1998 Bonds"), currently outstanding in the aggregate principal amount of \$79,315,000, its Highway Revenue Bonds, Series 2000 (the "2000 Bonds"), currently outstanding in the aggregate principal amount of \$47,325,000 and its Highway Revenue Bonds, Series 2001 (the "2001 Bonds"), currently outstanding in the aggregate principal amount of \$70,000,000 (collectively, the "Outstanding Bonds"). Additional bonds and refunding bonds may subsequently be issued on a parity with the 2003 Bonds and the Outstanding Bonds (collectively with the 2003 Bonds and the Outstanding Bonds, the "Senior Bonds") or may be issued subordinate in right of payment to the 2003 Bonds and other Senior Bonds (the "Subordinate Bonds"). The 2003 Bonds and the Outstanding Bonds and any additional Senior Bonds and Subordinate Bonds are collectively referred to as the "Bonds."

The 2003 Bonds are being issued to provide moneys, together with other available moneys of the State, for the current refunding of \$45,350,000 aggregate principal amount of the outstanding 1993 Bonds on and after July 1, 2004 as described in "PLAN OF FINANCE."

The Bonds are special limited obligations of the State, payable from and secured by Pledged Funds as provided under the Certificate, consisting of moneys held in the funds and accounts under the Certificate, revenues derived by the State from the ownership and operation of the statewide system of highways, streets and roads (the "State Highway System") and receipts of Pledged User Taxes related thereto, consisting principally of the highway fuel license taxes, vehicle registration fees, the vehicle weight tax, and the rental motor vehicle and tour vehicle surcharge taxes, as described in this Official Statement under "SECURITY FOR THE BONDS." All Senior Bonds, including the 2003 Bonds, are and will be secured equally and ratably by the Pledged Funds. Receipts of the Pledged User Taxes are deposited into the State Highway Fund, a special fund created by State law in the State Treasury, for credit to the Highway Revenue Special Account created by the Certificate. The 2003 Bonds do not constitute a general or moral

obligation of the State nor a charge upon the general fund of the State. The full faith and credit of the State are not pledged to the payment of or as security for the 2003 Bonds. See "SECURITY FOR THE BONDS" and "REVENUE SOURCES" for a description of the security for the Bonds and sources of Pledged Funds.

The State Highway System is owned, operated, maintained and improved by the Department of Transportation of the State (the "Department"). The Department maintains an ongoing capital improvement program (the "Program") to improve, renew and renovate the State Highway System. See "CAPITAL IMPROVEMENT PROGRAM" for a description of the Program and Appendix B - "ADDITIONAL INFORMATION RELATING TO REVENUE SOURCES, THE STATE HIGHWAY SYSTEM AND THE DEPARTMENT OF TRANSPORTATION" for a description of the State Highway System.

Every other fiscal year, the Department prepares a program of proposed capital improvement projects to the State Highway System for approval of the Governor and the Legislature of the State. The Program is funded on a biennial basis through Legislative appropriations. In the first year of a biennium budget, the Department may revise the second year of that biennium budget for presentation to the Governor for approval and to the Legislature for subsequent authorization.

Payment of principal of and interest on the 2003 Bonds maturing on July 1, 2005 and bearing interest at 3.000% and the 2003 Bonds maturing on July 1 of the years 2006 through 2013, inclusive (the "Insured Bonds") will be guaranteed by an insurance policy issued concurrently with the delivery of the 2003 Insured Bonds by Financial Security Assurance Inc. ("Financial Security"). Payment of principal of and interest on the 2003 Bonds maturing on July 1, 2004 and the 2003 Bonds maturing on July 1, 2005 and bearing interest at 2.500% (the "Uninsured Bonds") will not be guaranteed by the aforementioned insurance policy. In addition, Financial Security will issue a debt service reserve fund policy to satisfy the Reserve Requirement for the Highway Senior Debt Service Reserve Subaccount, as defined in the Certificate. For additional information concerning the policies to be issued by Financial Security, see "INSURANCE" herein, and Appendix G - "SPECIMEN OF THE BOND INSURANCE POLICY" and Appendix H - "SPECIMEN OF THE DEBT SERVICE RESERVE FUND POLICY".

The cover page and this Introduction contain certain information for general reference only. They are not intended to be a summary of the 2003 Bonds. Investors are advised to read this entire Official Statement to obtain information essential to the making of an informed investment decision. This Official Statement contains descriptions of the Department and the Program, summaries of the 2003 Bonds, the security for the Bonds and certain provisions of the Certificate. All references to the Certificate and to the 2003 Bonds are qualified by the definitive forms of such Certificate and 2003 Bonds, copies of which may be obtained from the Department at 869 Punchbowl Street, 5th floor, Honolulu, Hawaii 96813. Any statement or information involving matters of opinion or estimates are represented as opinions or estimates made in good faith, but no assurance can be given that facts will materialize as so opined or estimated.

PLAN OF FINANCE

Refunding

Pursuant to the Certificate, a portion of the proceeds of the sale of the 2003 Bonds, together with other available moneys, will be deposited with The Bank of New York, as escrow agent (the "Escrow Agent"), in a separate account in an escrow fund (the "Escrow Fund") held by the Escrow Agent pursuant to an escrow deposit agreement (the "Escrow Deposit Agreement") by and between the Department, the Department of Budget and Finance of the State and the Escrow Agent. Upon deposit with the Escrow Agent, such moneys shall be immediately invested in non-callable direct obligations of the United States of America (the "Federal Securities"). The principal of and interest on the Federal Securities, together with any cash balances in the separate account in the Escrow Fund, shall be applied in accordance with the Escrow Deposit Agreement and will be sufficient to pay the principal of, and redemption premium and interest, on the refunded 1993 Bonds on July 1, 2003.

Discharge of State's Obligation upon Refunding

Upon such deposit to the Escrow Fund and the investment as aforesaid, the obligation of the State under the Certificate and the liens, pledges and charges and the covenants and agreements of the State made therein shall be fully discharged and satisfied as to the refunded 1993 Bonds, and the refunded 1993 Bonds shall no longer be deemed outstanding under the Certificate. See Appendix A — "SUMMARY OF CERTAIN PROVISIONS OF THE CERTIFICATE — Discharge of Obligations." At the time of such deposit, the State will give the Escrow Agent irrevocable instructions to give timely notice of redemption of the refunded 1993 Bonds, and to apply moneys on deposit in the Escrow Fund to the payment of the principal of and interest and premium, if any, on the refunded 1993 Bonds on July 1, 2003.

The accuracy of the mathematical computations concerning the adequacy of the Escrow Fund, including earnings derived from investment of moneys therein in Federal Securities, to refund the 1993 Bonds maturing on and after July 1, 2004 will be evidenced by a report of the independent certified public accounting firm of Causey, Demgen & Moore Inc. prior to or at the delivery of the 2003 Bonds. See "ESCROW VERIFICATION."

THE 2003 BONDS

General

The 2003 Bonds will be dated their date of delivery and will bear interest from such date at the rates per annum set forth on the inside cover page of this Official Statement, and will mature on July 1 in the years and in the principal amounts set forth on the cover of this Official Statement. Interest will be payable on each January 1 and July 1, commencing July 1, 2003 (each an "Interest Payment Date"). Principal of, premium, if any, and interest on the 2003 Bonds will be payable in any coin or currency of the United States of America which at the time of payment is legal tender for public and private debts.

The 2003 Bonds, when issued, will be registered in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York ("DTC"). DTC will act as securities depository for the 2003 Bonds. Individual purchases of the 2003 Bonds will be made in book-entry form only (the "Book-Entry System"), in the principal amount of \$5,000 or integral multiples thereof. Purchasers will not receive certificates representing their interest in the 2003 Bonds. Principal of and interest on the 2003 Bonds will be paid by the Paying Agent for the 2003 Bonds to DTC, which will in turn remit such principal and interest to its Participants (as hereinafter defined), for subsequent distribution to the Beneficial Owners (as hereinafter defined) of the 2003 Bonds, as described herein. See "BOOK-ENTRY SYSTEM," below.

If the Book-Entry System is discontinued for the 2003 Bonds, thereafter (i) principal of on the 2003 Bonds will be payable upon presentation and surrender of the 2003 Bonds at the principal office of the Department of Budget and Finance of the State, as Paying Agent for the 2003 Bonds (together with any successor, the "Paying Agent"); and (ii) interest on each 2003 Bond will be paid on each Interest Payment Date by check mailed by the Paying Agent to the owner in whose name the 2003 Bond is registered upon the books of registry to be kept and maintained by the Department of Budget and Finance of the State, as registrar for the 2003 Bonds (the "Registrar"), as of the close of business on the 15th day of the calendar month (whether or not a business day) next preceding each Interest Payment Date at such owner's address as shown on the Bond Register.

The Department, the Registrar, and the Paying Agent, may deem and treat the person in whose name any 2003 Bond is registered upon the Bond Register (an "Owner" or "Holder") as the absolute owner of such Bond for all purposes of the Certificate, including receiving payment of the principal of and interest due on the 2003 Bonds. So long as the 2003 Bonds are in the Book-Entry System, the registered owner of the 2003 Bonds in the Bond Register will be Cede & Co., and all such payments will be made to Cede & Co., as registered Owner.

Authority for Issuance

Article VII, Section 12 of the State Constitution and Part III, Chapter 39, Hawaii Revised Statutes (“HRS”), as amended (collectively the “General Revenue Bond Law”), permit the issuance of revenue bonds of the State payable from and secured by the Pledged Funds upon the approval of a majority of the members of each house of the Legislature and pursuant to a certificate of the Director of the Department (the “Director”), which becomes effective upon filing with the Director of Finance. The General Revenue Bond Law does not limit the aggregate principal amount of revenue bonds that may be issued, but does limit the maximum maturity of revenue bonds and also sets forth provisions for the sale, method of execution and other details of all revenue bonds. The Legislature from time to time enacts laws (including the general appropriations acts) authorizing the issuance of revenue bonds (without fixing any particular details), defining the purposes for which the bonds are to be issued and specifying the amount of the proceeds of such bonds which may be applied to such purposes; provided that the Department, with the approval of the Governor, may issue refunding bonds without further authorization of the Legislature. Pursuant to the General Revenue Bond Law, the Director has issued the Certificate, which under State law constitutes the security document pursuant to which all Bonds are issued and secured. The Certificate provides the terms of the Bonds, including principal amounts, interest rates, maturities, redemption provisions and the covenants of the Department.

The 2003 Bonds are being issued pursuant to the Certificate and under the authority of and pursuant to the General Revenue Bond Law and Act 289, Session Laws of Hawaii (“SLH”) 1993, as amended by Act 252, SLH 1994, Act 218, SLH 1995, as amended by Act 287, SLH 1996, Act 328, SLH 1997, as amended by Act 116, SLH 1998 and Act 91, SLH 1999, as amended by Act 281, SLH 2000 and Act 259, SLH 2001.

BOOK-ENTRY SYSTEM

Information concerning DTC and the Book-Entry System contained in this Official Statement has been obtained from DTC and other sources that the State and the Underwriter believe to be reliable, and is not guaranteed as to accuracy or completeness by, and is not to be construed as a representation by, the Underwriter or the State.

DTC will act as securities depository for the 2003 Bonds. The 2003 Bonds will be issued as fully-registered securities registered in the name of Cede & Co. (DTC’s partnership nominee). One fully registered Bond certificate will be issued for each maturity of the 2003 Bonds in the aggregate principal amount of such issue, and will be deposited with DTC.

DTC and its Participants

DTC is a limited-purpose trust company organized under the New York Banking Law, a “banking organization” within the meaning of the New York Banking Law, a member of the Federal Reserve System, a “clearing corporation” within the meaning of the New York Uniform Commercial Code, and a “clearing agency” registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds securities that its participants (“Participants”) deposit with DTC. DTC also facilitates the settlement among Participants of securities transactions such as transfers and pledges, in deposited securities through electronic computerized book-entry changes in Participants’ accounts, thereby eliminating the need for physical movement of securities certificates. “Direct Participants” include securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is owned by a number of its Direct Participants and by the New York Stock Exchange, Inc., the American Stock Exchange, Inc., and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as securities brokers and dealers, banks, and trust companies that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (“Indirect Participants”). The Rules applicable to DTC and its Participants are on file with the Securities and Exchange Commission.

Purchase of Ownership Interests

Purchases of 2003 Bonds under the DTC system must be made by or through Direct Participants, which will receive credit for the 2003 Bonds on DTC's records. The ownership interest of each purchaser of a beneficial interest in a 2003 Bond (for the purposes of the discussion under "Book-Entry System," a "Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase, but Beneficial Owners are expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of beneficial interests in the 2003 Bonds are to be accomplished by entries made on the books of Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their beneficial interests in 2003 Bonds, except in the event that use of the Book-Entry System for the 2003 Bonds is discontinued.

To facilitate subsequent transfers, all 2003 Bonds deposited by Participants with DTC are registered in the name of DTC's nominee, Cede & Co. The deposit of 2003 Bonds with DTC and their registration in the name of Cede & Co. effect no change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the 2003 Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such Bonds are credited, which may or may not be the Beneficial Owners. The Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Notices and Other Communications

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

Neither DTC nor Cede & Co. will consent or vote with respect to the 2003 Bonds. Under its usual procedures, DTC mails an Omnibus Proxy to the State as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts the 2003 Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal and Interest Payments

Principal and interest payments on the 2003 Bonds will be made by the Paying Agent only to Cede & Co., as registered Owner. DTC's practice is to credit Direct Participants' accounts on the payable date in accordance with their respective holdings shown on DTC's records unless DTC has reason to believe that it will not receive payment on the payable date. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name", and will be the responsibility of such Participant and not of DTC, or the State or the Department, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal and interest to DTC is the responsibility of the State, disbursement of such payments to Direct Participants shall be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners shall be the responsibility of Direct and Indirect Participants.

Discontinuance of Book-Entry System; Replacement Bonds

DTC may discontinue providing its services as securities depository with respect to the 2003 Bonds at any time by giving reasonable notice to the State or the Department. Under such circumstances, in the event that a successor securities depository is not obtained, Bond certificates are required to be printed and delivered.

The Department may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Bond certificates will be printed and delivered.

In the event the Book-Entry System is discontinued, the principal of and interest on the 2003 Bonds will be payable as described above under "The 2003 Bonds - General" and the following provisions will apply.

Each 2003 Bond may be transferred or exchanged upon the books of registry by the registered Owner, in person or by its duly authorized attorney, upon surrender of such 2003 Bond for cancellation, accompanied by a written instrument of transfer or exchange satisfactory in form to the Registrar, duly executed by the registered owner or its duly authorized attorney. Upon the surrender of any 2003 Bond for transfer or exchange, the Registrar will deliver in the name of the transferee or Owner one or more new 2003 Bonds of the same aggregate principal amount, maturity and interest rate as the surrendered 2003 Bond, in any authorized denomination and in the manner and subject to the conditions set forth in the Certificate.

All such transfers and exchanges will be made without expense to the owner of such Bonds, except that the Registrar shall require the payment by the owner requesting such transfer of any tax or other governmental charges required to be paid with respect to such transfer. No owner may require an exchange or transfer of 2003 Bonds to be made during the 15 days next preceding an Interest Payment Date or during a period beginning at the opening of business 15 days before the mailing of a notice of redemption of Bonds selected for redemption and ending on the close of business on the day of such mailing, or an exchange or transfer to be made of any 2003 Bond or portion thereof which has been selected for redemption.

Use of Certain Terms in Other Sections of the Official Statement

In reviewing this Official Statement it should be understood that so long as Cede & Co. is the registered Owner of the 2003 Bonds, references herein to the registered Owners or Holders will mean Cede & Co. and will not mean the Beneficial Owners. Under the Certificate, payments made by the State or the Paying Agent to Cede & Co. will satisfy the State's obligations under the Certificate to the extent of the payment. The Beneficial Owners will not be, and will not be considered by the State or the Paying Agent to be, and will not have any rights as, the Holders of the 2003 Bonds under the Certificate, but (i) all rights of ownership, must be exercised through DTC and the Book-Entry System and (ii) notices that are to be given to Owners by the State or the Paying Agent will be given only to DTC. DTC will forward (or cause to be forwarded) the notices to the Participants by its usual procedures so that such Participants may forward (or cause to be forwarded) such notices to the Beneficial Owners.

DTC and Book-Entry Information

Information concerning DTC and the Book-Entry System contained in this Official Statement has been obtained from DTC and is not guaranteed as to accuracy or completeness by, and is not to be construed as a representation by, the Underwriter, the State or the Department.

Neither the State nor the Department will have any responsibility or obligation to Direct Participants, to Indirect Participants or to Beneficial Owners with respect to (i) the accuracy of any records maintained by DTC, any Direct Participants or Indirect Participants, or (ii) the payment of any amount due by DTC to a Direct Participant, or the payment by any Direct Participants or any Indirect Participants of any amount in respect of principal or redemption price of or interest on the 2003 Bonds, or (iii) delivery of any notice by DTC to any Direct Participant or by any Direct Participant or Indirect Participant to any Beneficial Owner, which is required or permitted to be given to registered Owners under the Certificate, or (iv) any consent given or other action taken by DTC as owner of the 2003 Bonds, or (vi) any other event or purpose.

ESTIMATED SOURCES AND USES OF THE PROCEEDS OF THE 2003 BONDS

The following table shows the estimated sources and uses of moneys realized by the Department of the proceeds of the 2003 Bonds:

Sources:

Bond Proceeds:

Par Amount of 2003 Bonds	\$44,940,000
Original Issue Discount	(1,728)
Premium	2,333,336

Other Sources of Funds:

519,500

TOTAL SOURCES OF FUNDS

47,791,108

Uses:

Deposit to Escrow Fund 47,268,877

Underwriter's Discount 312,962

Bond Insurance and Debt Service Reserve Fund Policy 139,051

Other Costs of Issuance 70,218

TOTAL USES OF FUNDS

\$47,791,108

SECURITY FOR THE BONDS

General

The Bonds, including the 2003 Bonds, are special limited obligations of the State, and will be payable from and secured by the Pledged Funds. The 2003 Bonds, the Outstanding Bonds and any Additional Senior Bonds that may subsequently be issued under the Certificate are collectively referred to as "Senior Bonds." The Senior Bonds are equally and ratably secured by a lien and charge on the Pledged Funds prior and paramount to the lien thereon of any other bonds.

"Pledged Funds" is defined in the Certificate to include the Revenues held in the Highway Revenue Special Account created in the Certificate and the Highway Bond Proceeds Account in the State Bond Fund. "Revenues" is defined to include the following when deposited in the State Highway Fund: Pledged User Taxes, certain revenues derived from the ownership or operation of, or disposition of properties constituting part of, the State Highway System, and certain investment earnings. "Pledged User Taxes" is defined to include the receipts of the highway fuel license taxes, vehicle registration fees, the vehicle weight tax, and the rental motor vehicle and tour vehicle surcharge taxes. See "REVENUE SOURCES" below.

The Bonds do not constitute general or moral obligations of the State nor a charge upon the general fund of the State. The full faith and credit of the State are not pledged to the payment of the principal of or interest on the Bonds. The real property and improvements comprising the State Highway System have not been pledged or mortgaged to secure payment of the Bonds.

State law creates a special fund in the Treasury of the State designated as the State Highway Fund. The Certificate creates the Highway Revenue Special Account in the State Highway Fund and requires that the Highway Revenue Special Account be continued as long as any Bonds remain outstanding and provides that all Revenues will be deposited in the State Highway Fund for credit to the Highway Revenue Special Account. The Certificate further provides that amounts deposited in the Highway Revenue Special Account will be used in the order of priority established by the Certificate. Payment of principal of and interest on the Senior Bonds is the first priority and charge against the Highway Revenue Special Account. See "Funds and Accounts and Application of Revenues" below.

In the event of a default, the Holders of at least 25% in principal amount of the Senior Bonds then outstanding and the Holders of at least 25% in principal amount of the Subordinate Bonds outstanding may declare an immediate acceleration of maturities by written notice to the Department, which notice shall also be filed with the Director of Finance of the State.

Under the doctrine of sovereign immunity, a state of the Union (including the State) cannot be sued by its own citizens. Under the United States Constitution, a state (including the State) cannot be sued by citizens of another state of the Union or by citizens or subjects of any foreign state. A state (including the State) may waive its immunity and consent to a suit against itself. The State has waived by statute its immunity from contractual claims. However, such waiver and consent may subsequently be withdrawn by the State. Such immunity from and constitutional prohibition against suits against a state extends to officers of a state acting in their official capacity.

Therefore, there can be no assurance that in the event the State fails to make timely payment of principal of or interest on the Bonds, a right of action would lie against the State or State officials to enforce such payment.

The State has never defaulted in the payment of either principal of or interest on any indebtedness.

Pledge of Revenues

Under the Certificate, the State and the Department pledge and grant a lien on the Pledged Funds to secure the Senior Bonds, which pledge and lien are superior and prior to the pledge of and lien upon the Pledged Funds in respect of

the Subordinate Bonds; and pledge and grant a lien on the Pledged Funds to secure the Subordinate Bonds, which pledge and lien are inferior and subordinate to the pledge of and lien upon the Pledged Funds in respect of the Senior Bonds. The Certificate provides that the lien on the Pledged Funds to secure the Bonds is a prior and paramount lien, subject only to the provisions of the Certificate permitting the application of such funds for the purposes and on the terms and conditions thereof.

The Certificate further provides that the moneys in the State Highway Fund shall, until used, applied and disbursed in accordance with the provisions of the Certificate, be held in trust: (1) for the equal benefit and security of the Holders of the Senior Bonds; and (2) subject to the prior and senior rights, benefits and security of the Holders of the Senior Bonds, for the equal benefit and security of the Holders of the Subordinate Bonds. Subject to the provisions of the Certificate concerning application of amounts on deposit in the subaccount relating to the Senior Bonds, all Senior Bonds have a prior and paramount lien on the Revenues paid into the Highway Revenue Special Account for credit to such subaccount and the investments in which such Revenues may be invested, over and ahead of all Subordinate Bonds and all bonds, notes or other evidences of indebtedness which may subsequently be issued. Subject to the prior and paramount lien provided in respect of the Senior Bonds and further subject to the provisions of the Certificate concerning application of amounts on deposit in the subaccount relating to the Subordinate Bonds, all Subordinate Bonds have a prior and paramount lien on the Revenues paid into the Highway Revenue Special Account for credit to such subaccount and the investments in which such Revenues may be invested, over and ahead of all bonds, notes or other evidences of indebtedness which may subsequently be issued.

Under the General Revenue Bond Law, the Department is obligated to impose, prescribe and collect rates, rents, fees, or charges for the use and services of, and the facilities and commodities furnished by, the State Highway System which, together with the proceeds of the Pledged User Taxes derived from the State Highway System, are at least sufficient: (1) to make the required payments of principal and interest on all Bonds, including reserves therefor; (2) to pay the costs of operation, maintenance and repair of the State Highway System, including reserves therefor; and (3) to carry out the covenants of the Certificate.

The State has considered but does not presently anticipate imposing any tolls, rates, rentals, fees or charges for the use and services provided by the State Highway System and, as indicated, expects that the principal source of payment of the Bonds will derive from the Pledged User Taxes imposed pursuant to law.

The State Constitution defines a "user tax" as a tax on goods or services or on the consumption thereof, the receipts of which are substantially derived from consumption, use or sale of goods and services in the utilization of the functions or services furnished by a public undertaking (an "Undertaking"), improvement or system. The specific acts of the Legislature authorizing Highway Revenue Bonds direct that they shall be payable from and secured by the revenues derived from highways and related facilities under the ownership of the State or operated and managed by the Department comprising the State Highway System, and from the highway fuel license taxes, vehicle registration fees, the vehicle weight tax, and the rental motor vehicle and tour vehicle surcharge taxes levied and paid pursuant to Sections 243-4, 248-8, 249-31, 249-33, and 251-2, HRS, and federal moneys received by the State or any department thereof which are available to pay principal of and interest on indebtedness of the State, and other user taxes, fees or charges currently or hereafter derived from or arising through the ownership, operation, and management of highways and related facilities and the furnishing and supplying of the services thereof. Each of the aforesaid taxes, charges and fees constitutes a "user tax" within the meaning of the State Constitution.

Under the General Revenue Bond Law, the Legislature has covenanted, pledged and obligated the Legislature, whenever the Legislature shall have authorized the issuance of bonds for an Undertaking such as the State Highway System, payable from and secured by the user taxes derived with respect to such Undertaking, or by both revenues and user taxes, or by any combination of both, to impose or continue to impose user taxes with respect to such Undertaking in amounts at least sufficient, together with the revenue of the Undertaking, to make the payments described above. These provisions would not prohibit the Legislature from changing the rate of existing Pledged User Taxes or other user taxes or fees or from deleting some or all of existing Pledged User Taxes or other user taxes or fees and substituting other or different user taxes or fees.

There is no requirement under the Certificate or the General Revenue Bond Law that the Legislature levy and deposit Pledged User Taxes into the State Highway Fund in excess of the amount necessary to make the deposits described in paragraphs FIRST through FIFTH under “Funds and Accounts and Application of Revenues” below.

Highway Senior Debt Service Reserve Subaccount

In order to provide a reserve for the payment of the principal of and interest on the Senior Bonds, the Certificate creates a Highway Senior Debt Service Reserve Subaccount in the Highway Revenue Special Account. The Certificate requires that moneys on deposit in the Highway Senior Debt Service Reserve Subaccount shall be maintained in an amount at least equal to one-half (1/2) of the maximum Aggregate Bond Service for the Senior Bonds at the time outstanding for any Bond Year (the “Reserve Requirement”), beginning with the Bond Year in which such determination is made. In lieu of the deposit of moneys to the Highway Senior Debt Service Reserve Subaccount, the Certificate allows the Department to credit one or more Support Facilities in an amount equal to the difference between the Reserve Requirement and the aggregate of (1) moneys already deposited in such Subaccount and (2) amounts available to be drawn under any Support Facility already credited to such Subaccount. See “Highway Senior Debt Service Reserve Subaccount” and definitions of Aggregate Bond Service, Bond Year and Support Facility in Appendix A - “SUMMARY OF CERTAIN PROVISIONS OF THE CERTIFICATE.”

At the time of the delivery of the 2003 Bonds, the Reserve Requirement will be satisfied by a support facility in the form of a debt service reserve fund policy (the “Reserve Fund Policy”) issued by Financial Security. See “INSURANCE - Reserve Fund Policy” herein and Appendix H - “SPECIMEN OF THE RESERVE FUND POLICY”.

Funds and Accounts and Application of Revenues

The Certificate creates the Highway Revenue Special Account, comprised of the subaccounts listed below, within the State Highway Fund and provides that, so long as any Bonds are Outstanding: (1) the State Highway Fund and the Highway Revenue Special Account shall both be continued; and (2) all Revenues deposited in the State Highway Fund shall be credited to the Highway Revenue Special Account. Revenues from specified sources are deposited into the State Highway Fund. See “REVENUE SOURCES” below. Moneys that are paid into and are on deposit in the State Highway Fund constitute the Revenues that are pledged to the payment of the Bonds. Revenues credited or to be credited to the Highway Revenue Special Account are required to be applied and used in the following order of priority:

FIRST: For further credit to the following subaccounts in the following order of priority in the amounts required pursuant to the provisions of the Certificate:

- (a) Highway Senior Interest Subaccount;
- (b) Highway Senior Principal Subaccount; and
- (c) Highway Senior Debt Service Reserve Subaccount;

SECOND: For further credit to the following subaccounts in the following order of priority in the amounts required pursuant to the provisions of the Certificate:

- (a) Highway Subordinate Interest Subaccount;
- (b) Highway Subordinate Principal Subaccount; and
- (c) Highway Subordinate Debt Service Reserve Subaccount;

THIRD: For payment of operation and maintenance expenses of the State Highway System;

FOURTH: For payment of the costs of acquisition, construction, addition, expansion, improvement, renewal, replacement, reconstruction, engineering, investigation and planning for the State Highway System;

FIFTH: To reimburse the general fund of the State for reimbursable general obligation bonds of the State;

SIXTH: All or any portion of available moneys credited to the Highway Revenue Special Account, after satisfying the requirements of priority items FIRST through FIFTH above, determined in conformance with law by the Director of Transportation to be in excess of 135% of the requirements for the ensuing 12 months for the Highway Revenue Special Account, or such other percentage as may be authorized by law, may be transferred from the Highway Revenue Special Account as permitted by and in accordance with State law; and

SEVENTH: To provide funds for other special reserve funds and other special funds as may be created by law.

Additional Bonds and Refunding Bonds

The Certificate permits the issuance of Additional Bonds payable from and secured by Pledged Funds on a parity with the 2003 Bonds, the Outstanding Bonds and other Senior Bonds, or the issuance of Additional Bonds which are Subordinate Bonds, for the purpose of paying or reimbursing the cost of acquisition or construction of properties to constitute part of the State Highway System or the making of additions to, expansions of, improvements of, renewals of or reconstructions of the State Highway System. Additional Bonds which are Senior Bonds must be fixed rate bonds. Additional Bonds which are Subordinate Bonds may be fixed rate bonds or variable rate bonds. The conditions for issuance of Additional Bonds include, among other things, that the Director certify that:

(1) no default in the payment of any Bond has occurred and is continuing; no deficiency exists in the State Highway Fund or the Highway Revenue Special Account; and there does not exist any Event of Default under the Certificate or a condition which upon the passage of time would constitute such an Event of Default;

(2) upon delivery of such Bonds, there shall be credited to the Highway Revenue Special Account for credit to the Highway Senior Debt Service Reserve Subaccount and the Highway Subordinate Debt Service Reserve Subaccount an amount equal to, in each case, the Reserve Requirement; provided that such requirement may be satisfied by a deposit of proceeds of such Bonds or a support facility; and

(3) in the case of Additional Bonds, the Revenues for any consecutive twelve-month period out of the last eighteen consecutive calendar months immediately preceding the date of issuance of such Bonds shall be at least equal to: (a) in the case of Senior Bonds proposed to be issued, two times maximum Aggregate Bond Service for any future Fiscal Year on all Senior Bonds to be outstanding after the issuance of such Additional Senior Bonds; and (b) in the case of Subordinate Bonds proposed to be issued, 1.30 times maximum Aggregate Bond Service for any future Fiscal Year on all Bonds to be outstanding after the issuance of such Additional Subordinate Bonds.

The Certificate permits the issuance of Refunding Bonds payable from and secured by Pledged Funds on a parity with the 2003 Bonds and other Senior Bonds, or Refunding Bonds which are Subordinate Bonds, for the purpose of refunding any then outstanding Bonds, so long as the State has satisfied the requirement set forth in the first and second subparagraphs described above and without satisfying any financial tests. See Appendix A "SUMMARY OF CERTAIN PROVISIONS OF THE CERTIFICATE - Conditions Precedent to Issuance of Additional Bonds and Refunding Bonds."

The Certificate permits the issuance of other bonds or obligations payable from the Revenues subordinate and inferior to the payment of the Bonds from the Revenues.

INSURANCE

The following information concerning the Bond Insurance Policy and the Reserve Fund Policy has been provided by Financial Security Assurance Inc.. No representation is made by the State or the Underwriters as to the accuracy, completeness or adequacy of such information, or as to the absence of material adverse changes in such information subsequent to the date hereof.

Bond Insurance Policy

Concurrently with the issuance of the Bonds, Financial Security Assurance Inc. (the "Financial Security") will issue its Municipal Bond Insurance Policy (the "Policy") for the 2003 Bonds maturing on July 1, 2005 bearing interest at 3.000% and on July 1 of the years 2006 through 2013, inclusive (the "Insured Bonds"). The Policy guarantees the scheduled payment of principal of and interest on the Insured Bonds when due as set forth in the form of the Policy included as an exhibit to this Official Statement.

The Policy is not covered by any insurance security or guaranty fund established under New York, California, Connecticut or Florida insurance law.

Financial Security Assurance Inc.

Financial Security is a New York domiciled insurance company and a wholly owned subsidiary of Financial Security Assurance Holdings Ltd. ("Holdings"). Holdings is an indirect subsidiary of Dexia, S.A., a publicly held Belgian corporation. Dexia, S.A., through its bank subsidiaries, is primarily engaged in the business of public finance in France, Belgium and other European countries. No shareholder of Holdings or Financial Security is liable for the obligations of Financial Security.

At September 30, 2002 Financial Security's total policyholders' surplus and contingency reserves were approximately \$1,728,433,000 and its total unearned premium reserve was approximately \$972,390,000 in accordance with statutory accounting principles. At September 30, 2002, Financial Security's total shareholder's equity was approximately \$1,928,564,000 and its total net unearned premium reserve was approximately \$814,684,000 in accordance with generally accepted accounting principles.

The financial statements included as exhibits to the annual and quarterly reports filed by Holdings with the Securities and Exchange Commission are hereby incorporated herein by reference. Also incorporated herein by reference are any such financial statements so filed from the date of this Official Statement until the termination of the offering of the Insured Bonds. Copies of materials incorporated by reference will be provided upon request to Financial Security Assurance Inc.: 350 Park Avenue, New York, New York 10022, Attention: Communications Department (telephone (212) 826-0100).

The Policy does not protect investors against changes in market value of the Insured Bonds, which market value may be impaired as a result of changes in prevailing interest rates, changes in applicable ratings or other causes. Financial Security makes no representation regarding the Insured Bonds or the advisability of investing in the Insured Bonds. Financial Security makes no representation regarding the Official Statement, nor has it participated in the preparation thereof, except that Financial Security has provided to the Issuer the information presented under this caption for inclusion in the Official Statement.

Debt Service Reserve Fund Policy

Concurrently with the issuance of the 2003 Bonds, Financial Security will issue its Municipal Bond Debt Service Reserve Fund Policy (the "Reserve Policy"). The Reserve Policy unconditionally guarantees the payment of that portion of the principal of and interest on the 2003 Bonds which has become due for payment, but shall be unpaid by reason of nonpayment by the Issuer, provided that the aggregate amount paid under the Reserve Policy may not exceed the maximum amount set forth in the Reserve Policy, which maximum amount represents \$2,848,200. Financial Security will make such payments to the paying agent (the "Paying Agent") for the 2003 Bonds on the later of the date on which such principal and interest is due or on the business day next following the day on which Financial Security shall have received telephonic or telegraphic notice subsequently confirmed in writing or written notice by registered or certified mail from the Paying Agent of the nonpayment of such amount by the Issuer. The term "nonpayment" in respect of a 2003 Bond includes any payment of principal or interest made to an owner of a 2003 Bond which has been recovered from such owner pursuant to the United States Bankruptcy Code by a trustee in bankruptcy in accordance with a final nonappealable

order of a court having competent jurisdiction.

The Reserve Policy is non-cancelable and the premium will be fully paid at the time of delivery of the 2003 Bonds. The Reserve Policy covers failure to pay principal of the 2003 Bonds on their respective stated maturity dates, or dates on which the same shall have been called for mandatory sinking fund redemption, and not on any other date on which the 2003 Bonds may have been accelerated, and covers the failure to pay an installment of interest on the stated date for its payment. The Reserve Policy shall terminate on the earlier of the scheduled final maturity date of the 2003 Bonds or the date on which no 2003 Bonds are outstanding under the Certificate.

Generally, in connection with its issuance of a Reserve Policy, Financial Security requires, among other things, (i) that, so long as it has not failed to comply with its payment obligations under the Reserve Policy, it be granted the power to exercise any remedies available at law or under the authorizing document other than (A) acceleration of the Bonds or (B) remedies which would adversely affect holders in the event that the issuer fails to reimburse Financial Security for any draws on the Reserve Policy; and (ii) that any amendment or supplement to or other modification of the principal legal documents be subject to Financial Security's consent. The specific rights, if any, granted to Financial Security in connection with its issuance of the Reserve Policy are set forth in the description of the principal legal documents appearing elsewhere in this Official Statement. Reference should be made as well to such description for a discussion of the circumstances, if any, under which the issuer of the 2003 Bonds is required to provide additional or substitute credit enhancement, and related matters.

The Reserve Policy is not covered by any insurance security or guaranty fund established under New York, California, Connecticut or Florida insurance law.

REVENUE SOURCES

State Highway Fund

The State imposes taxes, fees and charges relating to the operation and use of motor vehicles on the public highways of the State. These funds are deposited into the State Highway Fund established under Section 248-8, HRS. Moneys deposited in the State Highway Fund are used for acquisition, planning, design, construction, operation, repair and maintenance of the State Highway System.

The current taxes, fees and charges deposited to the State Highway Fund consist of: (1) the highway fuel license taxes; (2) vehicle registration fees; (3) the vehicle weight tax; and (4) the rental motor vehicle and tour vehicle surcharge taxes. Together, these taxes, fees and charges accounted for most of the receipts of the State Highway Fund in the Fiscal Year ended June 30, 2002. See "Historical Revenues" below. Other sources of Revenues include interest earnings on moneys previously credited to the State Highway Fund, vehicle weight tax penalties, certain rental income from State Highway System properties, passenger motor vehicle inspection charges, overweight permits, sales of surplus lands, commercial license fees and other miscellaneous Revenues. There are no toll roads or bridges in the State. The primary sources of Revenues are further described below.

Sources of Revenues and Pledged User Taxes

The following is a summary of the sources of Revenues that are deposited to the State Highway Fund. This summary does not purport to be a complete description of each of these Revenue sources and accordingly is qualified by reference to the Hawaii Revised Statutes regarding sources of Revenues. The Legislature has altered and may in the future alter the statutes governing these Revenue sources, the rates of the Pledged User Taxes and their allocation.

Highway Fuel License Taxes. Highway fuel license taxes consist of license taxes on fuel sold to motor vehicle operators pursuant to Chapter 243, HRS. The distributor of motor vehicle fuel pays the fuel license tax for liquid fuel produced or imported by the distributor to be sold or used by the distributor. Highway fuel license taxes are assessed at a

rate of \$0.16 per gallon of gasoline and diesel oil (highway use), \$0.11 per gallon of liquid petroleum gas (highway use), and \$0.01 per gallon of gasoline, diesel oil and liquid petroleum gas (non highway use). The highway fuel license taxes are collected by the Department of Taxation, which then transfers the receipts to the State Highway Fund. The counties have a similar tax that is not included in the State's fuel license tax rate, as described in Appendix B - "ADDITIONAL INFORMATION RELATING TO REVENUE SOURCES, THE STATE HIGHWAY SYSTEM AND THE DEPARTMENT OF TRANSPORTATION." Receipts of aviation fuel taxes and taxes collected with respect to liquid fuel sold for use in small boats are transferred to the Airport Revenue Fund and the Boating Special Fund, respectively, and not to the State Highway Fund.

Vehicle Registration Fees. All vehicles, including motor vehicles, must be registered annually with one of the four counties of the State. The vehicle owner must pay a State registration fee of \$20 for each vehicle, pursuant to Section 249-31, HRS. The four counties each collect the vehicle registration fee along with their respective county registration fees and transfer the State's vehicle registration fee to the State Highway Fund. (See Appendix B - "ADDITIONAL INFORMATION RELATING TO REVENUE SOURCES, THE STATE HIGHWAY SYSTEM AND THE DEPARTMENT OF TRANSPORTATION.")

Vehicle Weight Taxes. All vehicles, including motor vehicles, are assessed an annual State vehicle weight tax pursuant to Section 249-33, HRS. The tax rate is \$0.0075 per pound for vehicles less than 4,000 pounds; \$0.01 per pound for vehicles between 4,001 and 7,000 pounds, \$0.0125 per pound for vehicles between 7,001 and 10,000 pounds, and \$150.00 per vehicle for vehicles over 10,000 pounds. Vehicle weight taxes increased from a minimum rate of \$0.0045 per pound to \$0.0050 per pound to \$0.0075 per pound and a maximum charge of \$36.00 per vehicle to \$65.00 per vehicle to \$150.00 per vehicle over the period from 1991 to 2002. The four counties each collect the vehicle weight tax along with their respective county vehicle taxes and transfer the State's vehicle weight tax to the State Highway Fund. (See Appendix B - "ADDITIONAL INFORMATION RELATING TO REVENUE SOURCES, THE STATE HIGHWAY SYSTEM AND THE DEPARTMENT OF TRANSPORTATION.")

Rental Motor Vehicle and Tour Vehicle Surcharge Taxes. Chapter 251, HRS, imposes a surcharge tax on all rental motor vehicles and tour vehicles. The rental motor vehicle surcharge tax is imposed on the owner of the rental company when a rental motor vehicle is rented or leased. Through Act 223, SLH 1999, the surcharge tax was increased from \$2.00 per day to \$3.00 per day or any portion of the day. The additional \$1.00 per day or any portion of the day is effective from September 1, 1999 through August 31, 2007.

The tour vehicle surcharge tax is imposed on the tour vehicle operator. The surcharge tax is \$65.00 per month for each tour vehicle used or partially used during the month.

All rental and tour companies must register with the State. The registration fee is a one-time \$20.00 fee.

Recent concerns regarding domestic security, particularly following the terrorist attacks of September 11, 2001, have had a negative effect on tourism in the State. Current U.S. military operations overseas may lead to additional concerns over security. A decline in tourism could adversely affect the Revenues of the Highways System, and particularly Revenues from the rental motor vehicle and tour vehicle surcharge tax and the Highways fuel license tax. At this time, neither the State nor the Department can predict either the severity or duration of these effects.

Interest Earnings. Interest income is derived from the investment of moneys on deposit in the Highway Special Fund.

Historical Revenues

The following table sets forth the sources of Revenues which were deposited into the State Highway Fund for each of the last ten (10) fiscal years ended June 30, 2002.

Sources of Revenues Deposited in the State Highway Fund
(in thousands of \$)

Pledged User Taxes

Fiscal Year	Fuel Taxes	Registration Fees	Weight Taxes -	Rental/ Tour Vehicle Surcharge	Interest	Misc.(1)	Total Revenues
1993	66,151	16,104	20,316	20,914	6,094	2,815	132,394
1994	68,525	15,733	20,377	20,366	5,022	3,208	133,231
1995	67,702	17,352	21,013	21,465	9,924	3,559	141,015
1996	69,010	16,130	21,055	21,951	11,054	3,468	142,668
1997	69,880	16,245	21,363	22,600	10,961	3,323	144,372
1998	68,580	16,418	21,753	23,702	8,076	3,255	141,784
1999	67,209	16,749	22,434	23,591	10,535	3,885	144,403
2000	68,088	17,216	24,425	34,587	12,314	5,662	162,292
2001	71,931	17,616	25,345	38,633	13,616	5,616	172,757
2002	73,046	19,491	28,620	36,054	11,439	4,399	173,049

(1) Miscellaneous Revenues include vehicle weight tax penalties, periodic motor vehicle inspection charges, rents from State Highway System properties, commercial license fees, and other miscellaneous Revenues.

Source: Department of Transportation

The rate of taxation on fuel and the registration fee and taxes on motor vehicles changed and increased significantly between 1975 and 1991 but has not changed since 1991. Highway fuel license taxes increased from \$0.085 per gallon of gasoline and diesel oil and \$0.060 per gallon of liquid petroleum gas in 1975, to \$0.110 per gallon of gasoline and diesel oil and \$0.080 per gallon of liquid petroleum gas in 1985, to the present rate of \$0.160 per gallon of gasoline and diesel oil and \$0.110 per gallon of liquid petroleum gas, which became effective on July 1, 1991.

The State vehicle registration fee has been increased from \$1.00 per vehicle in 1979 to \$10.00 per vehicle in 1985 to \$20.00 per vehicle in 1991 and has not changed since 1991. Vehicle weight taxes increased from a minimum rate of \$0.0045 per pound to \$0.0050 per pound to \$0.0075 per pound and a maximum charge of \$36.00 per vehicle to \$65.00 per vehicle to \$150.00 per vehicle over the same period.

See "DEBT SERVICE COVERAGE" for a discussion of projected Revenues.

THE DEPARTMENT OF TRANSPORTATION

Department Organization

The Department is one of 18 principal executive departments of the State. Chapter 26, HRS, empowers the Department to establish, maintain and operate the transportation facilities of the State, including highways, airports, harbors and such other transportation facilities. The Department's activities are carried out through three primary operating divisions: Airports, Harbors and Highways. The Department's Airports Division has general responsibility to construct, operate and maintain the Airports system. The Harbors Division has general responsibility to construct, operate and maintain the Harbors system.

Through the Highways Division (the "Highways Division"), the Department has general supervision of the management and maintenance of the State Highway System and the location, design and construction of new highways

and facilities. The Highways Division provides supervision to assure completion of State highway contracts in accordance with plans and specifications.

The Department also has administrative offices which are responsible for Department-wide administrative functions and multi-modal statewide transportation planning. See Appendix B - "ADDITIONAL INFORMATION RELATING TO REVENUE SOURCES, THE STATE HIGHWAY SYSTEM AND THE DEPARTMENT OF TRANSPORTATION" for additional information regarding the Department.

Department Management

The Department is headed by the Director, a single executive appointed by the Governor and confirmed by the State Senate. The Governor also appoints, without State Senate confirmation, two Deputy Directors of Transportation. The Director and Deputy Directors of Transportation serve four-year terms coterminous with the Governor's term.

Chapter 26, HRS, establishes the Commission on Transportation which sits in an advisory capacity to the Director on matters within the jurisdiction of the Department. The Commission on Transportation consists of at least one member from each of the four counties of the State.

The Highways Division is managed by the Highways Division Administrator. Each of the major islands is managed by a district manager with the exception of Maui District which includes the islands of Maui, Molokai and Lanai. The Staff Services Office, headed by the Administrative Services Officer, is responsible for personnel, budget, procurement, financial management and method, standards and evaluation functions of the Highways Division. Other major functional operations within the Highways Division include Landscape Services Office, Motor Vehicle Safety Office, Planning Branch, Design Branch, Materials Testing and Research Branch, Construction and Maintenance Branch, Traffic Branch and Rights of Way Branch.

Management Personnel

The following are the senior executives of the Department responsible for the management of the State Highway System:

Rodney K. Haraga, Director assumed his present position in January 2003. Mr. Haraga retired from the City of Los Angeles, Department of Public Works as a Deputy City Engineer. He has over 32 years of design and construction management experience in the public sector. His project knowledge and experience are diverse. He has managed and directed many programs including municipal buildings, police and fire facilities, emergency operations, sewers, bridges, storm drains, fire/life safety programs, earthquake reconstruction programs and seismic restoration. He has successfully directed projects from the Federal Highway Administration for grade separation projects, street improvements projects and seismic restoration of bridges. He was successful as the lead negotiator for the City of Los Angeles in obtaining \$140 million from the Federal Emergency Management Agency, Northridge Earthquake, 1994.

Glenn Okimoto, Acting Deputy Director assumed his present position in January 2003. Prior to his appointment as Acting Deputy Director, Mr. Okimoto served as Interim Director from December 2002 to January 2003. Mr. Okimoto is also the current Department of Transportation, Harbors Division Administrator. Mr. Okimoto also served as the State Comptroller of the Department of Accounting and General Services and as Deputy Director of Transportation where he was responsible for administrative functions of the Department of Transportation, including budget, fiscal and personnel matters. Prior to assuming this position, he served as the Program Evaluation Analysis Manager (1989-1994) and Economist (1981-1989) for the Department. Before joining the Department, Mr. Okimoto was a research assistant at the University of Hawaii. Mr. Okimoto received a Masters of Science and Doctor of Philosophy degree in Resource Economics from the University of Hawaii.

Glenn M. Yasui, Highways Division Administrator, assumed the position of Administrator on June 1, 2001. He is responsible for the operations, maintenance and management of the State Highway System and the planning, design and

construction of new state highways and ancillary facilities. Prior to assuming this position, he served as the Senior Transportation Engineer with the Federal Highway Administration, Hawaii Division. Mr. Yasui has over 38 years of highway engineering and administrative experience. From 1964 to 2001, he worked for the Federal Highway Administration in progressive positions of responsibility including Highway Engineer, Assistant Area Engineer, Area Engineer, Urban Transportation Engineer and Senior Transportation Engineer/Territorial Representative. Mr. Yasui graduated from the University of Hawaii with a Bachelor of Science in Civil Engineering in 1964 and received a Master of Public Administration from the University of Southern California in 1985. He is a member of the American Society of Civil Engineers and the Institute of Transportation Engineers. Mr. Yasui is Licensed Professional Engineer (Civil) in Hawaii, California, Guam and the Commonwealth of the Northern Mariana Islands. While with the Federal Highway Administration, Mr. Yasui guided the successful completion of the \$1.4 billion Interstate Route H-3 project and managed the marketing, technology transfer and implementation of the state-of-art Intelligent Transportation System (ITS) projects in Hawaii. He was also responsible for improving the efficiency and effectiveness of the programming, planning, design and construction processes of the Federal-aid highway programs in the State of Hawaii, the Territory of American Samoa, the Territory of Guam and the Commonwealth of the Northern Mariana Islands.

Gerald K.L. Dang, Administrative Services Officer, became the head of the Staff Services Office of the Highways Division in July 1995. He is responsible for project programming, budgeting, fiscal and personnel activities of the Highways Division. Prior to joining the Department, Mr. Dang served as the Administrative Services Officer for the Department of Business, Economic Development and Tourism (1993-1995), and Budget and Accounting Officer for the Department of Accounting and General Services (1990-1993), and Accountant for various state agencies from 1980-1990. Mr. Dang received a bachelor's degree in Business Administration from the University of Hawaii.

Employees

The Highways Division presently has approximately 1,000 employees. Hawaii law grants public employees in Hawaii, except appointed officials and division administrators, the right to organize for the purpose of collective bargaining. Each recognized bargaining unit designates an employee organization as the exclusive representative of all employees of such unit, which organization negotiates with the public employer.

Substantially all of the Highways Division employees are represented by bargaining units. Generally, blue collar workers are represented by United Public Workers, Local 606. Blue collar supervisors, white collar workers and white collar supervisors are represented by Hawaii Government Employees' Association, Local 152, American Federation of State, County and Municipal Employees.

CAPITAL IMPROVEMENT PROGRAM

General

In every odd-numbered year, the Department prepares for the Governor's approval a capital improvements program for the next six fiscal years, describing ongoing and proposed State Highway System capital improvement projects which the Department proposes to undertake during that period. After the Governor's review, the succeeding two fiscal years' capital improvement projects for the State Highway System are submitted to the Legislature as a part of the Administration's executive biennium budget. The Legislature reviews the executive biennium budget in detail and authorizes all or a portion of the executive biennium budget by individual capital improvement project. Subsequently, in every even-numbered year, the Department may amend the second year of that executive biennium budget for presentation to the Governor for approval and to the Legislature for supplemental authorization.

Authorization of a capital improvement project by the Legislature as a part of the executive biennium budget includes the appropriation of moneys from a designated source to pay for that project. Since the Legislature only appropriates for a two-year period, appropriations to complete capital improvement projects extending beyond that period must be approved by subsequent Legislatures. An appropriation of bond funds to match federal funds does not lapse.

The Legislature can appropriate funds for the State Highway System capital improvement projects from six sources: bonds (either general obligation bonds, reimbursable general obligation bonds or revenue bonds), federal funds, the State general fund, special funds, other funds (such as AMTRAK funds) and private contributions (such as private development impact fees). The Legislature also authorizes the issuance of bonds to fund the appropriation for which bond funds are designated as the source for payment of a capital improvement project.

The Department prepares a three year multimodal transportation improvement program for U.S. Department of Transportation review and approval, that is updated every two years. This program, called the Statewide Transportation Improvement Program ("STIP"), includes all projects for which the Department will request federal aid during the three year period. See Appendix B - "ADDITIONAL INFORMATION RELATING TO REVENUE SOURCES, THE STATE HIGHWAY SYSTEM AND THE DEPARTMENT OF TRANSPORTATION" for additional information regarding the STIP.

The Program includes many capital improvement projects still in the preliminary stage. As the Program is continuously developed and revised, the individual capital improvement projects included in the Program undergo changes in priority, timing and cost. The current Program for fiscal years 2003 through 2008 provides authorization for completion of previously approved capital improvement projects, for new capital improvement projects, and for certain additional capital improvement projects which have not yet been authorized.

The Program consists of separate capital improvement projects on the six major islands of the State. From the first year of issuance of Highway Revenue Bonds in 1993 through 2002, the Legislature has appropriated a total of \$1.661 billion, excluding lapses, for the planning, design, and acquisition and construction of projects.

Plan of Finance

The Governor and the Legislature have approved the funding sources for all appropriations made in prior fiscal years. Of the \$1.661 billion appropriated from 1993 through the 2002 session, excluding lapses, the Department has been authorized to finance approximately \$958.52 million with federal funds, approximately \$153.18 million with available State Highway funds, approximately \$2.02 million with the proceeds from general obligation bonds, approximately \$535.99 million with the proceeds from the sale of revenue bonds and approximately \$11.52 million with other funds.

The Department has previously received federal funds for surface transportation projects under the Intermodal Surface Transportation Efficiency Act of 1991 ("ISTEA"). In 1998, the Transportation Equity Act for the 21st Century (TEA-21) to provide for federal aid was passed by Congress, and the Department expects that the level of funding that it receives under the TEA-21 legislation will be the same as or greater than the levels it has received in the past. Accordingly, the Department does not expect any material adverse impact as a result of the TEA-21 legislation.

Historically the Department financed a major portion of the State's share of the cost of capital improvement projects using reimbursable general obligation bonds. The Department is required to reimburse the State general fund for the payment of the principal of and interest on such bonds. See "DEBT SERVICE COVERAGE -Reimbursable General Obligation Bonds" for additional information.

Beginning in 1993, the State determined to finance the Program by issuing revenue bonds secured by a pledge of the Pledged Funds rather than by issuing reimbursable general obligation bonds. The Department has previously issued \$75 million in such revenue bonds in 1993, \$55 million in 1996, \$95 million in 1998, \$50 million in 2000 and \$70 million in 2001.

DEBT SERVICE COVERAGE

Projected Revenues

The Department's current forecast of Revenues assumes that future Revenues will grow at a lower rate than the historical growth. The forecast reflects an upward growth trend, with Revenues increasing at an average annual rate of approximately one percent (1%), exclusive of any fuel tax increase.

The actual Revenues which will be collected and deposited into the State Highway Fund may vary from this projection because of fluctuating economic conditions, changes by the Legislature in the laws governing the Pledged User Taxes and other variables affecting Revenues. Such variances *could be* material.

Projected Revenues Fiscal Years Ending June 30, 2003 through June 30, 2009 (in thousands of \$)

Fiscal Year	<u>Pledged User Taxes</u>						Total Revenues
	Fuel Taxes	Registration Fee	Weight Taxes	Rental/ Tour Vehicle Surcharge(1)	Interest	Misc. (2)	
2003	73,722	17,692	26,077	36,516	13,900	2,621	170,528
2004	73,570	18,203	26,915	38,223	12,900	2,741	172,552
2005	74,246	18,434	27,548	38,684	11,900	2,758	173,570
2006	74,922	18,665	28,181	39,144	10,900	2,775	174,587
2007	75,598	18,896	28,814	39,605	10,900	2,793	176,606
2008	76,275	19,128	29,446	31,596	10,900	2,812	170,157
2009	76,951	19,359	30,079	32,639	10,900	2,832	172,760

- (1) Reflects \$1.00 increase in the rental car surcharge by Act 223/99, effective September 1, 1999 to August 31, 2007.
- (2) Miscellaneous Revenues include vehicle weight tax penalties, periodic motor vehicle inspection charges, rents from State Highway System properties, commercial license fees, and other miscellaneous Revenues.

Source: Department of Transportation

Debt Service Requirements for the Bonds

The following table sets forth the principal and interest requirements for the 2003 Bonds and the Outstanding Bonds:

Fiscal Year	Outstanding Debt(1)	DEBT SERVICE 2003 Refunding Bonds Debt Service			Total Debt Service
		Principal	Interest	Total	
2003	\$23,655,579		\$368,352	\$368,352	\$24,023,931
2004	18,914,976	\$3,875,000	1,744,825	5,619,825	24,534,801
2005	18,905,575	3,960,000	1,667,325	5,627,325	24,532,900
2006	18,915,045	4,025,000	1,550,800	5,575,800	24,490,845
2007	18,916,389	4,175,000	1,450,175	5,625,175	24,541,564
2008	18,907,743	4,310,000	1,307,200	5,617,200	24,524,943
2009	18,887,468	4,480,000	1,147,900	5,627,900	24,515,368
2010	18,888,275	4,750,000	946,400	5,696,400	24,584,675
2011	18,887,100	4,900,000	740,150	5,640,150	24,527,250
2012	18,890,817	5,105,000	519,650	5,624,650	24,515,467
2013	18,891,318	5,360,000	264,400	5,624,400	24,515,718
2014	24,752,862				
2015	24,756,395				
2016	24,757,200				
2017	24,745,681				
2018	24,749,189				
2019	9,810,225				
2020	9,807,569				
2021	5,670,468				
2022	5,670,000				
TOTALS	\$367,379,871	\$44,940,000	\$11,707,177	\$56,647,177	\$269,307,459

(1) Assumes that all Series 1993 Bonds maturing 7/1/04 through 7/1/13 will be refunded with the proceeds of the Series 2003 Refunding Bonds.

Source: Department of Transportation

Historic and Projected Debt Service Coverage

The following table sets forth historical and projected debt service coverage for fiscal years ending June 30, 1994 through 2008. (A fiscal year is a twelve month period ending on a June 30). Debt service for the fiscal years ending June 30, 1994 through 2002 is based on the actual interest rates for the Outstanding Bonds. Debt service projections for future fiscal years are based on the interest rates for the Outstanding Bonds and an assumed rate of 3.98% for the 2003 Bonds. Revenues for the fiscal years ending June 30, 1994 through 2002 are based on actual Revenues for such fiscal years; projected Revenues for present and future fiscal years are based on the Department's projections identified in the table entitled "Projected Revenues" under "DEBT SERVICE COVERAGE" herein. (The Department calculates Revenues on the basis of its fiscal year).

**HISTORIC AND PROJECTED DEBT SERVICE COVERAGE
(Revenue Bond Debt Service Only)**

Fiscal Year	Pledged Revenues(1)	Outstanding Revenue Bond Debt Service(2)	Series 2003 Refunding Bonds Debt Service	Aggregate Revenue Bond Debt Service	Total Debt Supported By Highway Revenue	Coverage (Revenue and G.O. Bonds) (1)
1994	\$133,231,000	\$5,865,243		\$5,865,243	\$34,432,901	3.87
1995	141,015,000	5,864,683		5,864,683	33,594,010	4.20
1996	142,668,000	5,868,562		5,868,562	55,590,280	2.57
1997	144,372,000	10,003,143		10,003,143	50,386,386	2.87
1998	141,784,000	10,434,609		10,434,609	41,736,315	3.40
1999	144,403,000	14,408,883		14,408,883	43,493,604	3.32
2000	158,646,000	14,965,993		14,965,993	38,111,771	4.16
2001	172,757,000	17,954,646		17,954,646	45,228,599	3.82
2002	172,307,000	21,452,982		21,452,982	45,947,073	3.75
2003	170,528,000	23,655,579	\$368,352	24,009,699	41,867,895	4.07
2004	172,552,000	18,914,976	5,619,825	24,529,651	38,586,800	4.47
2005	173,570,000	18,905,575	5,627,325	24,529,050	38,344,106	4.53
2006	174,587,000	18,915,045	5,575,800	24,535,520	41,807,732	4.18
2007	176,606,000	18,916,389	5,625,175	24,532,264	42,183,248	4.19
2008	170,157,000	18,907,743	5,617,200	24,530,868	41,612,694	4.09
2009	172,760,000	18,887,468	5,627,900	24,504,968	40,312,749	4.29

(1) Actual for 1994 through 2002; projected for 2003 through 2009.

(2) Assumes that all Series 1993 Bonds maturing 7/1/04 through 7/1/13 will be refunded with the proceeds of the Series 2003 Refunding Bonds.

Source: Department of Transportation.

**HISTORIC AND PROJECTED DEBT SERVICE COVERAGE
(Total Debt Service Supported by Highway Revenue)**

Fiscal Year	Pledged Revenues (1)	Outstanding Revenue Bond Debt Service (2)	Series 2003 Refunding Bonds Debt Service	Aggregate Revenue Bond Debt Service	G.O. Debt Service	Total Debt Supported By Highway Revenue	Coverage (Revenue and G.O. Bonds) (1)
1994	\$133,231,000	\$5,865,243		\$5,865,243	\$28,567,658	\$34,432,901	3.87
1995	141,015,000	5,864,683		5,864,683	27,729,327	33,594,010	4.20
1996	142,668,000	5,868,562		5,868,562	49,721,718	55,590,280	2.57
1997	144,372,000	10,003,143		10,003,143	40,383,243	50,386,386	2.87
1998	141,784,000	10,434,609		10,434,609	31,301,706	41,736,315	3.40
1999	144,403,000	14,408,883		14,408,883	29,084,721	43,493,604	3.32
2000	158,646,000	14,965,993		14,965,993	23,145,778	38,111,771	4.16
2001	172,757,000	17,954,646		17,954,646	27,273,953	45,228,599	3.82
2002	172,307,000	21,452,982		21,452,982	24,494,091	45,947,073	3.75
2003	170,528,000	23,655,579	\$354,120	24,009,699	17,858,196	41,867,895	4.07
2004	172,552,000	18,914,976	5,614,675	24,529,651	14,057,149	38,586,800	4.47
2005	173,570,000	18,905,575	5,623,475	24,529,050	13,815,057	38,344,106	4.53
2006	174,587,000	18,915,045	5,620,475	24,535,520	17,272,212	41,807,732	4.18
2007	176,606,000	18,916,389	5,615,875	24,532,264	17,650,985	42,183,248	4.19
2008	170,157,000	18,907,743	5,623,125	24,530,868	17,081,826	41,612,694	4.09
2009	172,760,000	18,887,468	5,617,500	24,504,968	15,807,781	40,312,749	4.29

(1) Actual for 1994 through 2002; projected for 2003 through 2009.

(2) Assumes that all Series 1993 Bonds maturing 7/1/04 through 7/1/13 will be refunded with the proceeds of the Series 2003 Refunding Bonds.

Source: Department of Transportation.

Reimbursable General Obligation Bonds

As of June 30, 2002, there were outstanding \$143,715,292 reimbursable general obligation bonds issued for the State Highway System. These bonds are general obligation bonds of the State, but since the proceeds of these bonds were used to finance improvements to the State Highway System, the Department is required to reimburse the State general fund for the payment of the principal of and interest on such bonds. Reimbursement currently is made principally from the Pledged User Taxes, and occurs after the payment of the principal of and interest on the Bonds, including reserves therefor, and the costs of operation and maintenance and improvement of the State Highway System.

The following table sets forth the principal and interest requirements for all reimbursable general obligation bonds outstanding as of June 30, 2003. Debt service requirements on the reimbursable general obligation bonds are set forth in the year in which they are scheduled to be paid. There are no current legislative authorizations for additional reimbursable general obligation bond funded State highway projects.

**STATE HIGHWAY SYSTEM REIMBURSABLE
GENERAL OBLIGATION BOND DEBT SERVICE**

Fiscal Year Ending <u>June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Reimbursable General Obligation Bond Debt Service</u>
2002	\$17,781,182	\$6,712,908	\$24,494,091
2003	12,446,521	5,411,674	17,858,196
2004	9,182,553	4,874,596	14,057,149
2005	9,355,578	4,459,479	13,815,057
2006	13,252,351	4,019,862	17,272,212
2007	14,296,149	3,354,836	17,650,985
2008	14,413,816	2,668,010	17,081,826
2009	13,834,939	1,972,842	15,807,781
2010	8,700,652	1,317,718	10,018,370
2011	8,833,459	869,460	9,702,919
2012	6,146,269	477,141	6,623,409
2013	3,056,305	176,841	3,233,146
2014	2,270,819	99,347	2,370,166
2015	2,016,916	54,872	2,071,788
2016	645,181	17,268	662,449
2017	146,746	10,856	157,603
2018	19,328	4,136	23,464
2019	20,308	3,170	23,477
2020	21,334	2,154	23,488
2021	22,409	1,088	23,496

Source: Department of Transportation

LITIGATION

The State is subject to litigation in connection with the day-to-day operation of the State Highway System by the Department. There are no claims or judicial proceedings affecting the State Highway System or the Pledged Funds, except for claims incidental to the operation of the State Highway System. The State is self-insured with respect to tort claims against the Department and the State Highway System. To pay for tort judgments and settlements involving the State Highway System, the Legislature appropriates money from the State Highway Fund after providing for payment of the Bonds and required reserves. There is no litigation now pending or threatened to restrain or to enjoin the issuance and delivery of the 2003 Bonds or the power and authority of the Department or the State to impose, prescribe or collect Pledged User Taxes or in any manner questioning the power and authority of the Department or State to impose, prescribe or collect such Pledged User Taxes or to issue and deliver the 2003 Bonds or affecting the validity of the 2003 Bonds.

TAX MATTERS

Concurrently with the delivery of the 2003 Bonds, McCorriston Miller Mukai MacKinnon LLP, Bond Counsel, will deliver its legal opinion addressing certain tax matters relating to the 2003 Bonds. A complete copy of Bond Counsel's proposed legal opinion is attached as Appendix E hereto.

In the opinion of Bond Counsel, under existing federal tax laws, as presently enacted and construed, interest on the 2003 Bonds is excluded from gross income for federal income tax purposes under Section 103(a) of the Internal

Revenue Code of 1986, as amended (the "Code"), and is not an item of tax preference for purposes of the alternative minimum tax imposed on individuals and corporations under the Code. However, interest on the 2003 Bonds is included in the adjusted current earnings of certain corporations for purposes of computing their alternative minimum tax liability under the Code. Bond Counsel is of the further opinion that, under the laws of the State, as presently enacted and construed, the 2003 Bonds and the income therefrom are exempt from all taxation by the State or any county or other political subdivision thereof, except inheritance, transfer and estate taxes, and the franchise tax imposed on banks and other financial institutions.

Bond Counsel's opinion will assume the accuracy of certain representations and certifications of the State as to facts, circumstances, estimates and expectations which are material to the exclusion of interest on the 2003 Bonds from gross income under the Code. Bond Counsel has not undertaken any independent investigation of the accuracy of such representations and certifications.

Bond Counsel's opinion will further assume compliance with certain requirements of the Code which must be met subsequent to the issuance of the 2003 Bonds in order for the interest thereon to be and to remain excluded from gross income for federal income tax purposes. The State has covenanted to comply with such requirements so as to ensure that the interest on the 2003 Bonds is and will remain excluded from gross income. Noncompliance with these requirements may cause the interest on the 2003 Bonds to be included in gross income, and therefore subject to federal income tax, retroactively to the date of their issuance. Bond Counsel has not undertaken to determine or advise whether any actions taken or omitted by the State or other events or circumstances may adversely affect the tax status of the 2003 Bonds.

Purchasers of the 2003 Bonds should be aware that the ownership or disposition of the 2003 Bonds, or the accrual or receipt of interest thereon, may have collateral tax consequences to certain taxpayers under the Code, including certain corporations, financial institutions, insurance companies, recipients of Social Security and Railroad Retirement benefits, those that are deemed to incur or continue indebtedness to acquire or carry tax-exempt obligations and individuals otherwise eligible for the earned income tax credit. In addition, the interest on the 2003 Bonds may be subject to a branch profits tax imposed on certain foreign corporations doing business in the United States. The applicability and extent of such tax consequences will depend upon the particular tax status or other tax items of the owner of the Bonds. Bond Counsel expresses no opinion regarding such consequences.

CERTAIN LEGAL MATTERS

Certain legal matters incident to the authorization, issuance and sale of the 2003 Bonds are subject to the approval of McCorriston Miller Mukai Mackinnon LLP, Bond Counsel to the State. Copies of the approving opinion of Bond Counsel will be available at the time of delivery of the 2003 Bonds. The form of opinion Bond Counsel proposes to render is set forth in Appendix E hereto. Bond Counsel undertakes no responsibility for the accuracy, completeness or fairness of this Official Statement. Certain legal matters will be passed upon for the Underwriter by its counsel, Pillsbury Winthrop LLP.

The Sixth Supplemental Certificate of the Director, providing for the issuance of the 2003 Bonds, will be approved as to form and legality by the Attorney General of the State.

RATINGS

Moody's Investors Service, Standard & Poor's and Fitch have assigned ratings of "Aaa", "AAA" and "AAA" respectively, to the Insured Bonds, in each case based upon the understanding that upon delivery of the 2003 Insured Bonds, Financial Security will issue its Bond Insurance Policy with respect to the Insured Bonds. Moody's, Standard & Poor's and Fitch have also assigned underlying ratings of Aa3, AA and AA-, respectively, to the Uninsured Bonds, in each case determined without regard to the Bond Insurance Policy.

Such ratings reflect only the views of such organizations and any desired explanation of the significance of such ratings should be obtained from the rating agency furnishing the same, at the following addresses: Moody's Investors

Service, 99 Church Street, New York, New York 10007; Standard & Poor's, 25 Broadway, New York, New York 10004; and Fitch IBCA, Inc., One State Street Plaza, New York, New York 10004. Generally a rating agency bases its rating on the information and materials furnished to it and on investigations, studies and assumptions of its own. There is no assurance that either of such ratings will continue for any given period of time or that such ratings will not be revised downward, suspended or withdrawn entirely by the rating agencies if, in the judgment of such rating agencies, circumstances so warrant. The State undertakes no responsibility to oppose any such revision, suspension or withdrawal. Any such downward revision, suspension or withdrawal of such ratings may have an adverse effect on the market price of the 2003 Bonds.

ESCROW VERIFICATION

Causey, Demgen & Moore Inc., a firm of independent public accountants, will deliver to the State and Bond Counsel its report indicating that it has examined, in accordance with standards established by the American Institute of Certified Public Accountants, the information and assertions provided by the State and its representatives related to the refunding of the 1993 Bonds effected from the proceeds of the 2003 Bonds. See "THE 2003 BONDS". Included in the scope of its examination will be a verification of the mathematical accuracy of the mathematical computations of the adequacy of the cash, the maturing principal amounts and the interest on the Federal Securities deposited with the Escrow Agent to pay the interest, principal and redemption price coming due on the 1993 Bonds on and prior to their respective maturity or redemption dates as described in "THE 2003 BONDS."

UNDERWRITING

The 2003 Bonds are being purchased by the A.G. Edwards & Sons, Inc. (the "Underwriter"). The Underwriter has agreed to purchase the 2003 Bonds at a price of \$47,271,609, which includes net original issue premium, and will retain an underwriting discount of \$312,962. The Underwriter will be responsible for the payment of certain costs of issuing the 2003 Bonds. The Purchase Contract provides that the Underwriter will purchase all of the 2003 Bonds, if any are purchased, the obligation to make such purchase being subject to certain terms and conditions set forth in the Purchase Contract, the approval of certain legal matters by counsel and certain other conditions. The initial public offering prices of the 2003 Bonds may be changed from time to time by the Underwriter. The Underwriter may offer and sell the 2003 Bonds to certain dealers (including dealers depositing 2003 Bonds into unit investment trusts, certain of which may be sponsored or managed by the Underwriter) at prices lower than the public offering prices stated on the cover of this Official Statement.

CONTINUING DISCLOSURE

The Department has executed a Continuing Disclosure Certificate (the "Disclosure Certificate") for the benefit of the Holders and beneficial owners of the 2003 Bonds to provide certain financial information and operating data relating to the Department to certain information repositories annually and to provide notice to the Municipal Securities Rulemaking Board of the occurrence of certain enumerated events, if material, pursuant to the requirements of Section (b)(5)(i) of Securities and Exchange Commission Rule 15c2-12 (17 C.F.R. § 240.15c2-12) (the "Rule"). See Appendix F - "FORM OF CONTINUING DISCLOSURE CERTIFICATE."

A failure by the Department to comply with the Disclosure Certificate will not constitute an event of default under the Certificate or on the 2003 Bonds. Any such failure must be reported in accordance with the Rule and must be considered by any broker, dealer or municipal securities dealer before recommending the purchase or sale of the 2003 Bonds in the secondary market. Consequently, such a failure may adversely affect the transferability and liquidity of the 2003 Bonds and their market price. The State has never failed to comply in all material respects with any previous undertakings with regard to the Rule to provide annual reports or notices of material events. The Department has complied in all material respects with all previous similar undertakings under continuing disclosure certificates.

The obligations of the Department described in the Disclosure Certificate will remain in effect until the 2003 Bonds are no longer Outstanding (within the meaning of the Certificate) or the Rule no longer applies to the 2003 Bonds. Any provision of the Disclosure Certificate may be amended or waived upon the conditions set forth therein.

The Disclosure Certificate is solely for the benefit of the Holders and beneficial owners from time to time of the 2003 Bonds. The exclusive remedy for any breach of the Disclosure Certificate by the Department is limited to the right of the Holders and beneficial owners to cause to be instituted and maintained proceedings to obtain specific performance by the Department of its obligations under the Disclosure Certificate. Any such proceedings challenging the adequacy of the information provided in accordance with the Disclosure Certificate may be instituted and maintained only by Holders and beneficial owners of not less than 25% in principal amount of the 2003 Bonds then Outstanding.

FINANCIAL STATEMENTS

The audited financial statements of the Highways Division as of and for the fiscal year ended June 30, 2002, are set forth in Appendix D to this Official Statement. These financial statements have been audited by PricewaterhouseCoopers LLP, Honolulu, Hawaii, independent certified public accountants, whose report is set forth in Appendix D.

MISCELLANEOUS

The references in this Official Statement to Acts of the Legislature and the Certificate (including the supplements thereto) do not purport to be complete and are subject to the detailed provisions thereof to which reference is hereby made. The Acts and other Hawaii statutes may be amended by the Legislature. The Department has provided the information in this Official Statement relating to the Highways Division, and other matters, as indicated.

All statements in this Official Statement involving matters of opinion, estimates, forecasts, projections, or the like, whether or not expressly so stated, are intended as such and not as representations of fact. No representation is made that any such statements will be realized. The agreements of the Department and the State are fully set forth in the Certificate and the General Revenue Bond Law, and the Official Statement is not to be construed as a contract or agreement between the Department or the State and the purchasers or Holders of any of the 2003 Bonds.

DEPARTMENT OF TRANSPORTATION
STATE OF HAWAII


/s/ Rodney K. Haraga
By: Rodney K. Haraga
Director of Transportation

SUMMARY OF CERTAIN PROVISIONS OF THE CERTIFICATE

For purposes of this Appendix A, Certificate means the Certificate of the Director of Transportation Providing for the Issuance of State of Hawaii Highway Revenue Bonds, dated as of August 1, 1993, as heretofore supplemented and as further supplemented by the Sixth Supplemental Certificate. The following is a summary of certain of the provisions of the Certificate. The summary does not purport to be complete or to follow the exact language of the Certificate, and, accordingly, is qualified by reference thereto and is subject to the full text thereof. Capitalized terms not otherwise previously defined in this Official Statement or defined below have the meanings set forth in the Certificate. For the complete provisions of the Certificate and the precise wording thereof, reference should be made to the Certificate, copies of which are available upon request at the office of the Department. Unless clearly indicated otherwise, all section references are to the Certificate only.

Definitions of Certain Terms [Certificate Section 1.01]

The following are definitions in summary form of certain terms contained in the Certificate and used in this Official Statement.

“Aggregate Bond Service” means, as of any date of calculation and with respect to any period, the sum of the amounts of Bond Service for all Series of Bonds for such period.

“Average Annual Bond Service” of a Series of Bonds means the result obtained by dividing (A) the aggregate Bond Service for such Series for the period from the date of issuance of such Series until the final maturity date of such Series by (B) the number of Bond Years in such period.

“Bond Service” means, as of any date of calculation and with respect to any period for any Series of Bonds, an amount equal to the sum of: (i) the interest accruing during such period on the Bonds of such Series, except to the extent that such interest is to be paid from (y) amounts credited to the Highway Senior Interest Subaccount or the Highway Subordinate Interest Subaccount, (z) any other account set aside exclusively for the payment of interest, and (ii) that portion of the next succeeding Principal Installment for the Bonds of such Series accruing during such period assuming each such Principal Installment were deemed to accrue daily (based on a year of 12 months each of 30 days’ duration) in equal amounts from the next preceding Principal Installment due date (or, in the event there shall have been no such preceding Principal Installment due date for such Series, then from a date one year preceding the due date of such Principal Installment or from the date of delivery of the Bonds of such Series, whichever is later). Such interest and Principal Installments shall be calculated on the assumption that no Bonds of such Series Outstanding at the date of calculation will cease to be Outstanding except by reason of the payment of each Principal Installment for the Bonds of such Series on the due date thereof. The Bond Service definition contains additional provisions concerning the calculation of debt service on Variable Rate Bonds and Capital Appreciation Bonds.

“Bond Year” means, with respect to any series of Bonds, any period of 12 consecutive months terminating on the due date of a Principal Installment for the Bonds of such series; provided that the initial Bond Year for each series shall be of such duration as is set forth in the Supplemental Certificate providing for such series.

“Code” means the Internal Revenue Code of 1986, as from time to time amended, and any successor statute thereto, and any Treasury regulations or proposed regulations thereunder.

“Federal Securities” means any of the following:

(i) any direct and general obligations of, or any obligations fully and unconditionally guaranteed as to the full and timely payment of principal and interest by, the United States of America;

(ii) obligations issued or guaranteed by any of the following federal agencies, provided that such obligations are backed by the full faith and credit of the United States of America; Export-Import Bank of the United States (backed by the full faith and credit of USA); Government National Mortgage Association (Ginnie Mae) (backed by the full faith and credit of USA); Public Housing Authority (backed by the full faith and credit of USA); Farm Credit System Financial Assistance Corporation (senior debt rated in highest category by the Rating Agencies); Student Loan Marketing Association (Sallie Mae) (senior debt rated in highest category by the Rating Agencies); Tennessee Valley Authority (senior debt rated in highest category by the Rating Agencies); Inter-American Development Bank (senior debt rated in highest category by the

Rating Agencies); World Bank (International Bank for Reconstruction & Development) (senior debt rated in highest category by the Rating Agencies); Federal Farm Credit Banks (Consolidated Systemwide Bonds) (senior debt rated in highest category by the Rating Agencies); Federal Home Loan Banks (consolidated debt of banks and deposits of 8 of the 12 individual banks rated in highest category by the Rating Agencies); Federal Home Loan Mortgage Corp. (senior debt (not subordinated debt) rated in highest category by the Rating Agencies); Federal National Mortgage Association (senior debt (not subordinated debt) rated in highest category by the Rating Agencies); and Resolution Funding Corporation (Refcorp) (rated in highest category by the Rating Agencies);

(iii) any obligations of any state or political subdivision of a state (collectively, "Municipal Bonds") which Municipal Bonds are either (A) rated "Aaa" by Moody's and "AAA" by S&P (whether such rating is based upon the credit of the issuer, an insurance policy, a letter of credit or otherwise) or (B) are fully secured as to principal and interest by an irrevocable pledge of moneys or direct and general obligations of, or obligations guaranteed by, the United States of America, which moneys or obligations are segregated in trust and pledged for the benefit of the holder of the Municipal Bonds, and which Municipal Bonds are rated "Aaa" by Moody's and "AAA" by S&P and provided, however, that such Municipal Bonds are accompanied by (a) an opinion of Bond Counsel to the effect that such Municipal Bonds are not subject to redemption prior to the date the proceeds of such Municipal Bonds will be required for the purposes of the investment being made therein and (b) a report of an Independent Public Accountant verifying that the moneys and obligations so segregated are sufficient to pay the principal of, premium, if any, and interest on the Municipal Bonds; and

(iv) securities commonly referred to as CATs, TGRs, STRIPS, or other certificates of direct ownership of the principal of, or interest on, direct and general obligations of the United States of America or certificates of direct ownership of the interest on obligations of the Resolution Funding Corporation, which obligations are held by a commercial bank which is a member of the Federal Reserve System in trust on behalf of the holders of the derivative product;

provided, however, that the term Federal Securities shall exclude unit investment trusts or mutual funds which otherwise meet the criteria set forth above in clauses (i) through (iv) unless the trust or fund is in the highest rating category of the Rating Agency.

"Highway Bond Proceeds Account" means the special account created in the State Bond Fund into which shall be credited proceeds of any Bond for the payment of the costs of highway and road projects, and other related facilities and properties constituting a part of the Undertaking.

"Highway Revenue Special Account" means the special account of that name created in the Certificate in the State Highway Fund.

"Highway Senior Debt Service Reserve Subaccount" means the separate special subaccount of the Department created pursuant to the Certificate in the Highway Revenue Special Account and designated as the "Highway Senior Debt Service Reserve Subaccount."

"Highway Senior Interest Subaccount" means the separate special subaccount of the Department created pursuant to the Certificate in the Highway Revenue Special Account and designated as the "Highway Senior Interest Subaccount."

"Highway Senior Principal Subaccount" means the separate special subaccount of the Department created pursuant to the Certificate in the Highway Revenue Special Account and designated as the "Highway Senior Principal Subaccount."

"Highway Subordinate Debt Service Reserve Subaccount" means the separate special subaccount of the Department created pursuant to the Certificate in the Highway Revenue Special Account and designated as the "Highway Subordinate Debt Service Reserve Subaccount."

"Highway Subordinate Interest Subaccount" means the separate special subaccount of the Department created pursuant to the Certificate in the Highway Revenue Special Account and designated as the "Highway Subordinate Interest Subaccount."

"Highway Subordinate Principal Subaccount" means the separate special subaccount of the Department created in the Highway Revenue Special Account and designated as the "Highway Subordinate Principal Subaccount."

"Operation and Maintenance Expenses" means the expenses of operation, maintenance and repair of the properties constituting the Undertaking, including without limitation, the cost of equipment and general administrative overhead in connection with those properties, but excluding any (i) arbitrage earnings which are required to be paid to the United States Government pursuant

to Section 148 of the Code, (ii) depreciation expense, and (iii) surcharges imposed by the State for central services relating to administration of funds of the Department.

“Outstanding”, when used with respect to any Bond, shall have the construction given to such word in Section 11.01 of the Certificate, as described below under “Discharge of Obligations of the State Under the Certificate”. For purposes of the Certificate, in the event any Bonds of a Series are issued and sold at a price such that a portion or all of the interest thereon is intended to be earned by accrual of original issue discount or the compounding of interest, the amount of such Bonds deemed to be Outstanding for the purpose of calculating the principal amount of any such Bonds and the principal amount of Bonds Outstanding in connection with the exercise of any voting right or privilege, the giving of any consent or direction or the taking of any other action that the Holders of the Bonds are entitled to take pursuant to Articles X and XI of the Certificate or otherwise, shall be the accreted value thereof.

“Pledged Funds” means the Revenues and the moneys held in the Highway Revenue Special Account, the Highway Bond Proceeds Account and such other funds and accounts which may be hereafter pledged to the payment of the principal of and interest on the Bonds.

“Pledged User Taxes” means the highway fuel license taxes, the vehicle weight taxes, the vehicle registration fees, the rental motor vehicle surcharge taxes and tour vehicle surcharge taxes, respectively levied and paid pursuant to Sections 243-4, 249-33, 249-31, and 251-2, Hawaii Revised Statutes, and other user taxes, fees or charges currently or hereafter derived from or arising through the ownership, operation, and management of the Undertaking and the furnishing and supplying of the services thereof, which are deposited in the State Highway Fund and made available pursuant to State law for the payment of the Bonds.

“Principal Installment” means, as of any date of calculation and with respect to any Series of Bonds, so long as any Bonds thereof are Outstanding: (i) the principal amount of Bonds of such Series due on a certain future date for which no Sinking Fund Installments have been established, or (ii) the unsatisfied balance (determined as provided in the definition of “Sinking Fund Installment”) of any Sinking Fund Installment due on a certain future date for Bonds of such Series which would be applicable upon redemption of such Bonds on such future date in a principal amount equal to such unsatisfied balance of such Sinking Fund Installment, or (iii) if such future dates coincide as to different Bonds of such Series, the sum of such principal amount of Bonds and of such unsatisfied balance of such Sinking Fund Installment due on such future date.

“Rating Agency” means Moody’s Investors Service and Standard & Poor’s Corporation and their respective successors and assigns or, if either (or both) shall for any reason no longer perform the functions of a securities rating agency, such other nationally recognized rating agency designated by the Department; provided, however, that any reference to a Rating Agency (other than in the definition of Federal Securities) shall only be effective while such Rating Agency is providing a rating on the Outstanding Bonds.

“Reimbursable General Obligation Bonds” means general obligation bonds of the State to which the State has pledged its full faith and credit and which are payable from the general fund of the State, the proceeds of which were or are to be used to finance highway and road projects with respect to properties constituting part of the Undertaking, and with respect to which the general fund of the State is to be reimbursed from Revenues, except insofar as the obligation or reimbursement has been or is canceled by the State Legislature.

“Reserve Fund Facility” means each Support Facility at any time on deposit in the Highway Senior Debt Service Reserve Subaccount, including the Series 2003 Reserve Fund Policy.

“Reserve Requirement” means with respect to Senior Bonds or Subordinate Bonds, an amount, as of any date of determination, equal to one-half (1/2) of the maximum Aggregate Bond Service for Senior Bonds or Subordinate Bonds, as the case may be, in any Bond Year, beginning with the Bond Year in which the date of determination occurs and ending with the Bond Year after which no Senior Bonds or Subordinate Bonds, as the case may be, are Outstanding.

“Revenues” means and includes the items set forth below when and to the extent the same are deposited in the State Highway Fund to the credit of the Highway Revenue Special Account: (A) all income, revenues and moneys collected by the State from the ownership or operation of the Undertaking or the supplying and furnishing of the services, facilities and commodities thereof, and without limiting the generality of the foregoing, shall include all income, revenues and moneys derived from rates, rentals, fees, tolls and charges prescribed for the uses and services of, and the facilities and commodities furnished by, the Undertaking; (B) earnings on the investment of moneys held under the Certificate and the proceeds of the sale of any such investments; (C) income, revenues and moneys paid to the State or the Department with respect to properties that constitute part of the Undertaking on the effective date of the Certificate but are sold, leased or otherwise disposed of or transferred pursuant to the provisions of the Certificate so as to no longer constitute part of the Undertaking; (D) the Pledged User Taxes; and (E) any other moneys or funds deposited by the State or the

Department into the Highway Revenue Special Account; provided, however, that the term "Revenues" shall not include: (i) moneys received as proceeds from the sale of Bonds; (ii) condemnation proceeds or insurance proceeds except insurance proceeds received from rental or business interruption insurance; (iii) grants-in-aid or similar payments received from the Federal Government or public agencies if (1) the application of such moneys are restricted to a specific purpose other than payment of principal of and interest on indebtedness of the State, or (2) such grants or payments constitute a reimbursement to the State for expenditures previously made from the State Highway Fund or the Highway Revenue Special Account; (iv) moneys or securities received by the State or the Department as gifts or grants, the use of which is restricted by the donor or grantor; (v) investment income derived from any moneys or securities which may be placed in escrow or trust to defease bonds of the State, including the Bonds, or which may be held in the Highway Bond Proceeds Account; (vi) any arbitrage earnings which are required to be paid to the United States Government pursuant to Section 148(f) of the Code; and (vii) the proceeds of any Support Facility.

"Senior Bond" or "Senior Bonds" means any bond, some of the bonds or all of the bonds issued under and at any time Outstanding pursuant to the Certificate, being the 1993 Bonds, the 1996 Bonds, the 1998 Bonds, the 2001 Bonds and the 2003 Bonds issued pursuant to the Certificate, any Additional Senior Bonds issued pursuant to the Certificate, and any Refunding Senior Bonds issued pursuant to the Certificate.

"Sinking Fund Installment" means, with respect to each Series of Bonds, the amount designated as such in the Supplemental Certificate authorizing such Series of Bonds. The portion of any such Sinking Fund Installment remaining after the deduction of any such amounts credited toward the same (as the original amount of any such Sinking Fund Installment if no such amounts shall have been credited toward the same) shall constitute the unsatisfied balance of such Sinking Fund Installment for the purpose of calculation of Sinking Fund Installments due on a future date.

"Subordinate Bond" or "Subordinate Bonds" means any bond, some of the bonds or all of the bonds issued under and at any time Outstanding pursuant to the Certificate, being any Additional Subordinate Bonds and any Refunding Subordinate Bonds issued pursuant to the Certificate.

"Supplemental Certificate" or "Certificate supplemental to the Certificate", means a certificate duly issued by the Director of Transportation for any of the purposes of Article IX of the Certificate or otherwise amendatory of or supplemental to the Certificate but only if and to the extent specifically authorized thereunder.

"Support Facility" means any instrument such as a letter of credit, a committed line of credit, an insurance policy, a surety bond or a standby bond purchase agreement, or any combination of the foregoing, issued by a bank or banks, other financial institution or institutions, or any combination of the foregoing, which provides for: (i) with respect to any series of Bonds, the payment of all or a portion of the purchase price or principal, premium, if any, or interest due or to become due on specified Bonds of such series, or providing for the purchase of such Bonds or a portion thereof by the issuer of such Support Facility; or (ii) with respect to the Highway Senior Debt Service Reserve Subaccount or the Highway Subordinate Debt Service Reserve Subaccount, the funding, in whole or in part, of the Reserve Requirement.

"Undertaking" means and includes all highways and roads, and other related facilities and properties (real, personal or mixed) now belonging to or controlled by the State and under the administration, jurisdiction, control and management of the Department, and all improvements, betterments or extensions thereto hereafter constructed or acquired, except bikeways, and without limiting the generality of the foregoing, the term "Undertaking" shall include each and every, all and singular, the properties and facilities constructed or acquired from the proceeds of Bonds issued under the Certificate or constructed or acquired from the proceeds of any other bonds, notes or other evidences of indebtedness payable, or the principal and interest of which is reimbursable, from the State Highway Fund or from a fund maintained therefrom, or constructed or acquired from moneys in the State Highway Fund or in any other fund maintained therefrom.

"Value of Investment Securities" and words of like import means the amortized value thereof, provided, however, that all United States Treasury Obligations - State and Local Government Series shall be valued at par and those obligations which are redeemable or otherwise subject to payment (including purchase) at the option of the owner thereof shall be valued at the price at which such obligations are then redeemable or otherwise subject to payment. The computations made under this definition shall include accrued interest on the Investment Securities paid as a part of the purchase price thereof and not collected. For the purposes of this definition, "amortized value", when used with respect to a security purchased at par, means the purchase price of such security and when used with respect to a security purchased at a premium above or discount below par means, as of any subsequent date of valuation, the value obtained by dividing the total premium or discount by the number of interest payment dates remaining to maturity on any such security after such purchase and by multiplying the amount so calculated by the number of interest payment dates having

passed since the date of purchase and (i) in the case of a security purchased at a premium, by deducting the product thus obtained from the purchase price, and (ii) in the case of a security purchased at a discount, by adding the product thus obtained to the purchase price.

“Variable Rate Bonds” means any Subordinate Bonds issued bearing interest at a rate per annum subject to adjustment from time to time pursuant to the terms thereof, based upon an index, or otherwise calculated in a manner which precludes the actual rate for the entire term of such debt from being ascertainable in advance. For the purposes of this definition, Subordinate Bonds shall not be considered to be Variable Rate Bonds upon the establishment of or conversion of the rate of interest thereon to a fixed interest rate.

Allocation and Application of Revenues [Certificate Section 5.01]

For so long as any Bonds are Outstanding, (1) the State Highway Fund and the Highway Revenue Special Account shall both be continued and (2) all Revenues that are deposited in the State Highway Fund shall be immediately credited to the Highway Revenue Special Account. The Revenues credited or to be credited to the Highway Revenue Special Account shall be applied, used and disposed of as follows, and in the following order of priority:

FIRST: For further credit to the following subaccounts in the following order of priority in the amounts required pursuant to the provisions of the Certificate:

- (a) Highway Senior Interest Subaccount;
- (b) Highway Senior Principal Subaccount;
- (c) Highway Senior Debt Service Reserve Subaccount;

SECOND: For further credit to the following subaccounts in the following order of priority in the amounts required pursuant to the provisions of the Certificate:

- (d) Highway Subordinate Interest Subaccount;
- (e) Highway Subordinate Principal Subaccount; and
- (f) Highway Subordinate Debt Service Reserve Subaccount;

THIRD: For payment of Operation and Maintenance Expenses;

FOURTH: For payment of the costs of acquisition (including real property and interests therein), construction, addition, expansion, improvement, renewal, replacement, reconstruction, engineering, investigation, and planning for the Undertaking and bikeways, all or any of which in the judgment of the Department are necessary to the performance of its duties or functions;

FIFTH: To reimburse the general fund of the State for Reimbursable General Obligation Bonds;

SIXTH: All or any portion of available moneys credited to the Highway Revenue Special Account, after satisfying the requirements of priority items FIRST through FIFTH above, determined in conformance with Section 248-9, Hawaii Revised Statutes, as amended, or any successor statute thereto, by the Director of Transportation to be in excess of 135% of the requirements for the ensuing 12 months for the Highway Revenue Special Account may be transferred from the Highway Revenue Special Account as permitted by and in accordance with Section 37-53, Hawaii Revised Statutes, as amended, or any successor statute thereto; and

SEVENTH: To provide funds for other special reserve funds and other special funds as may be created by law.

Highway Senior Interest Subaccount [Certificate Section 5.02]

The moneys credited to the Highway Senior Interest Subaccount shall be disbursed solely for the purpose of paying interest on the Senior Bonds as the same becomes due. In each month, commencing with the first Business Day of the month which follows the last month for which interest on a Series of Senior Bonds, if any, is provided for from the proceeds of a Series of Senior Bonds, with respect to each Series of Senior Bonds, commencing on such first Business Day and continuing on the first Business Day of each month thereafter so long as any of the Senior Bonds of such Series are Outstanding, the Department shall credit to the Highway Senior Interest Subaccount from amounts credited to the Highway Revenue Special Account an amount such that, if the same amount were so credited on the first Business Day of each succeeding month thereafter, the aggregate of such amounts credited on the first Business Day of the month preceding an Interest Payment Date will be equal to the installment of interest falling due on the Senior Bonds on such Interest Payment Date or the amount required to reimburse the Support Facility provider for a draw on the Support Facility made to provide funds for the payment thereof. In making the credits to the Highway Senior Interest Subaccount required by this paragraph,

consideration shall be given to and allowance made for accrued interest received upon the sale of a Series of Senior Bonds, and for interest capitalized from the proceeds of a Series of Senior Bonds (which accrued or capitalized interest shall in each case be deposited in the Highway Revenue Special Account for credit to the Highway Senior Interest Subaccount), and for any other credits otherwise made to said account.

Highway Senior Principal Subaccount [Certificate Section 5.03]

In the event of the issuance of any Senior Bonds under the Certificate in the form customarily known as "serial bonds," in order to provide for the payment of principal of such Senior Bonds, or to reimburse the Support Facility provider for a draw on the Support Facility made to provide funds for the payment of such Senior Bonds maturing serially, commencing with the month which is 12 months prior to the first principal payment date of any of such Senior Bonds maturing serially and in each month thereafter so long as any of such Senior Bonds so maturing are Outstanding, there shall be credited to the Highway Senior Principal Subaccount an amount such that, if the same amount were so credited to this account on the first Business Day of such first month and each succeeding month thereafter prior to the next date upon which the principal of any of said Senior Bonds maturing serially becomes due and payable, the aggregate of the amounts on credit will on the first Business Day of the month preceding each such next principal payment date be equal to the principal amount of said Senior Bonds becoming due on such principal payment date.

In the event of the issuance of any Senior Bonds under the Certificate in the form customarily known as "term bonds", for the purpose of retiring such Senior Bonds, or to reimburse the Support Facility provider for a draw on the Support Facility made to provide funds for the payment of such term Senior Bonds, commencing with the month which is 12 months immediately prior to the date upon which the first Sinking Fund Installment to provide for the retirement of such term Senior Bonds is due, and in each month thereafter so long as any of such Senior Bonds are Outstanding, there shall be credited to the Highway Senior Principal Subaccount from amounts credited to the Highway Revenue Special Account an amount such that, if the same amount were so credited on the first Business Day of such first month and each succeeding month thereafter prior to the next date upon which a Sinking Fund Installment falls due, the aggregate of the amounts so credited will on the first Business Day of the month preceding each such next date upon which a Sinking Fund Installment falls due be sufficient to redeem the term Senior Bonds of each Series in the principal amounts and at the times specified in the Supplemental Certificate authorizing the issuance thereof.

The amounts of moneys credited to the Highway Senior Principal Subaccount for the purpose of providing for the retirement of Senior Bonds issued in the form of term bonds shall be applied by the Director of Finance, without further authorization or direction, to the redemption of the Senior Bonds of a Series on each date on which a Sinking Fund Installment for said Series of Senior Bonds is due in the respective principal amounts required to be credited on such dates, or, if so directed by the Department, commencing with respect to each Series of Senior Bonds with the second Sinking Fund Installment for each such Series, semi-annually on both such due date and the day six months prior to such due date so that the aggregate amount so applied in each calendar year will equal the respective principal amount required to be credited on such Sinking Fund Installment date. The Director of Finance shall give notice of a such redemptions, in the name and on behalf of the State, in accordance with the provisions of Article III of the Certificate. The Director of Finance may also, without further authorization or direction, apply the moneys credited to the Highway Senior Principal Subaccount for the retirement of term Senior Bonds of a Series to the purchase of said Senior Bonds; provided, however, that no Senior Bonds shall be purchased during the interval between the date on which notice of redemption of said Senior Bonds from Sinking Fund Installments for such Series is given and the date of redemption set forth in such notice, unless the Senior Bonds so purchased are Senior Bonds called for redemption in such notice or are purchased from moneys other than those credited to the Highway Senior Principal Subaccount for such Series, and provided further, that no purchases of Senior Bonds shall be made if such purchase would require the sale at a loss of securities credited to the Highway Senior Principal Subaccount unless the difference between the actual purchase price (including accrued interest and any brokerage or other charge) paid for such Senior Bonds and the then maximum purchase price (plus accrued interest) permitted to be paid therefor, is greater than the loss upon the sale of any such securities. Any purchase of Senior Bonds as described in this paragraph may be made with or without tenders of Senior Bonds and at either public or private sale, but in any event at a purchase price (including accrued interest and any brokerage or other charge) not to exceed the then applicable Redemption Price, plus accrued interest. All Senior Bonds purchased or redeemed as described in this paragraph shall be canceled and not reissued.

If the principal amount of Senior Bonds purchased and retired through application of any Sinking Fund Installment shall exceed the amount of such Sinking Fund Installment, or in the event of the purchase or redemption of Senior Bonds of any Series and maturity for which Sinking Fund Installments have been established from moneys other than Sinking Fund Installments, such excess or the principal amount of Senior Bonds so purchased or redeemed, as the case may be, shall be credited toward future Sinking Fund Installments either (i) in order of their due dates or (ii) in such order as the Department establishes in a certificate of the Director of Transportation and delivered to the Registrar on or prior to the forty-fifth day preceding the next Sinking Fund Installment due date established for such Senior Bonds.

Highway Senior Debt Service Reserve Subaccount [Certificate Section 5.05]

The Highway Senior Debt Service Reserve Subaccount shall be maintained in an amount equal to the Reserve Requirement and shall be disbursed solely for the purpose of paying principal of and interest on Senior Bonds for the payment of which there shall be insufficient money in the Highway Senior Interest Subaccount or Highway Senior Principal Subaccount. The Reserve Requirement shall be determined at the time of issuance of a Series of Senior Bonds, the deposit therein of any Support Facility, July 1 of each year, and such other time or times as the Department shall determine and shall be funded upon the issuance of each Series of Senior Bonds.

Subject to the remaining provisions described under this caption, (a) if at any time during a Fiscal Year the moneys on credit to the Highway Senior Debt Service Reserve Subaccount are less than the Reserve Requirement (including any deficiency in a Support Facility used to fund all or a portion of the Reserve Requirement), the amount of the deficiency shall be restored from the first available Pledged Funds (after making the deposits and credits required by the Certificate); (b) if at the end of any fiscal year, the moneys (taking into account the amount then available to be drawn under any Reserve Fund Facility) credited to the Highway Senior Debt Service Reserve Subaccount are less than the Reserve Requirement, the Department shall (after making the deposits and credits required by the Certificate) credit an amount to the Highway Senior Debt Service Reserve Subaccount from Pledged Funds credited to the Highway Revenue Special Account so that there shall then be credited to the Highway Senior Debt Service Reserve Subaccount an amount equal to the Reserve Requirement; (c) if the deficiency in the Highway Senior Debt Service Reserve Subaccount is due to the application of moneys credited thereto (or payments under any Reserve Fund Facility) to pay principal of or interest on any Senior Bonds, then in each month, commencing with the month which follows the month in which such application is made from the Highway Senior Debt Service Reserve Subaccount, the Department shall (after making the deposits and credits as required by the Certificate) credit from the Pledged Funds credited to the Highway Revenue Special Account to the Highway Senior Debt Service Reserve Subaccount the greater of (1) 1/12 of the aggregate Reserve Fund Facility Costs (as hereinafter defined) relating to each draw under any Reserve Fund Facility (which amounts will be used by Department to pay amounts due under a Support Facility) or (2) an amount which, if the same amount were so credited in each month thereafter until such day as the Department shall determine, which day shall not be more than 60 months from the making of the first of such credits, there shall be credited to such Subaccount on such day an amount not less than the Reserve Requirement; (d) if at any time and for so long as the moneys credited to the Highway Senior Debt Service Reserve Subaccount are at least equal to the Reserve Requirement and all Reserve Fund Facility Costs have been paid, then no further credits shall be made to the Subaccount, and any amounts in excess of the Reserve Requirement may be retained in the Highway Revenue Special Account for use and application as are all other moneys on deposit therein; and (e) any Reserve Fund Facility Costs shall be paid by the Department from amounts deposited into the Highway Senior Debt Service Reserve Subaccount. For purposes of the foregoing, "Reserve Fund Facility Costs" shall mean any fees and expenses for, and amounts necessary to reimburse any claims or draws under a Reserve Fund Policy.

When Senior Bonds are refunded in whole or in part or are otherwise paid so that all or a portion of the Senior Bonds are no longer Outstanding and all amounts due to any issuer of a Support Facility are paid, then moneys credited to the Highway Senior Debt Service Reserve Subaccount in excess of the Reserve Requirement may be withdrawn from the Highway Revenue Special Account to pay or provide for the payment of such Senior Bonds or refunded Senior Bonds, as the case may be, or may be transferred and applied by the Department to make up any deficiency in any other subaccounts under the Certificate or to any other account in the State Highway Fund; provided that immediately after such withdrawal or transfer there shall be on credit to the Highway Senior Debt Service Reserve Subaccount an amount equal to the Reserve Requirement.

In lieu of the credit of moneys to the Highway Senior Debt Service Reserve Subaccount, the Department may cause to be so credited one or more Support Facilities in an amount equal to the difference between the Reserve Requirement and the aggregate of (1) amounts then credited to the Highway Senior Debt Service Reserve Subaccount and (2) the amounts then available to be drawn under any Reserve Fund Facility then credited to such Subaccount. In the event a Support Facility is obtained to satisfy a portion of the Reserve Requirement so long as such Support Facility is in effect any moneys in the Reserve Subaccount shall be used to make up any deficiency in the Highway Senior Principal and Interest Subaccounts prior to any draw on any Support Facility. The Support Facility shall be payable (upon the giving of notice as required thereunder) on any date on which moneys will be required to be applied from the Highway Senior Debt Service Reserve Subaccount to the payment of the principal of or interest on any Senior Bonds. Prior to the use of a Support Facility pursuant to the provisions of this paragraph, the Department shall receive written confirmation from the Rating Agency that the rating on the Senior Bonds Outstanding as then in effect shall not be reduced as a result of such use. If a disbursement is made pursuant to a Support Facility provided pursuant to this paragraph, the Department shall be obligated either (i) to reinstate the maximum limits of such Support Facility or (ii) to credit to the Highway Senior Debt Service Reserve Subaccount, funds in the amount of the disbursement made under such Support Facility, or a combination of such alternatives, as shall provide that the amount credited to the Highway Senior Debt Service Reserve Subaccount equals the Reserve Requirement for all Senior Bonds; provided, however, a failure to immediately restore such Reserve Requirement shall not constitute an Event of Default if the Reserve

Requirement is restored within the time period described in the second preceding paragraph. Notwithstanding the provisions of said second preceding paragraph, the Department shall not permit any Support Facility which has been established in lieu of a deposit into the Highway Revenue Special Account for credit to the Highway Senior Debt Service Reserve Subaccount to terminate or expire prior to depositing to such Subaccount for credit to such Subaccount the amount satisfied previously by such Support Facility.

Highway Subordinate Interest Subaccount [Certificate Section 5.06]

Moneys on credit to the Highway Subordinate Interest Subaccount shall be disbursed solely for the purpose of paying interest on the Subordinate Bonds as the same becomes due. In each month, commencing with the first Business Day of the month which follows the last month for which interest on a Series of Subordinate Bonds, if any, is provided for from the proceeds of a Series of Subordinate Bonds, (a) with respect to each Series of Subordinate Bonds (other than Variable Rate Subordinate Bonds which have Interest Payment Dates occurring at intervals of one month or less), commencing on such first Business Day and continuing on the first Business Day of each month thereafter so long as any of the Subordinate Bonds of such Series are Outstanding, the Department shall credit to the Highway Subordinate Interest Subaccount from amounts credited to the Highway Revenue Special Account an amount such that, if the same amount were so credited on the first Business Day of each succeeding month thereafter, the aggregate of such amounts credited on the first Business Day of the month preceding an Interest Payment Date will be equal to the installment of interest falling due on the Subordinate Bonds on such Interest Payment Date or the amount required to reimburse the Support Facility provider for a draw on the Support Facility made to provide funds for the payment thereof, and (b) with respect to Variable Rate Subordinate Bonds which have Interest Payment Dates occurring at intervals of one month or less, on the first Business Day of the month prior to each Interest Payment Date the Department shall credit to the Highway Subordinate Interest Subaccount from amounts credited to the Highway Revenue Special Account the amount required together with other funds available therefor credited to such account, to pay, or to reimburse the Support Facility provider for a draw on the Support Facility made to provide funds for the payment of, the interest payable on such Interest Payment Date or Dates on the Outstanding Variable Rate Subordinate Bonds. In making the credits to the Highway Subordinate Interest Subaccount required by this paragraph, consideration shall be given to and allowance made for accrued interest received upon the sale of a Series of Subordinate Bonds, and for interest capitalized from the proceeds of a Series of Subordinate Bonds (which accrued or capitalized interest shall in each case be deposited in the Highway Revenue Special Account for credit to the Highway Subordinate Interest Subaccount), and for any other credits otherwise made to said account. Variable Rate Subordinate Bonds shall be assumed to bear interest at the assumed interest rate as determined pursuant to the Certificate, and monthly credits made with respect to Variable Rate Subordinate Bonds shall be adjusted to the extent possible to reflect the actual interest rate on Variable Rate Subordinate Bonds in the preceding month so that, as of any Interest Payment Date, the amount available is sufficient to pay the interest then due; provided, however, that any payments to a Support Facility provider as Holder of a Subordinate Bond which are in excess of the stated rate of interest on such Subordinate Bond, whether denominated additional interest, penalty rate, or otherwise, shall not constitute interest for purposes of this paragraph.

Highway Subordinate Principal Subaccount [Certificate Section 5.07]

In the event of the issuance of any Series of Subordinate Bonds under the Certificate in the form customarily known as "serial bonds", in order to provide for the payment of principal of such Subordinate Bonds of such Series, or to reimburse the Support Facility provider for a draw on the Support Facility made to provide funds for the payment of such Subordinate Bonds maturing serially, commencing with the month which is 12 months prior to the first principal payment date of any of such Subordinate Bonds maturing serially and in each month thereafter so long as any of such Subordinate Bonds so maturing are Outstanding, there shall be credited to the Highway Subordinate Principal Subaccount an amount such that, if the same amount were so credited to this account on the first Business Day of such first month and each succeeding month thereafter prior to the next date upon which the principal of any of said Subordinate Bonds maturing serially becomes due and payable, the aggregate of the amounts on credit will on the first Business Day of the month preceding each such next principal payment date be equal to the principal amount of said Subordinate Bonds becoming due on such principal payment date.

In the event of the issuance of any Subordinate Bonds under the Certificate in the form customarily known as "term bonds", for the purpose of retiring such Subordinate Bonds, or to reimburse the Support Facility provider for a draw on the Support Facility made to provide funds for the payment of such term Subordinate Bonds, commencing with the month which is 12 months immediately prior to the date upon which the first Sinking Fund Installment to provide for the retirement of such term Subordinate Bonds is due, and in each month thereafter so long as any of such Subordinate Bonds are Outstanding, there shall be credited to the Highway Subordinate Principal Subaccount from amounts credited to the Highway Revenue Special Account an amount such that, if the same amount were so credited on the first Business Day of such first month and each succeeding month thereafter prior to the next date upon which a Sinking Fund Installment falls due, the aggregate of the amounts so credited will on the first Business Day of the month preceding each such next date upon which a Sinking Fund Installment falls due be sufficient to redeem the term Subordinate Bonds of each Series in the principal amounts and at the times specified in the Supplemental Certificate authorizing the issuance thereof.

The amounts of moneys credited to the Highway Subordinate Principal Subaccount for the purpose of providing for the retirement of Subordinate Bonds issued in the form of term bonds shall be applied by the Director of Finance, without further authorization or direction, to the redemption of the Subordinate Bonds of a Series on each date on which a Sinking Fund Installment for said Series of Subordinate Bonds is due in the respective principal amounts required to be credited on such dates, or, if so directed by the Department, commencing with respect to each Series of Subordinate Bonds with the second Sinking Fund Installment for each such Series, semi-annually on both such due date and the day six months prior to such due date so that the aggregate amount so applied in each calendar year will equal the respective principal amount required to be credited on such Sinking Fund Installment dates. The Director of Finance shall give notice of a such redemptions, in the name and on behalf of the State, in accordance with the provisions of Article III of the Certificate. The Director of Finance may also, without further authorization or direction, apply the moneys credited to the Highway Subordinate Principal Subaccount for the retirement of term Subordinate Bonds of a Series to the purchase of said Subordinate Bonds; provided, however, that no Subordinate Bonds shall be purchased during the interval between the date on which notice of redemption of said Subordinate Bonds from Sinking Fund Installments for such Series is given and the date of redemption set forth in such notice, unless the Subordinate Bonds so purchased are Subordinate Bonds called for redemption in such notice or are purchased from moneys other than those credited to the Highway Subordinate Principal Subaccount for such Series, and provided further, that no purchases of Subordinate Bonds shall be made if such purchase would require the sale at a loss of securities credited to the Highway Subordinate Principal Subaccount unless the difference between the actual purchase price (including accrued interest and any brokerage or other charge) paid for such Subordinate Bonds and the then maximum purchase price (plus accrued interest) permitted to be paid therefor, is greater than the loss upon the sale of any such securities. Any purchase of Subordinate Bonds as described in this paragraph may be made with or without tenders of Subordinate Bonds and at either public or private sale, but in any event at a purchase price (including accrued interest and any brokerage or other charge) not to exceed the then applicable Redemption Price, plus accrued interest. A Subordinate Bonds purchased or redeemed as described in this paragraph shall be canceled and not reissued.

If the principal amount of Subordinate Bonds purchased and retired through application of any Sinking Fund Installment shall exceed the amount of such Sinking Fund Installment, or in the event of the purchase or redemption of Subordinate Bonds of any Series and maturity for which Sinking Fund Installments have been established from moneys other than Sinking Fund Installments, such excess or the principal amount of Subordinate Bonds so purchased or redeemed, as the case may be, shall be credited toward future Sinking Fund Installments either (i) in order of their due dates or (ii) in such order as the Department establishes in a certificate of the Director of Transportation and delivered to the Registrar on or prior to the forty-fifth day preceding the next Sinking Fund Installment due date established for such Subordinate Bonds.

Highway Subordinate Debt Service Reserve Account [Certificate Section 5.09]

The Highway Subordinate Debt Service Reserve Account shall be maintained in an amount equal to the Reserve Requirement and shall be disbursed solely for the purpose of paying principal of and interest on Subordinate Bonds for the payment of which there shall be insufficient money in the Highway Subordinate Interest Subaccount or Highway Subordinate Principal Subaccount. The Reserve Requirement shall be determined at the time of issuance of a Series of Subordinate Bonds, July 1 of each year, at the time any Variable Rate Subordinate Bonds of a Series cease to be Variable Rate Subordinate Bonds, and such other time or times as the Department shall determine and shall be funded upon the issuance of each Series of Subordinate Bonds.

Subject to the remaining provisions described under this caption, (a) if at any time during a Fiscal Year the moneys on credit to the Highway Subordinate Debt Service Reserve Subaccount are less than the Reserve Requirement (including any deficiency in a Support Facility used to fund all or a portion of the Reserve Requirement), the amount of the deficiency shall be restored from the first available Pledged Funds; (b) if at the end of any Fiscal Year, the moneys credited to the Highway Subordinate Debt Service Reserve Subaccount are less than the Reserve Requirement, the Department shall (after making the deposits and credits to other subaccounts and purposes as required by the Certificate) credit an amount to the Highway Subordinate Debt Service Reserve Subaccount from Pledged Funds credited to the Highway Revenue Special Account so that there shall then be credited to the Highway Subordinate Debt Service Reserve Subaccount an amount equal to the Reserve Requirement; (c) if the deficiency in the Highway Subordinate Debt Service Reserve Subaccount is due to the application of moneys credited thereto to pay principal of or interest on a Series of Subordinate Bonds, then in each month, commencing with the month which follows the month in which such application is made from the Highway Subordinate Debt Service Reserve Subaccount, the Department shall (after making the deposits and credits to other subaccounts and purposes as required by the Certificate) credit from the Pledged Funds credited to the Highway Revenue Special Account to the Highway Subordinate Debt Service Reserve Subaccount an amount which, if the same amount were so credited in each month thereafter until such day as the Department shall determine, which day shall not be more than 60 months from the making of the first of such credits, there shall be credited to such account on such day an amount not less than the Reserve Requirement; and (d) if at any time and for so long as the moneys credited to the Highway Subordinate Debt Service Reserve Subaccount are at least equal

to the Reserve Requirement, no further credits shall be made to the account, and any amounts in excess of the Reserve Requirement may be retained in the Highway Revenue Special Account for use and application as are all other moneys on deposit therein.

When a Series of Subordinate Bonds is refunded in whole or in part or is otherwise paid so that all of the Subordinate Bonds of such Series are no longer Outstanding, moneys credited to the Highway Subordinate Debt Service Reserve Subaccount may be withdrawn from the Highway Revenue Special Account to pay or provide for the payment of such Subordinate Bonds or refunded Subordinate Bonds, as the case may be, or may be transferred and applied to any reserve fund or account established for the Refunding Subordinate Bonds issued to refund such refunded Subordinate Bonds; provided that immediately after such withdrawal or transfer there shall be on credit to the Highway Subordinate Debt Service Reserve Subaccount an amount equal to the Reserve Requirement.

In lieu of the credit of moneys to the Highway Subordinate Debt Service Reserve Subaccount, the Department may cause to be so credited a Support Facility in an amount equal to the difference between the Reserve Requirement and the amounts then credited to the Highway Subordinate Debt Service Reserve Subaccount. In the event a Support Facility is obtained to satisfy a portion of the Reserve Requirement allocable to a Series of Subordinate Bonds, so long as such Support Facility is in effect, the Owners of such Series of Subordinate Bonds shall not be entitled to payment from or a lien on the funds credited to the Highway Revenue Special Account credited to the Highway Subordinate Debt Service Account to satisfy that portion of the Reserve Requirement allocable to other Series of Subordinate Bonds, nor shall the Owners of Subordinate Bonds of such other Series be entitled to any payment from such Support Facility. The Support Facility shall be payable (upon the giving of notice as required thereunder) on any date on which moneys will be required to be applied from the Highway Subordinate Debt Service Reserve Subaccount to the payment of the principal of or interest on any Subordinate Bonds of such Series and such withdrawals may not be made from amounts credited to the Highway Subordinate Debt Service Reserve Subaccount for such Series of Subordinate Bonds. Prior to the use of a Support Facility pursuant to the provisions of this paragraph, the Department shall receive written confirmation from the Rating Agency that the rating on the Subordinate Bonds Outstanding as then in effect shall not be reduced as a result of such use. If a disbursement is made pursuant to a Support Facility provided pursuant to this paragraph, the Department shall be obligated either (i) to reinstate the maximum limits of such Support Facility or (ii) to credit to the Highway Subordinate Debt Service Reserve Subaccount, funds in the amount of the disbursement made under such Support Facility, or a combination of such alternatives, as shall provide that the amount credited to the Highway Subordinate Debt Service Reserve Subaccount allocable to a Series of Subordinate Bonds equals that portion of the Reserve Requirement allocable to such Series; provided, however, a failure to immediately restore such Reserve Requirement shall not constitute an Event of Default if the Reserve Requirement is restored within the time period described in clause (b) under "Events of Default; Remedies--Events of Default" below. Notwithstanding the provisions of said clause (b), the Department shall not permit any Support Facility which has been established in lieu of a deposit into the Highway Revenue Special Account for credit to the Highway Subordinate Debt Service Reserve Subaccount to terminate or expire prior to depositing to such fund for credit to such account the amount satisfied previously by the Support Facility.

Investment of Moneys [Certificate Section 5.10]

Moneys in the Highway Revenue Special Account credited to the Highway Senior Interest Subaccount, the Highway Senior Principal Subaccount, the Highway Subordinate Interest Subaccount, and the Highway Senior Subordinate Principal Subaccount therein shall be invested by the Director of Finance in Investment Securities which have ratings provided by Moody's and S&P that are not less than the ratings given to the Senior Bonds then Outstanding and which mature in such amounts and at such times so that the principal of and interest and premium, if any, on the Bonds can be paid when due, whether at maturity or upon the redemption thereof. Moneys in the Highway Revenue Special Account credited to the Highway Senior Debt Service Reserve Subaccount and the Highway Subordinate Debt Service Reserve Subaccount therein shall be invested by the Director of Finance in Federal Securities which have ratings provided by Moody's and S&P that are not less than the ratings given to the Senior Bonds then Outstanding and which have maturities or are redeemable at the option of the Holder thereof in not more than 5 years from the date of investment, but in any event by no later than the last or final maturity date of the Senior Bonds or Subordinate Bonds then Outstanding, as the case may be. The Department in the Certificate grants its approval for all investments made by the Director of Finance pursuant to the Certificate, and no further approvals of the Department shall be necessary therefor.

Income derived from investments made pursuant to the foregoing provisions of the Certificate shall be treated as Revenues; expenses of purchase, safekeeping, sale and redemption, and all other expenses attributable to such investments shall be proper expenses of the Undertaking. Securities so purchased shall be considered as being deposited in the custody or control of the Director of Finance by the Department.

All moneys in the Highway Revenue Special Account and the Highway Bond Proceeds Account, the investment of which is not otherwise provided for in the Certificate, may be invested, and the income from such investments disbursed or applied, as may be provided by applicable law.

All securities shall constitute a part of the respective fund or account from which the investment therein was made. For the purposes of making any calculations or computations at any time and from time to time of the amounts in the State Highway Fund, or any fund or account therein, which may be required for the purposes of the Certificate, the Value of Investment Securities shall be determined at the time of any withdrawal therefrom and as of July 1 of each year.

The Department will maintain records to enable it to cause to be made the computations necessary to determine whether a Series of Bonds the interest on which is intended to be excludable from gross income for federal income tax purposes meets the requirements of Section 148 of the Code, including, but not limited to, records showing the dates and amounts of all investments of funds credited to a subaccounts in the Highway Revenue Special Account and the Highway Bond Proceeds Account.

Revenues Held in Trust, Lien of Bondholders [Certificate Section 5.11]

The moneys in the State Highway Fund shall be, until used, applied and disbursed in accordance with the provisions of the Certificate, held in trust: (i) for the equal benefit and security of the Holders from time to time of the Senior Bonds; and (ii) subject to the prior and senior rights, benefits and security of the Holders from time to time of the Senior Bonds, for the equal benefit and security of the Holders from time to time of the Subordinate Bonds. Subject to the provisions of the Certificate relating to application of moneys, all Senior Bonds shall have a prior and paramount lien on the Revenues paid into the Highway Revenue Special Account for credit to the Highway Senior Interest Subaccount, the Highway Senior Principal Subaccount and the Highway Senior Debt Service Reserve Subaccount therein and the investments in which such Revenues may from time to time be invested, over and ahead of all Subordinate Bonds and all bonds, notes or other evidences of indebtedness which may subsequently be issued, and over and ahead of any claims, encumbrances or obligations subsequently arising or subsequently incurred, and all the Senior Bonds shall be equally and ratably secured, without priority by reason of series, number, date of execution or of any Supplemental Certificate providing for the issuance thereof, date of Senior Bonds, date of issuance, date of sale, date of execution, date of authentication, or date of delivery, by such lien in accordance with the provisions of the Certificate. Subject to the prior and paramount lien provided in the preceding sentence in respect of the Senior Bonds and further subject to the provisions of the Certificate relating to application of moneys, all Subordinate Bonds shall have a lien on the Revenues paid into the Highway Revenue Special Account for credit to the Highway Subordinate Interest Subaccount, the Highway Subordinate Principal Subaccount and the Highway Subordinate Debt Service Reserve Subaccount therein and the investments in which such Revenues may from time to time be invested, over and ahead of all bonds, notes or other evidences of indebtedness which may subsequently be issued, and over and ahead of any claims, encumbrances or obligations subsequently arising or subsequently incurred, and all the Subordinate Bonds shall be equally and ratably secured, without priority by reason of series, number, date of execution or of any Supplemental Certificate providing for the issuance thereof, date of Subordinate Bonds, date of issuance, date of sale, date of execution, date of authentication, or date of delivery, by such lien in accordance with the provisions of the Certificate. Subject to the provisions of the Certificate relating to application of moneys, no claim, encumbrance or obligation against the Pledged Funds subsequently arising or incurred shall be secured by or entitled to a lien or charge thereon prior to or equal with the payments required by the Certificate to be made from the Pledged Funds to provide for the payment of the Bonds.

Conditions Precedent to Issuance of Additional Bonds and Refunding Bonds [Certificate Section 4.02]

The Department at any time and from time to time may authorize the issuance of one or more Series of: (i) additional Senior Bonds ("Additional Senior Bonds") or refunding Senior Bonds ("Refunding Senior Bonds") payable from the Highway Revenue Special Account on a parity with all other Senior Bonds then Outstanding and equally and ratably secured therewith, or (ii) additional Subordinate Bonds ("Additional Subordinate Bonds") or refunding Subordinate Bonds ("Refunding Subordinate Bonds") payable from the Highway Revenue Special Account on a parity with any Additional Subordinate Bonds or Refunding Subordinate Bonds then Outstanding and equally and ratably secured therewith, in each case upon compliance with the following conditions:

1. The issuance of the Additional Bonds or Refunding Bonds shall have been authorized by law and are issued under and pursuant to a Supplemental Certificate or Certificates.
2. The Supplemental Certificate providing for the issuance of such Bonds shall provide that any accrued interest received upon the sale of said Bonds or any interest capitalized from the proceeds of said Bonds shall be paid into the Highway Revenue Special Account for credit to the Highway Senior Interest Subaccount or the Highway Subordinate Interest Subaccount;
3. At the time of the issuance of such Bonds, no default exists in the payment of the principal of and premium, if any, and interest on any Bond; no deficiencies exist in the State Highway Fund or the Highway Revenue Special Account;

and there does not exist an "Event of Default" or a condition which upon the passage of time would constitute such an "Event of Default";

4. Upon the delivery of such Bonds, there shall be credited to the Highway Revenue Special Account for credit to the Highway Senior Debt Service Reserve Subaccount and the Highway Subordinate Debt Service Reserve Subaccount an amount equal to, in each case, the Reserve Requirement; provided however, that the Supplemental Certificate providing for the issuance of such Series of Bonds may provide that part of the proceeds thereof shall be paid or a Support Facility may be deposited, into the Highway Revenue Special Account for credit to the Highway Senior Debt Service Reserve Subaccount or the Highway Subordinate Debt Service Reserve Subaccount, as the case may be.

5. In the case of the issuance of Additional Bonds, upon compliance with the additional conditions summarized below.

6. In the case of the issuance of Refunding Bonds, upon compliance with the additional conditions summarized below.

Additional Conditions for the Issuance of Additional Bonds [Certificate Section 4.03]

Each of the following conditions, in addition to those set forth above, shall be met upon the issuance of Additional Bonds:

(a) Such Bonds shall be issued only for the purpose of the payment or reimbursement of the cost of the acquisition or construction of properties to constitute part of the Undertaking or the making of additions to, expansions of, improvements of, renewals of, replacements of, or reconstructions of, the Undertaking or of properties which shall constitute part of the Undertaking; and

(b) The Revenues for any 12 consecutive calendar month's period out of the last eighteen (18) consecutive calendar month's period immediately preceding the date of issuance of the Series of Bonds, as derived from the most recent publicly available financial statements of the Department, shall be at least equal to: (i) in the case of Senior Bonds proposed to be issued, two (2) times maximum Aggregate Bond Service for any future Fiscal Year on a Senior Bonds to be Outstanding after the issuance of such Additional Senior Bonds; and (ii) in the case of Subordinate Bonds proposed to be issued, one and thirty-hundredths (1.30) times maximum Aggregate Bond Service for any future Fiscal Year on all Bonds to be Outstanding after the issuance of such Additional Subordinate Bonds.

Additional Conditions for the Issuance of Refunding Bonds [Certificate Section 4.04]

The following conditions, in addition to those set forth above under "Conditions Precedent to Issuance of Additional Bonds and Refunding Bonds," shall be met upon the issuance of Refunding Bonds:

(a) Such Refunding Bonds are being issued for the purpose of refunding at their maturity or at any time within one year prior to their maturity, any of the then Outstanding Bonds, for the payment of which sufficient funds are not available, which Bonds to be refunded shall be specified in the Supplemental Certificate providing for the issuance of the Refunding Bonds; and

(b) Refunding Bonds may be issued to refund prior to maturity all or part of the Outstanding Bonds, including therein amounts to pay principal of, and redemption and acquisition premium and interest on the Bonds to be refunded, which Bonds to be refunded shall be specified in the Supplemental Certificate providing for the issuance of the Refunding Bonds.

Variable Rate Bonds [Certificate Section 4.02]

Nothing in the Certificate shall prohibit or prevent, or be deemed or construed to prohibit or prevent, the Department from issuing Variable Rate Bonds; provided, however, that no Variable Rate Bond may be issued as a Senior Bond. The Supplemental Certificate providing for the issuance of such Variable Rate Bonds may provide for, without limitation, the following: Support Facilities or alternative Support Facilities and support agreements in connection therewith; remarketing agreements and the appointment of remarketing agents; the appointment of tender agents to accept mandatory or optional tenders of Variable Rate Bonds; the payment, redetermination and accrual over specified periods of interest; the establishment, use, composition, adjustment and change of interest indices or modes or the establishment and use of alternative interest indices or modes or the establishment of a fixed interest rate or rates; the establishment of special funds and accounts in connection with the issuance of such Variable Rate Bonds;

special redemption or purchase provisions for such Variable Rate Bonds and notice provisions in connection with the purchase, redemption, delivery or tender of such Variable Rate Bonds; and any other terms and provisions not in conflict with the Certificate.

Annual Audit [Certificate Section 6.04]

The Department shall maintain and keep, or cause to be maintained and kept, proper books, records and accounts in which complete and correct entries shall be made of all dealings and transactions relating to the Undertaking. Such accounts shall show the amount of the Revenues and the application of such Revenues to the purposes specified in the Certificate and all financial transactions in connection therewith, including all deposits into and disbursements from the State Highway Fund, the Highway Revenue Special Account and the Highway Bond Proceeds Account.

The Department shall cause its accounts to be audited by an accountant (herein defined and referred to as the "Independent Public Accountant") employed by it, such period of appointment or employment to be from year to year. Such Independent Public Accountant shall be selected with special reference to his general knowledge, skill and experience in auditing books and accounts, and shall be a certified or licensed accountant or firm of certified or licensed accountants who, or each of whom, is in fact independent and not under the domination of the State (including the Department) and who, or each of whom, is not connected with the State (including the Department) as an officer or employee thereof, but who may be regularly retained to make annual or similar audits of any of the books of the State (including the Department). Such audit shall be made annually and shall be completed within 270 days after the close of each Fiscal Year, shall include a detailed statement of the Revenues and the expenditure and application thereof for such year and a detailed balance sheet of the Undertaking as of the close of such year, including therein a statement of the State Highway Fund and the Highway Revenue Special Account and accounts therein, and be accompanied in writing by a certificate of the Independent Public Accountant. Each such audit shall certify as to the correctness of the schedules contained in the audit report. A copy of each such annual audit shall be filed with the Director of Finance and shall be open for public inspection, and shall be mailed to any Holder of the Bonds filing with the Department a request for same. The cost of any such audit shall be an Operation and Maintenance Expense.

Annual Budget [Certificate Section 6.05]

The Department shall prepare and file with the proper officers of the State at the time and in the manner prescribed by law, an estimated budget of Revenues and Operation and Maintenance Expenses, Bond Service, capital improvements and any other proposed expenditures for the Undertaking for each Fiscal Year, which budgets shall be open to inspection by any Holder of Bonds or other interested party.

Amending Certificate Without Consent of Bondholders [Certificate Section 9.01]

The State, acting by and through the Department or as may otherwise then be provided by law, from time to time and at any time and without the consent or concurrence of the Holder of any Bond, may make and execute a Supplemental Certificate (i) for the purpose of providing for the issuance of Additional Bonds or the issuance of Refunding Bonds, (ii) to make any changes or modifications thereof, or amendments, additions or deletions thereto which may be required to permit the Certificate to be qualified under the Trust Indenture Act of 1939 of the United States of America, and (iii) if the provisions of such Supplemental Certificate shall not materially adversely affect the rights of the Holders of the Bonds then Outstanding, for any one or more of the following purposes:

1. To make any changes or corrections in the Certificate or any supplement thereto as to which it shall have been advised by its counsel that the same are minor clerical or typographical corrections or changes or are required for the purpose of curing or correcting any ambiguity or defective or inconsistent provision or omission or mistake or manifest error contained therein or in any such supplement thereto, or to insert in the Certificate such provisions clarifying matters or questions arising under the Certificate as are necessary or desirable;
2. To add additional covenants and agreements of the State for the purpose of further securing the payment of the Bonds, provided that such additional covenants and agreements are not contrary to or inconsistent with the covenants and agreements contained in the Certificate as originally issued or as amended with the consent of Bondholders;
3. To surrender any right, power or privilege reserved to or conferred upon the State by the terms of the Certificate or any supplement hereto;

4. To confirm as further assurance any lien, pledge or charge, or the subjection of any additional revenue, property or collateral to any lien, pledge or charge, created or to be created by the provisions of the Certificate or any supplement thereto;

5. To grant to or confer upon the Holders of the Bonds or any Support Facility provider, any additional rights, remedies, powers, authority or security that lawfully may be granted to or conferred upon them;

6. To prescribe further limitations and restrictions upon the issuance of Bonds and the incurring of indebtedness by the State payable from the Revenues;

7. To include any modifications, amendments or supplements as may be required with respect to any Series of Bonds in order to obtain a favorable rating or ratings from any Rating Agency;

8. To add or modify any provision of the Certificate as a result of enactment of any State or federal law which changes the treatment of the Bonds or interest thereon for tax purposes;

9. To include any modifications, amendments or supplements as may be required with respect to any Series of Bonds in order to permit such Series to be available through a book-entry system maintained by, or to be cleared through, The Depository Trust Company, New York, New York, or other securities depository, clearing corporation, or clearing agency;

10. To make any changes or corrections to the Certificate as are necessary to provide for the issuance of Bonds in a form not contemplated by the express provisions of the Certificate, including without limitation in the form of commercial paper, indebtedness which converts from a variable rate to a fixed rate, indebtedness which initially compounds or accrues interest and then converts to a current interest-bearing instrument, and a Series of Bonds whereby the State pays a particular rate of interest and such interest payment is divided in a manner such that certain Bondholders receive a variable interest rate determined by the market and other Bondholders receive a residual interest rate approximating the difference between the interest payment paid by the State and such variable rate of interest; or

11. To modify, amend or supplement in any other respect any of the provisions of the Certificate, provided that such modifications shall have no adverse affect as to any Bond or Bonds which are then Outstanding.

Except for Supplemental Certificates providing for the issuance of Additional Bonds or Refunding Bonds, the State shall not make and execute any instrument or Certificate supplemental to the Certificate, unless in the opinion of counsel the making and entering into of such instrument or such Supplemental Certificate is permitted by the provisions of the Certificate and the provisions of such instrument or of such Supplemental Certificate are not contrary to or inconsistent with the covenants or agreements of the State contained in the Certificate as originally issued or as amended with the consent of the Bondholders.

Amending Certificate With Consent of Bondholders [Certificate Section 9.02]

With the consent of the Holders of not less than a majority of the principal amount of the Bonds then Outstanding, the State, acting by and through the Department or as may otherwise then be provided by law, from time to time and at any time, may make and execute an instrument or certificate amending or supplementing the provisions of the Certificate for the purpose of adding any provisions to, or changing in any manner or eliminating any of the provisions of, the Certificate or of any supplement thereto, or modifying or amending the rights and obligations of the Department thereunder, or modifying in any manner the rights of the Holders of the Bonds; provided, however, that, without the specific consent of the Holder of each Bond which would be affected thereby, whether or not such Bond shall then be deemed to be Outstanding thereunder, no such instrument or certificate amending or supplementing the provisions thereof shall: (1) extend the fixed maturity date for the payment of the principal of any Bond, or reduce the principal amount of any Bond, or reduce the rate or extend the time of payment of interest thereon, or reduce any premium payable upon the redemption or prepayment thereof, or advance the date upon which any Bond may first be called for redemption prior to its fixed maturity date; (2) reduce the aforesaid percentage of Bonds, the Holders of which are required to consent to any such instrument or certificate amending or supplementing the provisions thereof; (3) give to any Bond or Bonds any preference over any other Bond or Bonds secured by the Certificate; (4) authorize the creation of any pledge of the Revenues or any lien or charge thereon prior or superior to or on a parity with the pledge of and lien and charge thereon created in the Certificate for the payment of the Bonds except to the extent provided in the Certificate; or (5) deprive any Holder of the Bonds of the pledge and lien created by the Certificate; and provided further, that if moneys or Federal Securities shall have been deposited in accordance with the provisions of the Certificate for the payment of particular Bonds and such Bonds shall not in fact have been paid, no amendments or supplements to the provisions of

Article XI of the Certificate shall be made without the specific consent of the Holder of each Bond which would be affected thereby. A modification or amendment of the provisions of Article V of the Certificate with respect to any of the accounts therein shall not be deemed a change in the terms of payment of the Bonds; provided, however, that no such modification or amendment shall, except upon the consent of the Holders of all Bonds then Outstanding affected thereby, reduce the amount or amounts required to be deposited in the Highway Revenue Special Account for credit to all accounts therein.

Events of Default; Remedies [Certificate Sections 10.01 to 10.05]

Events of Default. The following shall constitute "Events of Default":

(a) If payment of the interest on, or principal (including any Sinking Fund Installment) or premium (if any) of any Bond, whether at maturity or by proceedings for redemption, by declaration, or otherwise, shall not be made after the same shall become due and payable; or

(b) If the Department shall default in the due and punctual performance of any of the covenants, conditions, agreements and provisions contained in the Bonds or in the Certificate or in any Certificate supplemental thereto, on the part of the Department to be performed, and such default shall continue for 90 days after written notice specifying such default and requiring the same to be remedied shall have been given to the Department by the Holders of not less than 20% in principal amount of the Bonds then Outstanding, or any trustee or committee therefor; provided, however, that if such failure shall be such that it cannot be corrected within such 90-day period, it shall not constitute an Event of Default if correction action is instituted within such period and diligently pursued until the failure is corrected; or

(c) If any proceedings shall be instituted, with the consent or acquiescence of the State, for the purpose of effecting a composition between the State and its creditors and if the claim of such creditors is in any circumstance payable from any of the Revenues or any other moneys pledged and charged in the Certificate or in any Certificate supplemental thereto, or for the purpose of adjusting the claims of such creditors, pursuant to any federal or State statute now or hereafter enacted; or

(d) If, under the provision of any other law for the relief or aid of debtors, any court of competent jurisdiction shall assume custody or control of the Undertaking or any of the buildings and facilities thereof, and such custody or control shall not be terminated within 90 days from the date of assumption of such custody or control; or

(e) If the Department or the State shall for any reason be rendered incapable of fulfilling its obligations under the Certificate.

Declaration of Principal and Interest as Due. Upon the occurrence and continuation of an Event of Default, then and in each and every case the Holders of not less than 25% in principal amount of the Senior Bonds then Outstanding and the Holders of not less than 25% in principal amount of the Subordinate Bonds then Outstanding may, by written notice to the Department filed in the office of the Department and with the Director of Finance, proceed to declare the principal of all Bonds then Outstanding, together with all accrued and unpaid interest thereon and together with all other moneys secured thereby, if not already due, to be due and payable immediately, and upon any such declaration the same shall become and be due and payable immediately, anything in the Certificate, any Supplemental Certificate, or in any of the Bonds contained to the contrary notwithstanding, except to the extent otherwise provided in connection with a Support Facility. This provision is subject, however, to the condition that, if at any time after the principal of the Bonds, together with accrued and unpaid interest thereon shall have been so declared due and payable and before any further action has been taken (other than the making of the above declaration), the principal amount of all Bonds which have matured either according to the maturity date or dates specified therein or otherwise (except as a result of such declaration) and all arrears of interest upon all Bonds, except interest accrued but not yet due on said Bonds, shall be paid or caused to be paid, and all other Events of Default, if any, which shall have occurred shall have been remedied, cured or secured, then and in every such case the Holders of a majority in principal amount of the Senior Bonds then Outstanding and not less than 25% in principal amount of the Subordinate Bonds then Outstanding, by notice in writing delivered to the Department and the Director of Finance, may waive such default and its consequences and rescind such declaration. No such waiver or rescission or annulment shall extend to or affect any subsequent default or impair or exhaust any right or power consequent thereon.

Bondholders' Committee. Upon the occurrence of an Event of Default and at any time such Event of Default shall be continuing, the Holders of not less than 20% in principal amount of the Senior Bonds then Outstanding and not less than 20% in principal amount of the Subordinate Bonds then Outstanding may call a meeting of the Holders of Bonds for the purpose of electing a Bondholders' Committee. Such meeting shall be called and proceedings thereat shall be conducted as provided for other meetings of

Bondholders pursuant to the Certificate. At such meeting the Holders of not less than a majority of the principal amount of the Senior Bonds then Outstanding and not less than a majority of the principal amount of the Subordinate Bonds then Outstanding must be present in person or by proxy in order to constitute a quorum for the transaction of business, less than a quorum, however, having power to adjourn from time to time without any notice. A quorum being present at such meeting, the Bondholders present in person or by proxy may, by the votes cast by the Holders of a majority in principal amount of the Senior Bonds and by the Holders of a majority in principal amount of the Subordinate Bonds so present in person or by proxy, elect one or more persons who may or may not be Bondholders to the Bondholders' Committee which shall act as trustee for a Bondholders. The Bondholders present in person or by proxy at said meeting, or at any adjourned meeting thereof, shall prescribe the manner in which the successors of the persons elected to the Bondholders' Committee at such Bondholders' meeting shall be elected or appointed, and may prescribe rules and regulations governing the exercise by the Bondholders' Committee of the power conferred upon it, and may provide for the termination of the existence of the Bondholders' Committee.

Suits at Law or Equity and Mandamus. In case any one or more of the Events of Default shall happen and be continuing, then and in every such case, but subject to the provisions, limitations and conditions contained in the Certificate so far as the remedies provided in the Certificate are concerned, the Holder of any Bond at the time Outstanding shall be entitled, for the equal benefit and protection of all Holders of the Bonds similarly situated to proceed and protect and enforce the rights vested in such Holder by the Certificate by such appropriate judicial proceeding as such Holder shall deem most effectual to protect and enforce any such right, either by suit in equity or by action of law, whether for the specific performance of any covenant or agreement contained in the Certificate, or in aid of the exercise of any power granted in the Certificate, or to enforce any other legal or equitable right vested in the Holders of Bonds by the Certificate or by law.

Remedies Not Exclusive: Effect of Waiver of Default; Effect of Abandonment of Proceedings or Adverse Determination. The Holders from time to time of the Bonds shall be entitled to all the remedies and benefits of the Certificate as is and as shall be provided by law, and nothing herein shall be construed to limit the rights or remedies of any such Holders under any applicable statute that may now exist or be enacted hereafter. The remedies prescribed by the Certificate shall not be exclusive of any other remedy or remedies, and each and every such remedy shall be cumulative and shall be in addition to every other remedy given thereunder, or now or hereafter existing at law or in equity or by statute and may be exercised without exhausting and without regard to any other remedy.

No waiver of any default or breach of duty or contract by any Holder or any Bond shall extend to or affect any subsequent default or breach of duty or contract, or shall impair any rights or remedies thereon. No delay or omission of any Holder of a Bond to exercise any right or power accruing upon any default shall impair any such right, or power or shall be construed to be a waiver of any such default or acquiescence therein. Every substantive right and remedy conferred upon the Holders of the Bonds may be enforced from time to time and as often as may be deemed expedient. In case any suit, action or proceeding to enforce any right or exercise any remedy shall be brought or taken and then discontinued or abandoned, or shall be determined adverse to the Holders of the Bonds, then and in every such case the State and such Holders shall be restored to their former positions and rights and remedies as if no suit, action or proceeding had been brought or taken.

Discharge of Obligations of the State Under the Certificate [Certificate Section 11.01]

The obligations of the State, including, without limiting the generality of the foregoing, of the Department, under the Certificate and the liens, pledges, charges, trusts, assignments, covenants and agreements of the State, including the Department, therein made or provided for, shall be fully discharged and satisfied as to any Bond and such Bond shall no longer be deemed to be Outstanding under the Certificate,

(A) if such Bond shall have been purchased and cancelled by the State or surrendered to the Director of Finance or other Paying Agent, transfer agent or Registrar for cancellation or be subject to cancellation by him or it, or

(B) as to any Bond not theretofore purchased and cancelled, surrendered for cancellation or subject to cancellation, when payment of the principal of and the applicable redemption premium, if any, on such Bond, plus interest on such principal (calculated, in the case of Variable Rate Bonds, at the maximum numerical rate permitted by the terms thereof) to the due date thereof (whether such due date be by reason of maturity or upon redemption or prepayment or by declaration as provided in the Certificate, or otherwise) either

(1) shall have been made or caused to be made when due and payable in accordance with the terms thereof, or

(2) shall have been provided by irrevocably depositing with the Director of Finance or other Paying Agent therefor, in trust solely for such payment, either (i) moneys sufficient to make such payment or (ii) Federal Securities maturing as to principal and interest in such amounts and at such times as will insure the availability of sufficient moneys to make such payment, or (iii) a combination of both moneys and Federal Securities, and all necessary and proper fees, compensation and expenses of any Paying Agent, transfer agent or Registrar appointed by the State pertaining to the Bond with respect to which such deposit is made shall have been paid or the payment thereof provided for to the satisfaction of such Paying Agent, transfer agent or Registrar. At such time as a Bond shall be deemed to be no longer Outstanding under the Certificate, as aforesaid, except for the purpose of any such payment from such moneys or Federal Securities, such Bond shall no longer be secured by or entitled to the benefits of the Certificate and shall cease to accrue interest from the due date thereof (whether such due date be by reason of maturity or upon redemption or prepayment or by declaration as provided therein, or otherwise).

Notwithstanding the foregoing, with respect to Bonds which by their terms may be redeemed or otherwise prepaid prior to the stated maturities thereof and which the State elects to so redeem or prepay, no deposit under clause (2) of subparagraph (B) above shall constitute such discharge and satisfaction as aforesaid until such Bonds shall have matured or shall have been irrevocably called or designated for redemption or prepayment and proper notice of such redemption or prepayment shall have been given as provided in the Certificate or irrevocable provision shall have been made for the giving of such notice; provided that nothing in the foregoing shall require or be deemed to require the State to elect to redeem or prepay such Bonds or, in the event the State shall elect to redeem or prepay such Bonds, shall require or be deemed to require the redemption or prepayment as of any particular date or dates.

Any such moneys so deposited with the Director of Finance or other Paying Agents as described above may at the direction of the Department be invested and reinvested in Federal Securities, maturing in the amounts and times as hereinbefore set forth, and all income from all such Federal Securities in the hands of the Director of Finance and other Paying Agents which is not required for the payment of the Bonds and interest and premium, if any, thereon with respect to which such moneys shall have been so deposited, shall, to the extent permitted by law, be deposited in the Highway Revenue Special Account as and when realized and collected for use and application as are other moneys deposited in such Fund.

Notwithstanding the foregoing, the payment of (i) the purchase price of and interest on Variable Rate Bonds tendered for purchase pursuant to the terms thereof and of a remarketing agreement, or similar agreement, or (ii) principal of or interest on any Variable Rate Bonds with a draw, borrowing or payment under a Support Facility shall not be deemed payment of such Variable Rate Bonds pursuant to the Certificate; provided, however, that with respect to (ii) above, a reimbursement or other payment by the State with respect to a draw, borrowing or payment under a Support Facility for the payment of principal, premium, if any, or interest on Variable Rate Bonds when due, shall be deemed to the payment of such Variable Rate Bonds for the purpose of said provision.

All moneys or Federal Securities set aside and held in trust pursuant to the foregoing provisions for the payment of Bonds (including interest and premium thereon, if any) shall be applied to and used solely for the payment of the particular Bonds (including interest and premium thereon, if any) with respect to which such moneys and Federal Securities have been so set aside in trust.

If moneys or Federal Securities have been deposited or set aside with the Director of Finance or other Paying Agent pursuant to the Certificate for the payment of Bonds and such Bonds shall be deemed to have been paid and be no longer Outstanding, but such Bonds shall not have in fact been actually paid in full, no amendment to the provisions of the Certificate relating to the defeasance of Bonds shall be made without the consent of the Holder of each Bond affected thereby and such Bonds shall be considered to be Outstanding for purposes of the Certificate.

The State may at any time surrender to the Director of Finance for cancellation by him any Bonds previously executed and delivered, which the State may have acquired in any manner whatsoever, and such Bonds upon such surrender for cancellation shall be deemed to be paid and no longer Outstanding.

Additional Provisions Regarding Support Facilities [Articles VI and VII, Sixth Supplemental Certificate]

The Policy and Reserve Policy to be issued by Financial Security, as described in this Official Statement, will constitute Support Facilities with respect to the 2003 Bonds for purposes of the Certificate. The following is a brief description of certain provisions of the Sixth Supplemental Certificate regarding the Policy and the Reserve Policy.

The Policy. Unless it fails to honor its obligations under the Policy, Financial Security shall be deemed to be the holder of all Insured Bonds for the purpose of exercising any rights of holders to take, direct or consent to any actions taken pursuant to the Certificate, including actions taken upon the occurrence of an Event of Default. If the Insured Bonds are accelerated, Financial

Security may elect to pay the principal of and interest on the Insured Bonds either on the accelerated payment date or on the scheduled payment dates as if no acceleration had occurred. Upon making any payments under the Policy, Financial Security shall be subrogated to the rights of the holders of the Insured Bonds to the extent of such payments. Subject to the provisions of the Sixth Supplemental Certificate, Financial Security shall also have the rights, among others, to receive specified financial information and notices of certain material events regarding the Department, and to consent to amendments or supplements to the Certificate which require the consent of Bondholders.

The Reserve Policy. If the Department fails to reimburse Financial Security for draws under the Reserve Policy, Financial Security shall be entitled to exercise any and all legal and equitable remedies available to it other than (i) acceleration and (ii) any other remedy which adversely affects any holders of Senior Bonds. Subject to the provisions of the Sixth Supplemental Certificate, Financial Security shall also have the rights, among others, to receive specified financial information and notices of material events regarding the Department, and to consent to amendments or supplements to the Certificate which require the consent of Bondholders.

**ADDITIONAL INFORMATION RELATING TO REVENUE SOURCES,
THE STATE HIGHWAY SYSTEM AND
THE DEPARTMENT OF TRANSPORTATION**

This Appendix B contains additional information relating to Revenue sources and other factors affecting the Department's ability to raise Revenues, federal aid to Hawaii, the State Highway System and the Department of Transportation.

INFORMATION RELATING TO REVENUE SOURCES

Motor Vehicle Registration. The following table sets forth the total number of motor vehicle registrations subject to renewal in the State by type of vehicle for each of the ten calendar years ending December 31, 2002.

Motor Vehicle Registration

<u>Calendar Year</u>	<u>Passenger Vehicles</u>	<u>Ambulances & Hearses</u>	<u>Buses</u>	<u>Trucks</u>	<u>Motorcycles & Scooters</u>	<u>Trailers</u>	<u>Total</u>
1993	693,283	48	4,032	165,209	16,540	23,398	903,550
1994	691,158	53	3,772	163,227	16,934	22,864	898,008
1995	694,239	54	3,660	162,415	17,388	23,535	901,291
1996	703,094	59	3,468	160,742	17,254	23,153	907,770
1997	704,693	54	3,226	159,134	17,160	22,697	906,964
1998	713,732	61	3,084	159,614	16,936	22,326	915,753
1999	725,142	59	3,028	161,698	17,008	22,539	929,474
2000	754,840	56	2,902	165,783	17,661	23,496	964,738
2001	775,737	58	2,847	169,223	19,286	25,412	992,563
2002	792,482	62	2,814	171,813	20,427	25,996	1,013,594

Source: Department of Business, Economic Development and Tourism, Research and Economic Analysis Division, Statistics Branch. Department of Transportation Motor Vehicle Safety Office.

Licensed Drivers. The following table sets forth the total number of drivers licenses in force in the State for the ten calendar years ending December 31, 2002.

Drivers Licenses in Force

<u>Year</u>	<u>Oahu</u>	<u>Hawaii</u>	<u>Maui</u>	<u>Kauai</u>	<u>Total</u>
1993	522,016	92,264	78,191	41,910	734,381
1994	527,756	94,257	80,643	42,736	745,392
1995	516,780	94,048	79,639	42,041	732,508
1996	515,780	94,943	80,998	41,775	733,496
1997	517,904	96,665	82,217	42,079	738,865
1998	520,734	98,525	84,980	42,363	746,329
1999	521,671	100,331	87,550	43,141	752,693
2000	529,890	104,058	90,964	44,471	769,383
2001	542,244	106,557	93,595	45,424	787,820
2002	560,222	110,561	97,045	46,840	814,668

Source: Department of Transportation, Motor Vehicle Safety Office.

Fuel Consumption. The following table is a summary of the gallons of motor vehicle fuels imported into and consumed in the State, subject to the motor vehicle fuel tax for the ten fiscal years ending June 30, 2002.

Motor Vehicle Fuel Consumption
(In Thousands of Gallons)

<u>Fiscal Year</u>	<u>Gasoline</u>	<u>Diesel</u>	<u>Liquid Petroleum</u>	<u>Total</u>
1993	382,857	191,376	4,028	578,261
1994	394,081	181,457	4,065	579,603
1995	389,029	200,373	3,364	592,766
1996	397,078	177,883	3,665	578,626
1997	399,327	197,140	3,827	600,294
1998	395,866	185,612	3,821	585,299
1999	392,811	193,094	3,643	589,426
2000	391,114	310,299	3,583	704,996
2001	411,314	210,970	3,643	625,927
2002	416,827	219,694	3,179	639,700

Source: Department of Transportation.

FACTORS THAT MAY IMPACT REVENUE SOURCES

Potential Effect of International Hostilities and the Terrorist Attacks of September 11, 2001

Recent concerns regarding domestic security, particularly following the terrorist attacks of September 11, 2001, have had a negative effect on tourism in the State. Current U.S. military operations overseas may lead to additional

concerns over security. A decline in tourism could adversely affect the Revenues of the Highways System, and particularly Revenues from the rental motor vehicle and tour vehicle surcharge tax and the Highways fuel license tax. At this time, neither the State nor the Department can predict either the severity or duration of these effects.

Federal and County Fuel and Weight Taxes

Fuel taxes are presently imposed by federal, State and county governments. The retail price of a gallon of gasoline in the City and County of Honolulu presently includes fuel taxes of \$0.509 (\$0.184 federal + \$0.16 state + \$0.165 county) per gallon plus the State's 4% general excise tax, of which taxes only \$0.16 is the State fuel license tax. The feasibility of imposing additional taxes and fees on fuel and motor vehicles is affected in part by the amount and rate of fuel and other taxes and fees imposed by federal and county governments. These other taxes and fees are not pledged to the payment of the Bonds and are not available for such payment. The following is a summary of the various fuel taxes presently imposed by the federal government and fuel and vehicle taxes presently imposed by county governments:

Federal Fuel Taxes. The Internal Revenue Code imposes federal fuel taxes at the rate of \$0.184 per gallon of gasoline and \$0.244 per gallon of diesel fuel.

State General Excise Tax. The State's 4% general excise tax on goods and services extends to gasoline, diesel fuel and liquid petroleum gas. Since 1991, general excise tax collections have been paid to the State general fund, not the State Highway Fund.

County Fuel Taxes. Each county imposes a tax on gasoline, diesel oil and liquid petroleum gas for highway use. County fuel taxes are collected by the Department of Taxation together with the fuel license taxes and deposited into the respective county highway funds to be expended by each county on county highway improvements. The fuel tax rates for the County of Hawaii are \$0.088 per gallon of gasoline and diesel oil, and \$0.06 per gallon of liquid petroleum gas. The fuel tax rates for the City and County of Honolulu are \$0.165 per gallon of gasoline and diesel oil, and \$0.11 per gallon of liquid petroleum gas. The fuel tax rates for the County of Maui are \$0.13 per gallon of gasoline and diesel oil, and \$0.043 for liquid petroleum gas. The fuel tax rates for the County of Kauai are \$0.10 per gallon of gasoline and diesel oil, and \$0.07 per gallon of liquid petroleum gas.

County Vehicle Weight Taxes. Each county imposes and collects a tax on all vehicles, including motor vehicles, based on weight. Each county collects both State and county vehicle taxes and remits the State vehicle weight tax to the State to be paid into the State Highway Fund.

The county vehicle tax rates for the City and County of Honolulu are \$0.0125 per pound for passenger motor vehicles and noncommercial vehicles not exceeding 6,500 pounds, and \$0.02 per pound for commercial vehicles and all other motor vehicles, with a minimum of \$12.00 annually for all motor vehicles and \$1.00 annually for other vehicles.

The tax rates for the County of Maui are \$0.0125 per pound for passenger motor vehicles and noncommercial motor vehicles not exceeding 6,500 pounds, and \$0.020 per pound for nonpassenger commercial vehicles and all other motor vehicles, with a minimum of \$6.00 annually for all vehicles.

The tax rates for the County of Kauai are \$0.0075 per pound for passenger motor vehicles and noncommercial motor vehicles not exceeding 6,500 pounds, and \$0.02 per pound for nonpassenger vehicles and all other motor vehicles, with a minimum of \$12.00 annually for all vehicles.

The tax rates for the County of Hawaii are \$0.005 per pound for passenger motor vehicles and noncommercial motor vehicles not exceeding 6,500 pounds, and \$0.01 per pound for nonpassenger motor vehicles and commercial vehicles and motor vehicles over 6,500 pounds, with a minimum of \$6.00 annually for all vehicles.

County Vehicle Registration Fees

Each county imposes various registration fees for vehicles, including fees for certificates of registration, license plates and decals. Each county collects both State and county vehicle registration fees and remits the State vehicle registration fees and reimbursements for State-incurred expenses to the State to be paid into the State Highway Fund. The fees range from \$0.50 for decals, between \$2.00 to \$3.00 for registration certificates and between \$3.50 to \$5.00 for license plates.

None of such federal or county taxes or fees, nor the State general excise tax, is pledged to the payment of the Bonds or provides a source of revenues for such payment, but such taxes and fees do affect the feasibility of imposing additional charges on the use of vehicles.

FEDERAL AID TO HAWAII

Federal Aid Reimbursements

Generally the costs of financing highways for which the federal government provides assistance is undertaken on a shared basis with the State, with the federal government providing reimbursement to the State for 90% of eligible costs of construction when federal-aid funding is used on Interstate Highways and 80% of the costs on other highways and streets not functionally classified as local or rural minor collector roads. Federal aid reimbursements are deposited in the State Highway Fund. Such amounts are not Pledged Funds under the Certificate.

The following table sets forth federal aid reimbursements to the State for each of the last ten fiscal years ended June 30, 2002.

Federal Aid Reimbursements to the State

<u>Fiscal Year</u>	<u>Interstate</u>	<u>Primary</u>	<u>Secondary</u>	<u>Other</u>	<u>Total Amount Reimbursed</u>
1993	\$193,360,869	\$10,876,505	\$395,445	\$8,936,008	\$213,568,827
1994	180,269,823	3,382,703	1,237,141	33,131,081	218,020,748
1995	129,850,812	196,001	100,936	50,366,387	180,514,136
1996	114,012,607	4,039,307	1,195,734	69,686,057	188,933,705
1997	129,155,903	1,336,632	1,329,788	76,519,728	208,342,051
1998	66,735,974	186,552	411,853	67,257,999	134,592,378
1999	56,126,780	283,780	120,114	53,672,131	110,202,805
2000	20,813,022	307,449	283,863	57,611,498	79,015,832
2001	62,528,229	(226,626)	575,525	60,138,667	123,469,045
2002	12,299,728	2,040,319	2,106,025	122,276,644	138,722,716

Source: Department of Transportation

Intermodal Surface Transportation Efficiency Act of 1991 and Transportation Efficiency Act for the 21st Century

A significant portion of the federal aid reimbursements to the Department has been received pursuant to the Intermodal Surface Transportation Efficiency Act of 1991 ("ISTEA"). The stated purpose of said Act was "to develop a National Intermodal Transportation System that is economically efficient, environmentally sound, provides the foundation for the Nation to compete in the global economy and will move people and goods in an energy efficient manner." The major effect of ISTEA was to reorganize the manner in which federal aid for surface transportation projects, including

highways, would be provided to state and local governments. ISTEA provided authorization for federal assistance for highways, highway safety and mass transportation for federal fiscal years 1992 through 1997.

In 1998, Congress passed an ISTEA reauthorization bill called the Transportation Efficiency Act for the 21st Century ("TEA-21"). The bill reauthorizes the federal highway program for fiscal years 1998 through 2003. Hawaii's share of federal funds under TEA-21 will increase from \$116.4 million in 1998 to \$146.5 million in 2003. The average funding for the six year period is \$137.1 million. This is an increase of \$17 million over the average funding for the last three years of ISTEA (1995, 1996 and 1997) which was \$120.2 million. The actual apportionments of federal funds received were \$118.4 million in 1998; \$140.5 million in 1999; \$156.1 million in 2000; \$168.0 million in 2001; and \$171.7 million in 2002. The estimated apportionment of federal funds for 2003 is \$146 million. The increase in federal apportionments is primarily due to the additional funds authorized by the Revenue Aligned Budget Authority (RABA) and discretionary funds received.

THE STATE HIGHWAY SYSTEM

General

In the State, three levels of government have authority to construct and maintain public highways, streets and roads. These levels of government are the State, the counties and various federal agencies. The State is served by approximately 4,455 linear miles of public highways, streets and roads administered by the Department and the counties. An additional 138 miles of public highways, streets and roads open to the public in national parks and military reservations are the responsibility of various federal agencies, including the United States National Park Service and the military services.

There are four counties in the State: the City and County of Honolulu includes the entire island of Oahu and the uninhabited windward islands, Kauai County includes the islands of Kauai and Niihau, Maui County includes the islands of Molokai, Maui, Lanai and Kahoolawe, and Hawaii County is comprised of the island of Hawaii. There are no roadways or bridges connecting one island to another.

Honolulu, on Oahu, is the State's only major metropolitan area. Approximately 73% of the population of the State lives on Oahu.

The State's highways, streets and roads are discussed below, first by the level of government responsible for administering the roadways, followed by a discussion of the federal aid system and the functional classifications. The State Highway System receives most of the federal aid highway funds made available to the State.

State Highway System

The State Highway System, which is administered by the Department, consists of 936.75 linear miles of roadways. The Department has classified the State Highway System as follows: interstate (54.90 miles), freeway expressway (33.68 miles), principal arterial (241.50 miles), minor arterial (344.33 miles), major collector (262.34 miles), and minor collector (0 miles).

The following tables set forth the number of miles of the various categories of public highways, streets and roads, comprising the State Highway System.

State Highway System

<u>Functional Classification</u>	<u>Oahu</u>	<u>Hawaii</u>	<u>Maui</u>	<u>Kauai</u>	<u>Molokai</u>	<u>Lanai</u>	<u>Total</u>
Interstate	54.90	0.00	0.00	0.00	0.00	0.00	54.90
Freeway Expressway	33.68	0.00	0.00	0.00	0.00	0.00	33.68
Principal Arterial	117.88	69.29	37.21	17.12	0.00	0.00	241.50
Minor Arterial	26.91	220.26	46.56	50.60	0.00	0.00	344.33
Major Collector	6.22	64.75	85.14	39.03	53.52	13.68	262.34
Minor Collector	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>
Total	239.59	354.30	168.75	106.75	53.52	13.68	936.75

Source: Department of Transportation

The most important component of the State Highway System is the interstate system on Oahu. Interstate H-1 is a 27 mile freeway through the major populated areas of Honolulu, from Ewa on the western end of Oahu to Kahala on the eastern end. Interstate H-2 is an eight mile freeway from the H-1 freeway at Pearl City to the U.S. Army's Schofield Barracks in Wahiawa. Interstate H-3 is a recently-completed 16 mile freeway from the H-1 freeway at Halawa Valley in Pearl Harbor through the Koolau mountains to the U.S. Marine Corps Air Station at Kaneohe in windward Oahu. Interstate H-201, Moanalua Freeway connects to the H-1 Freeway at the Middle Street and Halawa Interchanges.

Other major State highways on the island of Oahu include the Pali Highway and Likelike Highway which connect Honolulu to the Windward Oahu communities of Kailua and Kaneohe, respectively, and Kamehameha Highway and Farrington Highway, which circle Oahu's windward and leeward coastlines. Kalaniana'ole Highway circles the eastern part of Oahu and connects eastern Honolulu to the windward coastline.

Major State highways on the island of Hawaii include the Queen Kaahumanu Highway in North Kona, the Kuakini Highway in South Kona, the Mamalahoa Highway in West Hawaii, and portions of the Hawaii Belt Road in East Hawaii.

Major State highways on the island of Kauai include Kaunualii Highway in west Kauai and Kuhio Highway in east Kauai.

Major State highways in Maui County, include on the island of Maui Honoapiilani Highway and Kahekili Highway in West Maui and Hana Highway, Haleakala Highway, Mokulele Highway and Piilani Highway in east Maui. Maunaloa Highway and Kamehameha V Highway are the major State roads on the island of Molokai.

Federal Agencies

Various federal agencies have jurisdiction over certain public highways, streets and roads open to the public in national parks and military reservations in the State, including the United States National Park Service and the military services. The United States National Park Service also builds and maintains roads within the boundaries of the national parks.

THE DEPARTMENT OF TRANSPORTATION

Management Directions. The Department continues to focus its management efforts on programs that will bring about operational improvements and cost efficiencies through innovation and new technology. The Department

implemented a new concept approach to working with the private sector referred to as “partnering.” All parties must agree to commit to the quality, safety, timeliness and cost efficiency of the project.

To increase efficiency for planning and maintaining highway improvements, the Department will be utilizing an integrated and automated database management system. This Coordinated Data System (CDS) will compile all highway improvement data (e.g., road inventory, pavement condition survey, vehicular traffic, highway improvement and maintenance expenditure) provided by the various offices within the Department. Updating and maintenance of such data will be transmitted electronically to the CDS.

The Department also installed a Computer-Aided Drafting and Design (“CADD”) System to increase design accuracy and efficiency. The CADD system automates drafting of contract plans, right-of-way plans, maps, roadway design and surveying. The CADD system consists of 35 CADD workstations, 6 servers, plotters and peripherals.

To service the general public more efficiently, the Department installed electronic highway message signs at various locations on Oahu to forewarn motorists of lane closures, obstructions or accidents ahead. The Department also keeps the employees and general public informed on projects, events, public hearings and departmental news with newsletters, an internet site and provides telephone hotlines for instant information and feedback.

Oahu Metropolitan Planning Organization (“OMPO”). The Federal Surface Transportation Assistance Act of 1973 and other federal laws require states to designate and fund a metropolitan planning organization (MPO) for any urbanized area with a population greater than 50,000 to ensure that the plans and program for each metropolitan area shall provide for the development and integrated management and operation of transportation systems and facilities that will function as an intermodal transportation system for the metropolitan area. The process for developing the plan and program is required to provide for the consideration of all modes of transportation and to be continuing, comprehensive, and cooperative.

In 1975, the State Legislature established the Oahu Metropolitan Planning Organization (OMPO), an advisory organization responsible for coordinating transportation planning for Oahu. The decision making body of OMPO is its Policy Committee, which consists of six state legislators, five Honolulu City Council members, the Director of the State Department of Transportation and the Director of the City Department of Transportation Services.

OMPO is responsible for identifying Oahu’s future transportation needs and programming the federal funds for projects and programs. The federal funds are programmed based on a process which prioritizes the projects based on needs and available funding. This is achieved through the development of the following three documents :

- (a) The Oahu Regional Transportation Plan (ORTP) – The 25 year long range transportation plan for Oahu.
- (b) The Overall Work Program (OWP) – Annual work program that identifies all of OMPOs planning activities.
- (c) The Transportation Improvement Program (TIP) - The three year multimodal transportation improvements program for Oahu, that is updated every two years.

Statewide Transportation Improvement Program (“STIP”). On October 24, 2001, the Federal Highway Administration and the Federal Transit Administration approved the STIP for Fiscal Years 2002-2004. The Department is currently working on revising the Fiscal Year 2003 STIP. The Department has started developing the STIP for Fiscal Years 2004-2006 and will obtain approval from the Federal Highway Administration and the Federal Transit Administration by October 2003.

THE STATE OF HAWAII

The statistical information presented by this Appendix C is the most current information available to the State. Because such information becomes available at different times, the dates of such information, as presented herein, are not the same.

INTRODUCTION

General

The State was admitted into the Union on August 21, 1959, as the fiftieth state. It is an archipelago of eight major islands, seven of which are inhabited, plus 124 named islets, totaling 6,425 square miles in land area, located in the Pacific Ocean in the Northern Hemisphere, mostly below the Tropic of Cancer, about 2,400 statute miles from San Francisco. The State is slightly larger than the combined area of the States of Connecticut and Rhode Island and ranks forty-seventh of the fifty states in land area, being also larger in area than the State of Delaware. The island of Hawaii is the largest island, with 4,028 square miles in area. The other inhabited islands in the order of size are Maui, Oahu, Kauai, Molokai, Lanai and Niihau. According to the U.S. Census, the total population of the State was 422,770 in 1940, 499,794 in 1950, 632,772 in 1960, 769,913 in 1970, 964,691 in 1980, 1,115,274 in 1990, and 1,211,537 in 2000, making the State the forty-second most populous state in the Union as of 2000. The City and County of Honolulu consists of the island of Oahu (plus some minor islets) with a land area of 599.8 square miles. The capital of the State and the principal port are located on Oahu. According to the 2000 U.S. Census, about 72.3% of the population of the State lives on Oahu. Hawaii's population shows greater ethnic diversity than other states because it is descended from immigrants from the Far East as well as from Europe and the mainland United States. The 2000 U.S. Census indicated that about 41.6% of the State's population is of Asian descent and about 24.3% of the State's population is Caucasian. Native Hawaiians and other Pacific Islanders constitute 9.4% of the population. The balance consists of other races, such as African Americans and American Indians.

State Government

The Constitution of the State provides for three separate branches of government: the legislative, the executive and the judicial. The legislative power is vested in a bicameral Legislature consisting of a Senate of twenty-five members elected for four-year terms and a House of Representatives of fifty-one members elected for two-year terms. The Legislature convenes annually. The executive power is vested in a Governor elected for a four-year term. In the event of the absence of the Governor from the State, or his inability to exercise and discharge the powers and duties of his office, the Lieutenant Governor, also elected for a four-year term, serves as the chief executive. Under the Constitution, the judicial power is vested in a Supreme Court, one intermediate appellate court, circuit courts, district courts, and such other courts as the Legislature may from time to time establish. Pursuant to statute, the Legislature has established four circuit courts, four district courts and an intermediate appellate court. The executive and administrative offices are limited to not more than twenty principal departments under the supervision of the Governor. The executive functions have in fact been grouped into eighteen departments. The heads of the departments are appointed by the Governor with the advice and consent of the Senate and hold office for a term to expire with the term of the Governor. The Department of Budget and Finance is one of the principal departments permitted by the Constitution of the State, with the head of said department being designated as the Director of Finance. Under the general direction of the Governor, the Department of Budget and Finance administers the State's proposed six-year program and financial plan, the State budget, and financial management programs of the State.

The Counties and Their Relationship to the State

There are four counties in the State, being the City and County of Honolulu, the County of Maui, the County of Hawaii and the County of Kauai, and one quasi-county, Kalawao. Each of the counties has a separate charter for its

government, each of which provides for an elected mayor and an elected council. The mayor is the chief executive and the council is the legislative body. *There are no independent or separate cities or other municipalities, school districts or townships.* The State government of Hawaii has total responsibility for many functions which in most other parts of the United States are performed by or shared by local governments. For example, the State pays all costs in connection with the public school system, libraries, public welfare, and judiciary. The greatest expenditures by the State in past years have been in the areas of education and public welfare. The counties' major areas of responsibility and expenditure are in police and fire protection, waste disposal, water and sewer facilities, and secondary streets and highways.

GENERAL ECONOMIC INFORMATION

General

Certain of the following material pertaining to economic factors in the State under the captions "State of the Economy" through and including "Table 10" has been excerpted from the December 2002 Quarterly Statistical and Economic Report ("QSER") prepared by the State of Hawaii Department of Business, Economic Development and Tourism ("DBEDT") and may be found at <http://www.hawaii.gov/dbedt/qsrl201/index.html>. Unless otherwise stated, the following information is historical; estimated figures are used only when the definitive figures are unavailable. The text refers to certain enumerated tables found under "GENERAL ECONOMIC INFORMATION."

Following descriptions of the various components of the State's economy and DBEDT's outlook for the economy, there is a brief description of the impact of these components on the State's fiscal position.

DBEDT's current forecast for real Gross State Product ("GSP") (the value of all goods and services produced and consumed within the State adjusted for inflation) growth in 2002 is 4.0%. In real terms (adjusting for inflation), DBEDT estimates that 2002 GSP growth over 2001 will be 2.1%.

State of the Economy

Economic data show that Hawaii is continuing to recover from the trials of the past year. Based on year-over-year growth rates for the third quarter 2002, Hawaii is improving in terms of planned and completed construction, general fund tax revenues, and visitor arrivals compared to the growth rates for the third quarter of 2001. However, the third quarter 2002 growth rates for labor force, civilian employment, wage and salary jobs, and income tax collections are down from third quarter 2001 levels.

In the third quarter of 2002, labor force and civilian employment in Hawaii were down 1.7% and 1.4%, respectively, which represent the second straight quarterly decline for each. On average, for the third quarter, 570,500 people were employed in Hawaii, 8,000 fewer than the year before. The unemployment rate was down in the third quarter of 2002 from 4.6% to 4.3% in the same period 2001.

The number of wage and salary jobs was down 1.0% measured year-to-year for the third quarter. The three industries that continue to account for most of the job losses, Transportation, Retail Trade, and Hotel jobs, recorded 9.9%, 3.3% and 5.4% decreases respectively. Increases were seen in Construction (4.9%); Finance, Insurance and Real Estate; (0.9%); Health Services (2.3%); Business Services (1.4%); Agriculture (8.8%) and Government (1.8%).

Nominal personal income rose 3.9% in the second quarter of 2002 compared to the second quarter of 2001, the period for which the most recent data are available. Transfer payments showed the highest rate of increase (8.8%) followed by other labor income (8.7%), wages and salaries (3.3%), proprietors' income (2.8%) and dividends, interest, and rent (1.6%). Most industries saw year-to-year quarterly increases in earnings with the exception of Manufacturing, Transportation and Public Utilities, and Retail Trade.

Tax revenues distributed to the State general fund were up 4.0% for the third quarter of 2002 compared to 2001. The general excise and use tax (GET) revenues increased by 16.4% in the third quarter of 2002. Transient

Accommodations Tax (TAT) revenues increased 7.3%. Revenues from the individual income tax decreased 8.0% over the third quarter's 2001 to 2002 period.

The number of visitors arriving by air increased 2.4% from the third quarter of 2001 to that of 2002, which is the first positive year-over-year quarterly growth in total visitor arrivals since the fourth quarter of 2000. Average daily visitor census numbers increased 6.3% in the third quarter. Hotel occupancy rates were also up, increasing from 70.3% in the third quarter of 2001 to 72.4% in the third quarter of 2002.

Hawaii construction industry activity continued to grow in the third quarter of 2002. The contracting tax base increased by 35.9% while total private authorizations increased 18.2%. As previously mentioned, construction jobs were up 4.9%.

In the third quarter of 2002, Hawaii bankruptcy filings decreased by 4.8%. U.S. filings were at record numbers.

Outlook for the Economy

By the end of the third quarter of 2002, year-to-date indicators of Hawaii's economy continued positive. Visitor arrivals continue to climb toward pre-2001 levels, tax revenues continue to improve, and construction and home sales remain strong. These signs must, however, be weighed in conjunction with the sluggish conditions prevailing in the Mainland and Japan economies. The following forecast attempts to recognize current security uncertainties and concerns, but it was assumed that no new catastrophic event would occur to further retard economic recovery.

The rate of recovery of visitor markets and U. S. and international economic performance are factors that will directly impact the rate of economic recovery in Hawaii. The consensus projections of U.S. economic performance have continued to weaken. The Blue Chip Economic Forecast, which is based on an average of 50 major U.S. forecasts, adjusted the forecast for growth in real U.S. GDP in 2002 downward in August from 2.8% to 2.3% and has maintained it at the 2.3% to 2.4% level through November. The Blue Chip Forecast for real U.S. GDP in 2003 was reduced from 3.6% in July to 2.8% in November.

Expectations are for Japan's economy to remain weak. Japan's real GDP declined at a 0.2% rate in 2001. For 2002, the Blue Chip Forecast expects Japan's economy to show a further 0.7% decline in GDP recovering to a 0.9% increase in real GDP in 2003.

Hawaii visitor counts are expected to improve. In 2002, total visitor arrivals are predicted to grow 1.8% and visitor expenditures are forecast to increase 2.2% from their depressed state during 2001. The positive growth in visitor arrivals comes from the strong recovery of tourism from the Western U.S. Mainland offsetting reduced levels of visitors from Japan. Visitor arrivals are projected to approach 2000 levels in 2003 with a further 6.1% increase over 2002 and then return to their historical growth range of 2.1% to 2.5% annually in the 2004-2005 period.

Total wage and salary jobs in the State are expected to finish 2002 at 0.5% below the 2001 total. This a reduction from the previous quarter's projection based on a weaker than expected third quarter employment rebound. Job growth is expected to be positive again in 2003 with a 1.6% growth rate.

After inflation, real personal income is forecast to show a 2.5% increase in 2002 and a 2.4% increase in 2003. This projection is up from the September forecast in response to a higher than expected second quarter estimate reported by the Bureau of Economic Analysis.

Honolulu's CPI is projected to remain low with a 1.2% increase in 2002 climbing to a 1.7% inflation rate in 2003. The projection for 2003 has been increased from the second quarter projection, because national price projections by Blue Chip and Anderson UCLA were raised at year-end.

Information on Employment, Wages and Salaries, Tax Revenues and Tax Base

Table 1
SELECTED ECONOMIC ACTIVITIES: STATE

SERIES	UNIT	3 rd QUARTER 2002		YEAR TO DATE	
		NUMBER	% CHANGE YEAR AGO	NUMBER	% CHANGE YEAR AGO
CIVILIAN LABOR FORCE ⁽¹⁾	Persons	593,300	-1.7	599,250	-0.8
Civilian Employment.....	Persons	570,500	-1.4	572,700	-0.8
Civilian Unemployment.....	Persons	25,800	-7.5	26,550	-0.4
UNEMPLOYMENT RATE ⁽²⁾	%	4.3	-0.3	4.4	0.0
TOTAL WAGE & SALARY JOBS ⁽¹⁾	Jobs	553,300	-1.0	556,100	-1.0
TOTAL NON-AGRICULTURE WAGE & SALARY ⁽¹⁾	Jobs	545,250	-1.2	548,450	-1.1
Contract Construction.....	Jobs	24,700	4.9	24,400	3.2
Manufacturing.....	Jobs	17,600	-2.2	17,650	-1.7
Transportation, Communication, Utilities.....	Jobs	38,950	-8.6	38,850	-9.4
Trade.....	Jobs	132,700	-3.0	132,400	-3.4
Retail.....	Jobs	112,050	-3.3	112,000	-3.6
Finance, Insurance, & Real Estate.....	Jobs	33,150	0.9	33,000	1.1
Services & Miscellaneous.....	Jobs	185,900	-1.9	185,050	-0.9
Hotels.....	Jobs	36,950	-5.4	36,850	-6.1
Health.....	Jobs	38,200	2.3	37,950	2.4
Business.....	Jobs	32,050	1.4	31,750	1.8
Government.....	Jobs	112,350	1.8	117,100	2.9
State.....	Jobs	64,600	2.5	70,050	4.8
Federal.....	Jobs	30,450	1.0	30,100	-0.2
Local.....	Jobs	17,300	0.9	16,950	1.5
AGRICULTURE WAGES AND SALARIES ⁽¹⁾	Jobs	8,050	8.8	7,700	5.5
STATE GENERAL FUND REVENUES.....	\$1,000	820,290	4.0	2,340,010	-3.8
TRANSIENT ACCOMMODATIONS TAX.....	\$1,000	48,199	7.3	124,883	-9.9
GENERAL EXCISE AND USE TAX.....	\$1,000	473,241	16.4	1,269,499	1.5

Notes: (1) Labor force and jobs based on monthly rounded data were rebenchmarked in April 2002.

(2) Change represents absolute change in rates rather than percentage change in rates.

Sources: Hawaii State Department of Labor & Industrial Relations; Hawaii State Department of Taxation; and Smith Travel Research, PricewaterhouseCoopers LLP. Compiled by Hawaii State Business Economic Development & Tourism Planning Information System.

Key Economic Indicators

Table 2
ACTUAL AND FORECASTED KEY ECONOMIC INDICATORS
FOR HAWAII: 2001 TO 2005

Economic Indicators	2001	%	2002	%	2003	%	2004	%	2005	%
	Actual	Change	Forecast	Change	Forecast	Change	Forecast	Change	Forecast	Change
Total population (thousands).....	1,224.4	1.0	1,236.6	1.0	1,249.0	1.0	1,261.5	1.0	1,274.1	1.0
Visitor arrivals (thousands).....	6,303.8	-9.3	6,417.3	1.8	6,808.7	6.1	6,978.9	2.5	7,125.5	2.1
Honolulu CPI-U (1982-84=100).....	178.4	1.2	180.5	1.2	183.7	1.7	187.2	1.9	190.7	1.9
Personal income (million dollars).....	35,509.6	3.5	36,850.5	3.8	38,410.4	4.2	39,862.5	3.8	41,377.2	3.8
Real Personal income (\$1996 million).....	33,976.9	2.3	34,841.9	2.5	35,694.4	2.4	36,353.6	1.8	37,031.9	1.9
Total wage & salary jobs (thousands).....	561.0	0.3	558.3	-0.5	567.2	1.6	576.3	1.6	585.5	1.6
Gross state product (million dollars).....	43,973.8*	3.8*	45,732.8	4.0	47,653.6	4.2	49,709.9	4.3	51,797.7	4.2
Real gross state product (\$1996 million).....	39,034.1*	1.2*	39,838.6	2.1	40,674.5	2.1	41,457.4	1.9	42,208.7	1.8
Gross state product deflator (1996=100).....	112.7*	2.6*	114.8	1.9	117.2	2.1	119.9	2.3	122.7	2.3

* Preliminary.

Source: Hawaii State Department of Business, Economic Development & Tourism, December 13, 2002.

Labor Force and Jobs

Hawaii's civilian employment declined by 1.4% in the third quarter of 2002 from the third quarter of 2001 or about 8,000 fewer persons employed. This third quarter decline followed a 1.0% decline in the second quarter of 2002. Hawaii's civilian employment is now at the same level it was in the third quarter of 2000. (Table 3)

Civilian labor force was down, decreasing by 1.7%, or 10,150 persons over the third quarter of 2001. (Table 3) This was the second quarterly decrease in Hawaii's labor force. The labor force increase observed during 2001 may have been related in part to Federal Welfare Reform. In November 2001, the 60-month limit on welfare benefits expired for those receiving benefits at the December 1996 effective date of the reform program. Several thousand Hawaii residents would have been required to enter the labor force in advance of November 2001.

The number of unemployed was 2,100, or 7.5%, fewer than the third quarter of 2001. As a result of the number of unemployed declining by a greater percentage than the decline in the labor force, the unemployment rate declined from 4.6% to 4.3% from the third quarter of 2001 to the third quarter 2002. (Table 3)

Total wage and salary jobs were down 1.0% measured year-to-year for the third quarter. The same three industries that have accounted for most of the job losses since September 2001 continue to lead the overall decline in jobs. Between the third quarters of 2002 and 2001, Retail Trade is down 3,850 jobs, Transportation is down 3,250 jobs, and Hotel jobs are down 2,100. These amounted to 3.3%, 9.9% and 5.4% decreases respectively from third quarter 2001, but all three industries have improved from the second quarter of 2002. (Table 1)

Several other industries showed negative job growth in the third quarter of 2002 compared to the same period in 2001. Jobs declined in Manufacturing (-2.2%); Communication (-6.3%); Utilities (-2.9%); and Wholesale Trade (-1.4%). (Table 1)

Private sector jobs increased in Construction, 4.9%; Finance, Insurance and Real Estate, 0.9%; Health Services, 2.3%; Business Services, 1.4%; and Agriculture, 8.8%. Jobs increased in all three government sectors in the third quarter of 2002. Federal government jobs rose 1.0 % from the third quarter of 2001, State government jobs increased by 2.5%, and local government jobs increased by 0.9%. (Table 1)

Table 3
CIVILIAN LABOR FORCE AND EMPLOYMENT
(in thousands of persons)

Year	Civilian Labor Force	% Change Civilian Labor Force	Civilian Employment	% Change Civilian Employment	Civilian Unemployment Rate
1992	584.0	1.8	557.4	-0.1	4.6
1993	586.0	0.3	560.9	0.6	4.3
1994	580.2	-1.0	545.0	-2.8	6.1
1995	576.4	-0.6	542.7	-0.4	5.9
1996	593.6	3.0	555.8	2.4	6.4
1997	594.7	0.2	556.7	0.2	6.4
1998	594.4	-0.1	557.2	0.1	6.2
1999	592.8	-0.3	559.6	0.4	5.6
2000	595.5	0.4	569.9	1.8	4.3
2001	605.5	1.7	577.5	1.3	4.6
2002 ¹	596.3	-1.7	570.5	-1.4	4.3

¹ As of Third Quarter 2002.

Note: Data from 1999 First Quarter were rebenchmarked by DLIR in April 2002.

Source: Hawaii State Department of Labor and Industrial Relations.

Income and Prices

Personal income continued to grow at a moderate rate during the second quarter of 2002 (the period for which the latest data are available from the Bureau of Economic Analysis) measured over the second quarter of 2001. Transfer

payments and other labor income showed the highest rates of increase followed by wages and salaries; proprietors' income; and dividends, interest, and rent. There were year-to-year quarterly increases in earnings for most industries, but Manufacturing; Transportation and Public Utilities; and Retail Trade showed decreases. (Table 4)

Nominal personal income, not adjusted for inflation, rose \$1.4 billion, or 3.9% in the second quarter of 2002 compared to the second quarter of 2001. The wage and salary component grew by about \$650 million, or 3.3% in the second quarter of 2002. Wages and salaries accounted for about 56% of personal income. (Table 4)

Other labor income, consisting of employer payments to retirement plans, private group health insurance plans, private workers compensation plans, and other such benefits, increased by \$260 million, or 8.7% in the second quarter of 2002 compared to 2001. (Table 4)

Proprietors' income, the income most closely related to entrepreneurial activity, grew by \$79 million, or 2.8% in the second quarter of 2002 compared to the second quarter of 2001. (Table 4)

Dividends, interest, and rent rose by \$110 million, or 1.6% in the second quarter of 2002. Transfer payments, consisting largely of retirement and medical payments, grew by \$380 million, or 8.8% for the quarter. (Table 4)

Private sector earnings increased across most industries. In dollar terms, the largest increases came in Services followed by Finance, Insurance and Real Estate and Construction. Earnings declined by 1.2% in Manufacturing; by 4.8% in Transportation and Public Utilities; and by 1.2% in Retail Trade. Earnings increased by 9.1% in the public sector, largely as a result of the 14.3% increase in the State and local government component. (Table 4)

Increases in personal income are enhanced by the low rate of inflation that exists in the Hawaiian economy. The Honolulu consumer price index rose by only 1.1% in the first half of 2002 compared to the same period in 2001, which was lower than was expected for Honolulu and also somewhat lower than the 1.3% inflation experienced on the Mainland during the period. (Table 6)

Table 4

PERSONAL INCOME FOR HAWAII BY MAJOR SOURCES
(in millions of dollars at seasonally adjusted annual rates)

Series	Annual Average 2000	Annual Average 2001	% Change Ann. Ave. 2000-2001	Second Quarter 2001	Second Quarter 2002	% Change 2 nd Qtr 01 - 2 nd Qtr 02
Derivation of Personal Income						
Wage and salary disbursements.....	19,270	19,885	3.2	19,835	20,482	3.3
Plus: Other labor income	2,851	3,009	5.5	2,992	3,253	8.7
Plus: Proprietors' income	2,717	2,788	2.6	2,800	2,879	2.8
Less: Personal contribution for social insurance.....	1,370	1,438	5.0	1,432	1,512	5.6
Dividends, interest, rent.....	6,751	6,895	2.1	6,891	7,001	1.6
Transfer payments	4,088	4,372	6.9	4,324	4,704	8.8
Personal income.....	34,308	35,510	3.5	35,411	36,807	3.9
Earnings by Industry.....	24,838	25,682	3.4	25,627	26,614	3.9
Farm	184	186	1.1	184	197	7.1
Nonfarm.....	24,654	25,496	3.4	25,443	26,417	3.8
Private.....	17,336	17,902	3.3	17,962	18,255	1.6
Agriculture forestry, fishery, other	154	159	3.2	157	160	1.9
Mining	27	27	0.0	26	29	11.5
Construction	1,477	1,525	3.2	1,515	1,614	6.5
Manufacturing	739	772	4.5	773	764	-1.2
Transportation and public utilities	1,961	1,981	1.0	1,993	1,897	-4.8
Wholesale trade	873	874	0.1	884	909	2.8
Retail trade.....	2,831	2,900	2.4	2,921	2,886	-1.2
Finance, insurance, real estate	1,922	1,985	3.3	1,980	2,082	5.2
Services.....	7,352	7,680	4.5	7,713	7,914	2.6
Government & government enterprises	7,319	7,594	3.8	7,481	8,162	9.1
Federal, civilian.....	1,953	1,970	0.9	1,992	2,051	3.0
Federal, military.....	2,403	2,557	6.4	2,558	2,759	7.9
State and local.....	2,963	3,068	3.5	2,931	3,351	14.3

Source: U.S. Department of Commerce, Bureau of Economic Analysis, State Quarterly Personal Income, June 24, 2002, and tabulations by the Hawaii State Department of Business, Economic Development & Tourism.

Table 5

PERSONAL INCOME
(in millions of dollars at seasonally adjusted annual rates)

YEAR	ANNUAL AVERAGE	% CHANGE ¹
1992	27,859	6.3
1993	29,068	4.3
1994	29,740	2.3
1995	30,202	1.6
1996	30,393	0.6
1997	31,218	2.7
1998	31,841	2.0
1999	32,573	2.3
2000	34,308	5.3
2001	35,510	3.5
2002 ²	36,807	3.9

¹ percentage change from the same period in previous year.

² As of second quarter 2002.

Source: U.S. Department of Commerce, Bureau of Economic Analysis. State Quarterly Personal Income: July 24, 2002 and tabulations by the Hawaii State Department of Business, Economic Development & Tourism.

Table 6

**CONSUMER PRICE INDEX, ALL URBAN CONSUMERS (CPI-U), AND
SELECTED ITEMS, FOR U.S. AND HONOLULU: 1992-2002 ²⁾**
(1982-1984 = 100)

Year	HONOLULU									
	U.S.	All Items	Food & Beverages	Housing	Apparel & Upkeep	Trans.	Medical Care	Recreation	Education & Comm.	Other Goods & Services
1992	140.3	155.1	148.5	161.7	114.2	147.4	182.6	(NA)	(NA)	189.0
1993	144.5	160.1	152.9	166.5	116.5	150.5	197.4	(NA)	(NA)	200.1
1994	148.2	164.5	153.4	171.6	118.7	156.4	206.0	(NA)	(NA)	209.6
1995	152.4	168.1	156.8	174.7	117.5	162.4	209.8	(NA)	(NA)	216.8
1996	156.9	170.7	156.6	176.8	118.5	167.0	215.0	(NA)	(NA)	226.5
1997	160.5	171.9	159.2	177.1	117.3	166.2	217.3	(NA)	(NA)	239.0
1998	163.0	171.5	159.1	176.0	112.2	162.5	226.1	100.8	99.1	256.1
1999	166.6	173.3	162.9	175.8	105.4	162.2	231.3	101.9	104.5	275.6
2000	172.2	176.3	164.8	177.9	103.5	169.6	239.8	102.8	106.5	279.7
2001	177.1	178.4	169.5	179.1	101.0	174.5	"	101.6	104.6	289.3
2002 ²⁾	178.9	180.1	172.3	180.5	106.2	171.7	"	99.9	106.9	299.1

¹⁾ No data were available or data did not meet U.S. Bureau of Labor Statistics' publication criteria.

²⁾ As of 1st half.

Source: U.S. Bureau of Labor Statistics, August 16, 2002.

Tourism

In the third quarter of 2002, Hawaii's visitor industry continued its recovery from the effects of the September 11, 2001 attacks. Both the number of visitor arrivals and the average daily visitor census were up from the third quarter 2001. These quarterly increases resulted from the large increases that occurred in September 2002 compared with the reduced visitor levels of September 2001. Hotel occupancy rates also showed improvement for the quarter.

The number of visitors arriving by air was up 2.4% in the third quarter of 2002 from the third quarter of 2001, which translates to about 40,000 more visitors than in the third quarter of 2001. The overall quarterly increase was produced by a healthy increase in domestic arrivals. The number of travelers on domestic flights increased by 6.8%, while arrivals on international flights fell by 6.2%, when the third quarter of 2002 is compared to the third quarter of 2001. (Table 7)

With respect to the different major market areas, the positive influence again comes from the domestic markets. The greatest increase came from the U.S. West that increased by about 47,000 visitors, or 7.3% from the third quarter 2001 to the third quarter 2002. Arrivals from the U.S. East were also up, increasing 3.6%, or a little over 13,000.

Visitors from Japan continued to decrease. In the third quarter of 2002, arrivals from Japan were down by over 35,000, or by 8.1% from the third quarter of 2001. The decline in visitor arrivals from Japan resulting from the recession in the Japanese economy and the weakening Yen, was accelerated by the September 11, 2001 event.

Average daily visitor census numbers followed the same pattern as visitor arrivals in the third quarter of 2002. For domestic visitors, those arriving on flights from U.S. mainland airports, average daily visitor census was up 9.7%, but it was down 3.5% for international visitors. This produced an increase in total visitor census of 6.3%. The average daily

census reflects both arrivals and length of stay. Average length of stay increased slightly for domestic visitors and international visitors in the third quarter (DBEDT Monthly Visitor Statistics). (Table 7)

8) Hotel occupancy rates rose from 70.3% in the third quarter of 2001 to 72.4% in the third quarter of 2002. (Table 8)

Table 7
VISITOR ARRIVALS ¹⁾
Average Length of Stay, Visitor Days, Average Daily Census
(Percentage Change from the Same Period in Previous Year)

	3 rd QUARTER 2001	3 rd QUARTER 2002	% Change
TOTAL ARRIVALS			
Total	1,647,050	1,686,817	2.4
Domestic	1,091,324	1,165,339	6.8
International	555,726	521,418	-6.2
AVERAGE LENGTH OF STAY			
Total	9.09	9.43	3.7
Domestic	10.11	10.38	2.7
International	7.08	7.29	3.0
VISITOR DAYS			
Total	14,966,033	15,901,939	6.3
Domestic	11,029,650	12,102,205	9.7
International	3,936,383	3,799,734	-3.5
AVERAGE DAILY CENSUS			
Total	162,674	172,747	6.3
Domestic	119,887	131,546	9.7
International	42,787	41,301	-3.5

1) *Staying overnight or longer.*

Source: *Hawaii State Department of Business, Economic Development & Tourism.*

Table 8
HOTEL OCCUPANCY RATE
(in percent)

Year*	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Annual
1992	75.3	68.6	75.5	75.2	72.7
1993	75.3	67.9	73.8	72.5	72.0
1994	80.9	72.7	79.1	74.8	76.5
1995	79.5	70.3	79.2	75.1	75.8
1996	81.9	72.3	77.1	70.0	75.2
1997	79.5	70.8	75.5	69.9	73.9
1998	77.4	68.7	72.9	67.7	71.5
1999	77.0	67.7	75.0	68.7	72.1
2000	79.2	75.2	78.5	73.1	76.0
2001	80.7	70.7	70.3	57.5	70.7
2002	70.8	67.5	72.4	NA	NA

NA – Not available.

Quarterly averages are computed by Hawaii State Department of Business, Economic Development & Tourism from PKF-Hawaii monthly averages through January 1995 and Hospitality Advisors LLC monthly

averages from February 1995.

* 1998 – 2001 quarterly data were revised.

Source: Hawaii State Department of Business, Economic Development & Tourism and PKF — Hawaii and Hospitality Advisors LLC.

Construction

Indicators of construction industry activity in Hawaii are generally positive in the third quarter of 2002. The contracting tax base and the value of government contracts awarded increased dramatically. Although less pronounced, private building authorizations also showed a healthy increase in the third quarter of 2002 compared to last year's third quarter level.

The contracting tax base, which measures construction activity subject to the general excise tax, increased by 35.9% from the third quarter of 2001 to the third quarter of 2002. GET was paid on \$1,213.7 million worth of construction in the third quarter of 2002. (Table 9)

Government contracts awarded were up a substantial 126.1% from the third quarter of 2001 to the third quarter of 2002. (Table 9) State Capital Improvement Project expenditures (CIP) were up for the third quarter by 6.6% over the third quarter of 2001. Most of the CIP expenditure was from General Obligation bond funds, but large shares were also from Special Funds and Federal Funds.

The value of residential building permit authorizations was up 35.3% statewide for the third quarter of 2002. (Table 9) The number of single family unit authorizations was up 24.2%. Multi-family units authorized were up 16.7%, but they account for a small share of the current residential construction market. Total private building permit authorizations for the State are up 18.2% for the third quarter of 2002. (Beginning in the first quarter of 2002, Kauai permit-value data are only for residential.) Honolulu's total private authorizations are up by 42.3% from the third quarter of 2001, Hawaii County authorizations increased 8.7%, Maui County was down 3.2% and Kauai residential was down 20.1%. (Table 10)

Median sale price for single family and condominium resales in Honolulu both continued to increase in the third quarter of 2002 over the third quarter of 2001. Single family median value was up 12.4% to \$345,000 and the median Honolulu condo price was up 15.7% to \$155,000. The number of single family units resold increased by 11.2% while the number of condo unit resales was up 29.8%.

Wage and salary jobs in the construction industry increased statewide in the third quarter compared to 2001. Construction jobs were up 4.9% from the third quarter of 2001 to the third quarter of 2002. (Table 1) Construction jobs continued to grow in all counties: Hawaii County (9.7%), Kauai County (9.5%), Maui County (6.9%), and the City and County of Honolulu (3.0%).

In the third quarter of 2002, the Honolulu Construction Cost Index for Single Family Residences increased by 5.0% over the third quarter of 2001. The comparable index for high-rise buildings rose by 3.7%.

Table 9

**ESTIMATED VALUE OF COMPLETED CONSTRUCTION, NEW PRIVATE BUILDING AUTHORIZATIONS, AND GOVERNMENT CONTRACTS AWARDED
(in millions of dollars and percentage change from the previous period)**

Year	Contracting Tax Base ¹⁾		Private Building Authorizations				Additions/Alterations		Govt. Contracts Awarded			
		%	Private Authorizations	%	Residential	%	Commercial Industrial ²⁾	%		%		
1992	4,012.7	-7.4	1,751.9	-18.6	811.1	-32.0	532.3	-4.3	408.5	1.2	1,159.1	58.9
1993	3,803.6	-5.2	1,505.4	-14.1	742.1	-8.5	308.0	-42.1	455.3	11.5	651.8	-43.8
1994	3,322.3	-12.7	1,612.9	7.1	849.3	14.4	370.3	20.2	393.4	-13.6	693.0	6.3
1995	3,133.5	-5.7	1,531.3	-5.1	745.5	-12.2	368.3	-0.5	417.5	6.1	490.2	-29.3
1996	3,285.1	4.8	1,117.8	-27.0	487.0	-34.7	252.8	-31.4	378.0	-9.5	885.5	80.6
1997	2,944.4	-10.4	1,179.2	5.4	542.5	11.4	264.5	4.4	372.2	-1.5	615.6	-30.5
1998	3,016.0	2.4	1,054.3	-10.5	485.5	-10.5	205.6	-22.1	363.2	-2.4	685.5	11.4
1999	2,991.2	-0.8	1,320.2	25.2	628.8	29.5	306.2	48.9	385.3	6.1	584.8	-14.7
2000 ³⁾	3,613.5	20.8	1,512.6	14.6	800.1	27.2	246.2	-19.6	466.2	21.0	810.9	38.7
2001 ⁴⁾	3,766.4	4.2	1,585.7	4.8	882.4	10.3	329.1	33.7	374.2	-19.7	715.7	-11.7
2002 ⁵⁾	1,213.7	35.9	497.6	18.2	346.6	35.3	47.2	-30.9	103.8 ³⁾	-7.7	255.7	126.1

- 1) Category formerly called "Value of Construction Completed"
- 2) Includes hotels.
- 3) Kauai County data for November consist of residential data only.
- 4) Kauai data available for residential only.
- 5) As of third quarter 2002 – latest data available.

Source: Hawaii State Department of Taxation; F.W. Dodge; County building departments; First Hawaiian Bank, Building Industry, and tabulation by Hawaii State Department of Business, Economic Development & Tourism.

Table 10

**ESTIMATED VALUE OF PRIVATE BUILDING CONSTRUCTION AUTHORIZATIONS, BY COUNTY
(in thousands of dollars and percentage change from the previous year)**

Year	State		City & County of Honolulu		Hawaii County		Kauai County		Maui County	
		%		%		%		%		%
1992	1,751,871	-18.6	1,060,700	-27.5	379,158	2.6	111,098	-6.3	200,916	-0.1
1993	1,496,486	-14.6	959,041	-9.6	248,236	-34.5	86,032	-22.6	203,177	1.1
1994	1,612,899	7.8	1,073,264	11.9	181,059	-27.1	164,681	91.4	193,894	-4.6
1995	1,531,317	-5.1	980,703	-8.6	267,108	47.5	78,918	-52.1	204,588	5.5
1996	1,117,760	-27.0	698,697	-28.8	171,017	-36.0	101,981	29.2	146,065	-28.6
1997	1,179,182	5.5	772,825	10.6	155,776	-8.9	97,808	-4.1	152,773	4.6
1998	1,054,281	-10.6	624,227	-19.2	178,220	14.4	88,196	-9.8	163,640	7.1
1999	1,320,218	25.2	706,358	13.2	243,852	36.8	140,846	59.7	229,162	40.0
2000 ¹⁾	1,512,601	14.6	694,223	-1.7	321,704	31.9	141,313	0.3	355,360	55.1
2001	1,585,739	4.8	682,660	-1.7	380,248	18.2	210,094	48.7	312,738	-12.0
2002 ²⁾	497,553	18.2	250,254	42.3	148,128	8.7	29,272 ³⁾	-20.1	69,900	-3.2

- 1) Kauai County data for November consist of residential data only.
 - 2) Third quarter 2002 – latest data available.
 - 3) Consist of residential data only; therefore growth rate computed using available data.
- Source: County Building Permits.

APPENDIX D

**AUDITED FINANCIAL STATEMENTS OF THE HIGHWAYS DIVISION FOR FISCAL YEAR ENDED
JUNE 30, 2002**

**Deloitte
& Touche**

***State of Hawaii
Department of
Transportation -
Highways Division***

***Financial Statements for the Year Ended
June 30, 2002 and Independent Auditors' Report***

**STATE OF HAWAII
DEPARTMENT OF TRANSPORTATION - HIGHWAYS DIVISION**

**TABLE OF CONTENTS
JUNE 30, 2002**

	Page
INDEPENDENT AUDITORS' REPORT	2-3
MANAGEMENT'S DISCUSSION AND ANALYSIS	4-11
FINANCIAL STATEMENTS AS OF AND FOR THE YEAR ENDED JUNE 30, 2002:	
Governmental Funds Balance Sheet / Government-wide Statement of Net Assets	12-13
Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances / Government-wide Statement of Activities	14-16
Governmental Funds Statement of Revenues and Expenditures – Budget and Actual State Highway Fund (Non-GAAP Budgetary Basis)	17
Notes to Financial Statements	18-36

INDEPENDENT AUDITORS' REPORT

The Director
Department of Transportation
State of Hawaii

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Highways Division, Department of Transportation, State of Hawaii ("Highways Division"), as of June 30, 2002 and for the year then ended, listed in the foregoing table of contents. These financial statements are the responsibility of the Highways Division's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. 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. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As discussed in Note 2 to the financial statements, the financial statements of the Highways Division are intended to present the financial position and the changes in financial position of only that portion of the governmental activities, each major fund, and the aggregate remaining fund information of the State of Hawaii that is attributable to the transactions of the Highways Division. They do not purport to, and do not, present the financial position of the State of Hawaii as of June 30, 2002, and the changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Highways Division at June 30, 2002, and the respective changes in financial position and the respective budgetary comparison for the State Highway Fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 2 to the financial statements, the Highways Division adopted the provisions of Governmental Accounting Standards Board ("GASB") Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, Statement No. 37,

Basic Financial Statements — and Management's Discussion and Analysis — for State and Local Governments: Omnibus, and Statement No. 38, Certain Financial Statement Note Disclosures, as of July 1, 2001.

The Management's Discussion and Analysis on pages 4 to 11 is not a required part of the financial statements but is supplementary information required by GASB. This supplementary information is the responsibility of the Highways Division's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 12, 2003 on our consideration of the Highways Division's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Deloitte & Touche LLP

March 12, 2003

STATE OF HAWAII

DEPARTMENT OF TRANSPORTATION - HIGHWAYS DIVISION

MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2002

The following Management's Discussion and Analysis (MD&A) of the Highways Division, Department of Transportation, State of Hawaii ("Highways Division") activities and financial performance provides the reader with an introduction and overview to the financial statements of the Highways Division for the year ended June 30, 2002. Because this is the first year in which the Highways Division implemented the provisions of the Governmental Accounting Standards Board ("GASB") Statement No. 34, this discussion and analysis provides only selected comparative information for the year ended June 30, 2001. Future reports are required to include additional comparisons. This discussion has been prepared by management and should be read in conjunction with the financial statements and the notes thereto, which follow this section.

The Territorial Highway Department was created by the Territorial Legislature on April 24, 1925 by Act 78 to qualify Hawaii for participation in the Federal-Aid Program. The purpose of the Federal-Aid Program was to ensure the development of an integrated network of highways in the United States. Congress defined that the Federal government would provide the funds for construction on a matching contribution basis while the State or its political subdivisions would administer the highway.

The Department of Transportation was created in 1959 by the Hawaii State Government Reorganization Act. In creating the new department, the legislature transferred the responsibilities of the old Highway Department to the Highways Division of the new Department of Transportation.

The mission of the Highways Division is to facilitate the rapid, safe, and economical movement of people and goods within the State by providing, maintaining, and operating land transportation facilities and support services. The major goals of the Highways Division are to plan, design, construct, and maintain highway facilities. In addition, the Highways Division, together with the Statewide Transportation Planning Office, implements innovative and diverse approaches to congestion management to increase the efficiency of the transportation system.

The Highways Division is managed by the Highways Division Administrator. Each island in the system is managed by a district manager with the exception of the Maui District, which includes the islands of Molokai and Lanai. The Staff Services Office, headed by the Administrative Services Officer, is responsible for personnel, budget, procurement, financial management, method, standards and evaluation functions of the Highways Division. Other major functional operations within the Highways Division include Landscape Services Office, Motor Vehicle Safety Office, Planning Branch, Design Branch, Rights-of-Way Branch, Materials Testing and Research Branch, Construction and Maintenance Branch, and Traffic Branch.

FINANCIAL HIGHLIGHTS

Government-Wide Financial Statements

- The assets of the Highways Division exceeded its liabilities at June 30, 2002 by \$5.969 billion. Of this amount, \$385.7 million is considered unrestricted and may be used to meet the Highways Division's ongoing obligations.
- The current year change in net assets was a decrease of \$123.5 million. This resulted from an excess of expenses over revenues of \$81.9 million and a transfer of \$41.6 million to other State departments. The excess of expenses over revenues was significantly impacted by depreciation expense of \$230.7 million.

Governmental Funds Financial Statements

- At June 30, 2002, the Highways Division's Governmental Funds reported a combined ending fund balance of \$362.3 million. The combined fund balance increased by \$44.8 million from the prior year's ending fund balance. Approximately \$86.2 million of the \$362.3 million fund balance is considered unreserved at June 30, 2002.
- The Highways Division's State Highway Fund, the major operating fund, reported an ending fund balance of \$197.4 million, of which \$89.0 million is considered unreserved. There was a \$15.8 million increase in fund balance for the year ended June 30, 2002.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the Highways Division's basic financial statements. The Highways Division's basic financial statements consist of three sections: 1) government-wide financial statements, 2) Governmental Funds financial statements, 3) notes to the financial statements. These sections are described below:

Government-Wide Financial Statements

The government-wide statements report information about the Highways Division as a whole in a manner similar to private-sector business. The statements provide both long-term and short-term information about the Highways Division's overall financial status. They are prepared using the economic resources measurement focus and the accrual basis of accounting. They take into account all revenues and expenses connected with the fiscal year, regardless of when cash is received or paid. The government-wide financial statements include the following two statements:

1. The *Statement of Net Assets* presents all of the Highways Division's assets and liabilities, with the difference between the two reported as "net assets." Over time, increases or decreases in the Highways Division's net assets are an indicator of whether its financial health is improving or deteriorating.
2. The *Statement of Activities* presents information showing how the Highways Division's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in this statement for some items that will not result in cash flows until future fiscal periods (such as certain receivables and earned, but unused compensatory and vacation leave).

The Highways Division's activities are considered governmental activities, and are primarily funded by taxes and intergovernmental revenues.

The government-wide financial statements can be found to the right of the "Adjustments" column, immediately following the Governmental Funds financial statements on pages 12 to 16 of this report.

Governmental Funds Financial Statements

A *fund* is a grouping of related accounts that are used to maintain control over resources that have been segregated for specific activities or objectives. The Highways Division, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All funds of the Highways Division are considered Governmental Funds.

The Governmental Funds financial statements focus on near-term inflows and outflows of *spendable resources*, as well as on the *balances of spendable resources* available at the end of the fiscal year. Governmental fund financials are prepared using the current financial resources measurement focus and the modified-accrual basis of accounting. These statements provide a detailed short-term view of the Highways Division's finances that assist in determining whether there will be adequate financial resources available to meet the current needs of the Highways Division.

Because the focus of Governmental Funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for Governmental Funds with similar information presented in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the Highways Division's near-term financing decisions. A reconciliation to facilitate this comparison between Governmental Funds financial statements and government-wide financial statements is included on pages 30 through 31 of this report (see Note 11).

The Highways Division has three Governmental Funds, all of which are considered major funds for presentation purposes. That is, each major fund is presented in a separate column in the Governmental Funds balance sheet and in the Governmental Funds statement of revenues, expenditures, and changes in fund balances. The Highways Division's three Governmental Funds are – the State Highway Fund (a Special Revenue Fund), the Debt Service Fund, and the Capital Projects Fund.

The basic Governmental Funds financial statements can be found to the left of the "Adjustments" column, immediately preceding the government-wide financial statements on pages 12 through 16 of this report.

Statement of Revenues and Expenditures – Budget and Actual – State Highway Fund (Non-GAAP Budgetary Basis)

The Governmental Funds financial statements are followed by a budgetary comparison schedule, which includes a reconciliation between the actual State Highway Fund revenues and expenditures on the budgetary basis compared to the State Highway Fund revenues and expenditures prepared for budgetary purposes.

The Statement of Revenues and Expenditures – Budget and Actual – State Highway Fund (Non-GAAP Budgetary Basis) can be found on page 17 of this report.

Notes to the Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and the Governmental Funds financial statements. The notes to the financial statements can be found on pages 18 through 36 of this report.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Statement of Net Assets

As noted earlier, net assets may serve over time as a useful indicator of the Highways Division's financial position. The Highways Division's assets exceeded liabilities by \$5.969 billion at June 30 2002.

ASSETS	
Current and other assets	\$ 449,449,304
Capital assets, net	<u>5,892,873,882</u>
Total assets	<u>\$ 6,342,323,186</u>
LIABILITIES	
Current liabilities	\$ 83,322,486
Long-term liabilities	<u>289,437,694</u>
Total liabilities	372,760,180
NET ASSETS	
Invested in capital assets, net of related debt	5,575,848,999
Restricted	8,000,000
Unrestricted	<u>385,714,007</u>
Total net assets	<u>5,969,563,006</u>
Total liabilities and net assets	<u>\$ 6,342,323,186</u>

The largest portion of the Highways Division's net assets (93.4 percent) reflects its investment in capital assets (e.g., land and land improvements, buildings, vehicles and equipment, and infrastructure), less any related debt used to acquire those assets that is still outstanding. The Highways Division uses these capital assets to provide services to citizens; therefore, these assets are not available for future spending. Although the Highways Division's investment in capital assets is reported net of related debt, it should be noted that the resources needed to repay the debt must be provided from other sources, since capital assets themselves cannot be used to liquidate these liabilities.

An additional portion of the Highways Division's net assets (0.1 percent) represents resources that are subject to restrictions as to how they may be used. This primarily relates to net assets reserved for the payment of the Highways Division's revenue bond debt service. The remaining balance of unrestricted net assets (\$385.7 million) may be used to meet the Highways Division's on-going obligations to citizens and creditors.

Statement of Activities

The Highways Division's net assets decreased by \$123.5 million. The following condensed financial information was derived from the government-wide Statement of Activities and reflects how the Highways Division's net assets changed during the year.

EXPENSES

Program expenses:

Operations and maintenance	\$ 79,395,012
Administration of Highways Division	15,153,856
Surcharge on gross receipts	7,187,140
Motor Vehicle Safety Office	6,869,550
Capital projects	37,749,712
Depreciation expense	230,705,793
Debt service/interest expense	13,386,681
Loss on disposal	<u>376,162</u>

Total expenses 390,823,906

REVENUES

Program revenues:

Charges for services	23,859,404
Operating grants and contributions	25,820,089
Capital grants and contributions	<u>109,389,357</u>

Total program revenues 159,068,850

General revenues:

Taxes	137,720,412
Interest income	11,439,160
Other	<u>688,192</u>

Total general revenues 149,847,764

Total revenues 308,916,614

DECREASE IN NET ASSETS BEFORE TRANSFERS (81,907,292)

TRANSFERS (41,597,149)

DECREASE IN NET ASSETS (123,504,441)

BEGINNING NET ASSETS:

As previously reported	316,870,524
Prior period adjustment	<u>5,776,196,923</u>

As restated 6,093,067,447

ENDING NET ASSETS \$ 5,969,563,006

Approximately 51 percent of the total revenues were derived from program revenues, which comprise charges for services as well as operating and capital grants, primarily from the federal government. The largest component of program revenues (69 percent) resulted from capital grants and

contributions from the Federal Highway Administration for the construction of roads and other infrastructure.

The remaining 49 percent of the revenues were considered general revenues and comprise primarily taxes and interest earnings. Of this amount, taxes represented 92 percent of the total.

FINANCIAL ANALYSIS OF THE HIGHWAYS DIVISION'S GOVERNMENTAL FUNDS

As noted earlier, the Highways Division uses fund accounting to ensure and demonstrate compliance with finance-related requirements.

The focus of the Highways Division's Governmental Funds is to provide information on near-term inflows, outflows, and balances of *spendable* resources. Such information is useful in assessing the Highways Division's financing requirements. In particular, the unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

At June 30, 2002, the Highways Division's Governmental Funds reported combined ending fund balances of \$362.3 million, an increase of \$44.5 million in comparison with the prior year. Approximately \$86.3 million of this amount constitutes *unreserved fund balance*, which is available for spending in the coming year. The remainder of fund balance is *reserved* to indicate that it is not available for new spending because it has already been committed to liquidate contracts and purchase orders of the prior period.

The *State Highway Fund* ("SHF") is the major operating fund of the Highways Division. The State imposes taxes, fees and charges relating to the operation and use of motor vehicles on the public highways of the State. These funds are deposited into the State Highway Fund established under Section 248-8, HRS. Moneys deposited in the SHF are used for acquisition, planning, design, construction, operation, repair and maintenance of the State Highway System.

The current taxes, fees and charges deposited to the SHF consist of: (1) the highway fuel taxes; (2) vehicle registration fees; (3) the vehicle weight tax; and (4) the rental motor vehicle and tour vehicle surcharge taxes. Together, these taxes, fees and charges accounted for most of the receipts of the State Highway Fund in the year ended June 30, 2002. Other sources of revenues include interest earnings on moneys previously credited to the SHF, vehicle weight tax penalties, certain rental income from State Highway System properties, passenger motor vehicle inspection charges, overweight permits, sales of surplus lands, commercial license fees and other miscellaneous revenues.

At June 30, 2002, the total fund balance of the SHF was \$197.4 million, of which \$89.0 million was unreserved. As a measure of the SHF's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures (including transfers out). Unreserved fund balance represents 47.9 percent of total fund expenditures (including transfers out), while total fund balance represents 106.2 percent of the same amount.

The fund balance of the Highways Division's SHF increased by \$15.8 million in the current year as compared to a \$34.9 million increase in the prior year. During the current year, the Highways Division incurred less expenditures, but also generated less revenues. The excess of revenues over expenditures before transfers remained virtually flat from the prior year at \$84.6 million in the current year as compared to \$84.1 million in the prior year. Transfers out however, increased substantially in the current year, due primarily to the transfer of unspent funds back to the Airports Division.

The *Debt Service Fund* (“DSF”) is used to track the revenue bond debt service for the Highways Division. Debt service requirements are transferred from the State Highway Fund. Increases in debt service expense from \$18 million in fiscal year 2001 to \$21.5 million in fiscal year 2002 are attributable to additional debt service requirements due to the current year issuance of the 2001 Series Revenue Bonds in the amount of \$70 million.

The *Capital Projects Fund* (“CPF”) accounts for the Highways Division’s capital improvements program. At June 30, 2002, the CPF had a total fund balance of \$164.9 million, including an unreserved fund deficit of \$2.7 million. The fund balance of the CPF increased by \$29.0 million in fiscal year 2002 as compared to an increase of \$12.7 million in the prior year. The change from the prior year was due primarily to increased construction in the current year, which was offset by the issuance of revenue bonds in the current year.

STATE HIGHWAY FUND BUDGETARY HIGHLIGHTS

The final amended State Highway Fund budget had total appropriations of approximately \$1.4 million more than the original budget. The total original appropriations, were \$169.2 million, while the final appropriations were \$170.6 million. There were no significant fluctuations between the original and final appropriations.

Revenues on the budgetary actual basis exceeded the final budget by \$26.3 million primarily due to the receipt of approximately \$22.5 million from the settlement of a lawsuit against certain gas and oil companies. Such amounts were not budgeted for. Of this amount, the Highways Division was allowed to retain \$0.5 million and remitted the balance of \$22 million to the State of Hawaii.

Expenditures on the budgetary actual basis were \$22.2 million lower than the final budgeted amounts. The difference was due primarily to significant repairs and maintenance work which was budgeted for being deferred into future periods.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

The Highways Division’s investment in capital assets as of June 30, 2002 amounts to \$5.893 billion (net of accumulated depreciation). This investment in capital assets includes land and land improvements, buildings and building improvements, vehicles and equipment, infrastructure assets and construction in progress. Infrastructure assets consist of land, roadways, tunnels and bridges, and miscellaneous roadway components.

During the fiscal year 2002, the Highways Division’s buildings and improvements increased by \$3.2 million, or 54.0 percent, from the prior year. This was primarily attributable to the completion of the Oahu District warehouse that accounted for \$1.9 million of the increase. The remaining increase was due to various improvements made to the Highways Division’s buildings.

Effective July 1, 2001, the Highways Division implemented GASB Statement No. 34 which required the capitalization of all infrastructure assets at their estimated historical cost less accumulated depreciation. The implementation of GASB 34 resulted in the prior period adjustment of \$6 billion to record the infrastructure assets, net of accumulated depreciation. The balance of such infrastructure assets was \$5.877 billion, net of accumulated depreciation, at June 30, 2002.

At June 30, 2002, the Highways Division had \$167 million in contracts encumbered in the Capital Projects Fund. Such amounts represent the balance of unliquidated contracts for work to be performed in the future.

Additional information on the Highways Division's capital assets can be found in Note 7 to the attached financial statements.

Long-Term Debt

At June 30, 2002, the Highways Division had \$287.3 million in outstanding long-term debt. This consisted of revenue bonds payable in the amount of \$284.6 million and unamortized revenue bond premiums of \$2.7 million.

Total long-term debt outstanding as of June 30, 2002 increased by \$65.6 million, from the prior year. This is primarily attributable to the issuance of the Series 2001 Revenue Bonds in the amount of \$70 million. These bonds were issued at a \$2.7 million premium which was deferred and will be amortized over the life bond using the effective interest rate.

The Highways Division's revenue bond rating by Moody's Investors Service, Inc., Standard & Poor's Corporation, and Fitch IBCA, Inc. are "Aaa", "AAA" and "AAA", respectively. Moody's Investors Service, Standard & Poor's Corporation, and Fitch IBCA, Inc. have also assigned underlying ratings of "Aa3", "AA" and "AA-", respectively, to all of the Highways Division's revenue bonds.

Bonds which are rated "Aaa" by Moody's Investors Service are judged to be of the best quality. They carry the smallest degree of investment risk and are generally referred to as "gilt edged." Interest payments are protected by a large or by an exceptionally stable margin and principal is secure. While the various protective elements are likely to change, such changes as can be visualized are most unlikely to impair the fundamentally strong position of such issues.

Generally, a rating agency bases its rating on the information and materials furnished to it and on investigations, studies and assumptions of its own. There is no assurance that either of such ratings will continue for any given period of time or that such ratings will not be revised downward, suspended or withdrawn entirely by the rating agencies if, in the judgment of such rating agencies, circumstances so warrant. The State undertakes no responsibility to oppose any such revision, suspension or withdrawal.

REQUEST FOR INFORMATION

This financial report is designed to provide a general overview of the Highways Division's finances for all interested parties. Questions concerning any of the information provided in this report or requests for additional information should be addressed to Gerald Dang, State of Hawaii, Department of Transportation, Highways Division, 869 Punchbowl Street, Honolulu, Hawaii, 96813.

STATE OF HAWAII, DEPARTMENT OF TRANSPORTATION, HIGHWAYS DIVISION

**GOVERNMENTAL FUNDS BALANCE SHEET / GOVERNMENT-WIDE STATEMENT OF NET ASSETS
JUNE 30, 2002**

ASSETS	Governmental Funds			Adjustments (Note 11)	Government- wide Statement of Net Assets
	State Highway Fund	Debt Service Fund	Capital Projects Fund		
Cash with Director of Finance, State of Hawaii	\$ 201,163,003		\$ 194,014,897		\$ 395,177,900
Receivables, net of allowance for doubtful accounts:					
Due from U.S. Government (Note 5)	5,427,997		9,240,050	\$ 6,573,641	21,241,688
Due from Capital Projects Fund	12,059,741			(12,059,741)	
Due from City and Counties	5,137,406				5,137,406
Due from other State Agencies	1,396,942				1,396,942
Land parcels held for sale	681,300				681,300
Prepaid expenses	1,733,250		200,000		1,933,250
Restricted cash and cash equivalents:					
Revenue bond debt service (Note 9)		\$ 15,269,995			15,269,995
Security deposits	7,916,224				7,916,224
Bond issue costs, net of accumulated amortization (Note 9)				694,599	694,599
Capital assets, net of accumulated depreciation (Note 7)				<u>5,892,873,882</u>	<u>5,892,873,882</u>
TOTAL	<u>\$ 235,515,863</u>	<u>\$ 15,269,995</u>	<u>\$ 203,454,947</u>	<u>\$ 5,888,082,381</u>	<u>\$ 6,342,323,186</u>

STATE OF HAWAII, DEPARTMENT OF TRANSPORTATION, HIGHWAYS DIVISION
GOVERNMENTAL FUNDS BALANCE SHEET / GOVERNMENT-WIDE STATEMENT OF NET ASSETS (Continued)
JUNE 30, 2002

	Governmental Funds			Total	Adjustments (Note 11)	Government- wide Statement of Net Assets
	State Highway Fund	Debt Service Fund	Capital Projects Fund			
LIABILITIES AND FUND BALANCES / NET ASSETS						
LIABILITIES:						
Accounts payable	\$ 1,998,476			\$ 2,357,290		\$ 2,357,290
Accrued payroll	1,905,895			1,905,895		1,905,895
Contracts payable:						
Current portion	1,863,197		19,373,616	21,236,813		21,236,813
Retained percentage	2,409,291		6,750,059	9,159,350		9,159,350
Payable from restricted assets:						
Matured bonds and interest payable (Notes 8 and 9)		\$15,269,995		15,269,995		15,269,995
Security deposits	7,916,224			7,916,224		7,916,224
Due to State Highway Fund			12,059,741	12,059,741	\$ (12,059,741)	
Due to State of Hawaii	22,000,000			22,000,000		22,000,000
Other liabilities	15,300			15,300		15,300
Long-term liabilities (Note 8):						
Due within one year:						
Workers' compensation payable					897,303	897,303
Accrued vacation payable					2,564,316	2,564,316
Due after one year:						
Workers' compensation payable					3,733,744	3,733,744
Accrued vacation payable					6,380,631	6,380,631
Revenue bonds payable (Notes 8 and 9)					279,323,319	279,323,319
Total liabilities	38,108,383	15,269,995	38,542,230	91,920,608	280,839,572	372,760,180
FUND BALANCES / NET ASSETS (Note 11):						
Fund Balances:						
Reserved for encumbrances	105,997,108		167,432,723	273,429,831	(273,429,831)	
Reserved for prepaid expenses	1,733,250		200,000	1,933,250	(1,933,250)	
Reserved for land parcels held for sale	681,300			681,300	(681,300)	
Unreserved, reported in State Highway Fund	88,995,822			88,995,822	(88,995,822)	
Unreserved, reported in Capital Projects Fund			(2,720,006)	(2,720,006)	2,720,006	
Total fund balances	197,407,480		164,912,717	362,320,197	(362,320,197)	
Net Assets:						
Invested in capital assets, net of related debt					5,575,848,999	5,575,848,999
Restricted for revenue bonds					8,000,000	8,000,000
Unrestricted					385,714,007	385,714,007
Total net assets					5,969,563,006	5,969,563,006
Total liabilities and fund balance / net assets	\$ 235,515,863	\$ 15,269,995	\$ 203,454,947	\$ 454,240,805	\$ 5,888,082,381	\$ 6,342,323,186

See notes to financial statements.

**STATE OF HAWAII, DEPARTMENT OF TRANSPORTATION,
HIGHWAYS DIVISION**

**GOVERNMENTAL FUNDS STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES / GOVERNMENT-WIDE
STATEMENT OF ACTIVITIES
YEAR ENDED JUNE 30, 2002**

	Governmental Funds			Adjustments (Note 11)	Government- wide Statement of Activities
	State Highway Fund	Debt Service Fund	Capital Projects Fund		
EXPENDITURES / EXPENSES:					
Operations and maintenance:					
Oahu highways and services	\$ 38,974,924			\$ 38,974,924	\$ 38,974,924
Hawaii highways and services	16,470,004			16,470,004	16,470,004
Maui highways and services	13,593,649			13,593,649	13,593,649
Kauai highways and services	7,762,147			7,762,147	7,762,147
Molokai highways and services	2,347,983			2,347,983	2,347,983
Lanai highways and services	246,305			246,305	246,305
Administration of Highways Division	20,791,723			20,791,723	15,153,856
Surcharge on gross receipts (Note 14)	7,187,140			7,187,140	7,187,140
Motor Vehicle Safety Office	6,869,550			6,869,550	6,869,550
Capital projects		\$ 153,068,645		153,068,645	37,749,712
Depreciation expense					230,705,793
Debt service:					
Principal payment (Note 9)		\$ 8,000,000		8,000,000	(8,000,000)
Interest expense (Note 9)		13,452,974		13,452,974	(66,293)
Loss on disposal					376,162
Total expenditures / expenses	114,243,425	21,452,974	153,068,645	288,765,044	390,823,906
PROGRAM REVENUES:					
Charges for services:					
Vehicle registration fees (Note 4)	19,490,560			19,490,560	19,490,560
Other fees and permits (Note 4)	2,718,931		658,096	3,377,027	3,377,027
Rentals	991,817			991,817	991,817
Operating grants and contributions (Note 5)	25,820,089			25,820,089	25,820,089
Capital grants and contributions (Note 5)			102,815,716	102,815,716	109,389,357
Total program revenues	49,021,397		103,473,812	152,495,209	159,068,850
NET PROGRAM EXPENSE (Forward)	(65,222,028)	(21,452,974)	(49,594,833)	(136,269,835)	(231,755,056)

**STATE OF HAWAII, DEPARTMENT OF TRANSPORTATION,
HIGHWAYS DIVISION**

**GOVERNMENTAL FUNDS STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES / GOVERNMENT-WIDE
STATEMENT OF ACTIVITIES (Continued)
YEAR ENDED JUNE 30, 2002**

	Governmental Funds			Adjustments (Note 11)	Government- wide Statement of Activities
	State Highway Fund	Debt Service Fund	Capital Projects Fund		
NET PROGRAM EXPENSE (Forwarded)	\$ (65,222,028)	\$ (21,452,974)	\$ (49,594,833)	\$ (95,485,221)	\$ (231,755,056)
GENERAL REVENUES:					
Taxes (Note 4):					
Fuel taxes	73,045,996			73,045,996	73,045,996
Rental motor and four vehicle surcharge taxes	36,054,296			36,054,296	36,054,296
Vehicle weight taxes	28,620,120			28,620,120	28,620,120
Interest income	11,439,160			11,439,160	11,439,160
Non-imposed fringe benefits (Note 6)	181,520			181,520	181,520
Other	506,672			506,672	506,672
Total general revenues	149,847,764			149,847,764	149,847,764
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	84,625,736	(21,452,974)	(49,594,833)	13,577,929	(81,907,292)
OTHER FINANCING SOURCES (USES) (Note 10):					
Transfers in	2,787,593	21,452,974	78,586,641	102,827,208	(102,827,208)
Transfers out	(71,636,764)			(71,636,764)	71,636,764
Total other financing sources (uses)	(68,849,171)	21,452,974	78,586,641	31,190,444	(31,190,444)
EXCESS (DEFICIENCY) OF REVENUES AND OTHER FINANCING SOURCES OVER EXPENDITURES AND OTHER FINANCING USES (Note 11)	15,776,565	-	28,991,808	44,768,373	(81,907,292)
TRANSFERS OUT (Note 10)					(41,597,149)
CHANGE IN NET ASSETS (Note 11) (Forward)					(123,504,441)

**STATE OF HAWAII, DEPARTMENT OF TRANSPORTATION,
HIGHWAYS DIVISION**

**GOVERNMENTAL FUNDS STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES / GOVERNMENT-WIDE
STATEMENT OF ACTIVITIES (Continued)
YEAR ENDED JUNE 30, 2002**

	Governmental Funds					
	State Highway Fund	Debt Service Fund	Capital Projects Fund	Total	Adjustments (Note 12)	Government- wide Statement of Activities
CHANGE IN NET ASSETS (Forwarded)						\$ (123,504,441)
FUND BALANCE / NET ASSETS (Note 12):						
Beginning of year, as previously reported	168,209,824		148,660,700	316,870,524		316,870,524
Prior year adjustment	<u>13,421,091</u>		<u>(12,739,791)</u>	<u>681,300</u>	<u>5,775,515.623</u>	<u>5,776,196,923</u>
Beginning of year, restated	<u>181,630,915</u>		<u>135,920,909</u>	<u>317,551,824</u>	<u>5,775,515.623</u>	<u>6,093,067,447</u>
End of year	<u>\$ 197,407,480</u>	<u>\$ -</u>	<u>\$ 164,912,717</u>	<u>\$ 362,320,197</u>	<u>\$ 5,607,242,809</u>	<u>\$ 5,969,563,006</u>

See notes to financial statements.

**STATE OF HAWAII, DEPARTMENT OF TRANSPORTATION,
HIGHWAYS DIVISION**

**GOVERNMENTAL FUNDS STATEMENT OF REVENUES AND EXPENDITURES--
BUDGET AND ACTUAL--STATE HIGHWAY FUND (NON-GAAP BUDGETARY BASIS)
YEAR ENDED JUNE 30, 2002**

	Original Budget	Final Budget	Budgetary Actual	Variance
REVENUES:				
Fuel taxes	\$ 70,664,861	\$ 70,476,508	\$ 73,045,996	\$ 2,569,488
Vehicle weight taxes	24,585,729	23,412,331	24,507,850	1,095,519
Rental motor and tour vehicle surcharge tax	38,201,044	34,522,051	36,054,296	1,532,245
Vehicle registration fees	17,647,066	16,904,765	17,461,165	556,400
Interest income	9,000,000	13,900,000	11,452,602	(2,447,398)
Enforcement fee	1,322,777	1,252,799	1,329,998	77,199
Vehicle registration penalties	1,203,450	911,239	935,616	24,377
Commercial drivers license fee	366,487	366,487	313,138	(53,349)
Rentals	850,000	850,000	991,817	141,817
Other	<u>271,000</u>	<u>255,619</u>	<u>23,145,401</u>	<u>22,889,782</u>
Total revenues	164,112,414	162,851,799	189,237,879	26,386,080
EXPENDITURES:				
Operations and maintenance:				
Oahu highways and services	43,968,549	44,353,657	35,090,616	9,263,041
Hawaii highways and services	20,024,067	20,200,734	15,193,225	5,007,509
Maui highways and services	13,544,792	13,653,881	12,652,204	1,001,677
Kauai highways and services	9,433,545	9,507,417	8,525,306	982,111
Molokai highways and services	3,328,468	3,292,758	3,108,395	184,363
Lanai highways and services	825,231	881,084	755,410	125,674
Administration of Highways				
Division including debt service (Note 10)	65,694,172	65,940,055	60,069,019	5,871,036
State of Hawaii surcharge on gross receipts	5,869,414	5,869,414	7,187,140	(1,317,726)
Motor Vehicle Safety Office	<u>6,546,383</u>	<u>6,933,976</u>	<u>5,809,569</u>	<u>1,124,407</u>
Total expenditures	<u>169,234,621</u>	<u>170,632,976</u>	<u>148,390,884</u>	<u>22,242,092</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	<u>\$ (5,122,207)</u>	<u>\$ (7,781,177)</u>	<u>\$ 40,846,995</u>	<u>\$ 48,628,172</u>

See notes to financial statements.

STATE OF HAWAII

DEPARTMENT OF TRANSPORTATION - HIGHWAYS DIVISION

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED JUNE 30, 2002

1. REPORTING ENTITY

Act 1, Session Laws of Hawaii ("SLH"), Second Special Session 1959, the Hawaii State Government Reorganization Act of 1959 ("Act"), established the Department of Transportation ("Department") whose function is to establish, maintain, and operate transportation facilities of the State of Hawaii ("State"), including highways, airports, harbors and such other transportation facilities and activities as may be authorized by law. The Department's activities are carried out through three primary operating divisions: Airports, Harbors and Highways. Through the Highways Division, the Department has general supervision of the management and maintenance of the State Highways System and the location, design, and construction of new highways and facilities. The Highways Division provides supervision to assure completion of State highway contracts in accordance with plans and specifications.

Taxes, fees, and charges authorized and collected relating to the operation and use of motor vehicles on public highways of the State are deposited into the State Highway Fund, and expenditures for purposes of the Act are made from the State Highway Fund.

The State Highway Fund also includes the Motor Vehicle Safety Office ("MVSO"). MVSO was originally established as the Highway Safety Coordinator's Office to implement the 1967 Hawaii Highway Safety Act. It was reorganized by the 1977 State Legislature to encompass the additional duty of the safety of operations of heavy motor vehicles. The MVSO is assigned as a staff office under the Highways Division.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Financial Statement Presentation and Basis of Accounting - In June 1999, the Government Accounting Standards Board ("GASB") issued Statement No. 34, *Basic Financial Statements -- and Management's Discussion and Analysis -- for State and Local Governments*. Statement No. 34, as amended, establishes financial reporting standards for state and local governments. Among its requirements, Statement No. 34 requires governmental entities to report certain supplementary information, including management's discussion and analysis of the entity's financial performance. Statement No. 34 also requires that governments should report all capital assets, including infrastructure assets, in a government-wide statement of net assets, and should report depreciation expense in the statement of activities. The Highways Division adopted the provisions of Statement No. 34 effective July 1, 2001.

In conjunction with the implementation of GASB Statement No. 34, the Highways Division has also implemented the following GASB Statements in the current fiscal year: Statement No. 37, *Basic Financial Statements -- and Management's Discussion and Analysis -- for State and Local Governments: Omnibus*, and Statement No. 38, *Certain Financial Statement Note Disclosures*. Statement No. 37 clarifies requirements set forth in Statement No. 34 related to the management's

discussion and analysis, the modified approach, program revenue classifications, and major fund criteria. Statement No. 38 establishes and modifies disclosure requirements related to the summary of significant accounting policies, actions taken to address violations of significant finance-related legal and contractual provisions, debt and lease obligations, short-term debt, disaggregation of receivable and payable balances, and interfund balances and transfers.

Implementation of these GASB statements resulted in a change in beginning fund balance as reported in the governmental fund financial statements on the modified accrual basis of accounting of \$13,421,091 and \$(12,739,791) in the State Highway Fund and Capital Projects Fund, respectively. Implementation of these GASB statements also resulted in a \$5,776,196,123 increase in beginning net assets for the government-wide financial statements. See Note 12 for a description of the adjustments.

The Highways Division's financial statements are prepared in conformity with generally accepted accounting principles as prescribed by GASB.

Governmental Funds Financial Statements - The accounts of the Highways Division are organized on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues, and expenditures. Governmental resources are allocated to and accounted for in individual funds based upon the purposes for which they are to be spent and the means by which spending activities are controlled. For financial reporting purposes, the Highways Division includes all funds that are controlled by or dependent on the Highways Division's administrative head. Control by or dependence on the Highways Division was determined on the basis of statutory authority and moneys flowing through the Highways Division to each fund or account.

Governmental Funds are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recognized when measurable and available. The Highways Division considers all revenues reported in the Governmental Funds to be available if the revenues are collected within 90 days after year-end. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, claims and judgments, and compensated absences, which are recognized as expenditures when payment is due. General capital asset acquisitions are reported as expenditures in Governmental Funds. Proceeds of general long-term debt are reported as other financing sources.

A description of the funds administered by the Highways Division and included in the Governmental Funds financial statements follows:

State Highway Fund: The State Highway Fund generally accounts for revenues and expenditures for highway operations and maintenance and administration.

The State Highway Fund is a special revenue fund of the State established by Section 248-8, Hawaii Revised Statutes ("HRS"). All fuel taxes collected under Section 243-4, HRS except county fuel taxes, aviation fuel taxes, and taxes on fuel sold for use by small boats are deposited in the State Highway Fund.

Section 248-9, HRS provides that moneys in the State Highway Fund shall be expendable by the Department of Transportation for the design, construction, reconstruction, repair and maintenance, and for acquisition of rights-of-way for public highways included in the State Highways System established under Section 264-41, HRS.

Debt Service Fund: The Debt Service Fund accounts for the Highways Division's financial resources obtained and used for the payment of principal and interest on State of Hawaii Highway Revenue Bonds.

Capital Projects Fund: The Capital Projects Fund accounts for the Highways Division's construction projects and the related sources of financing.

The accompanying financial statements include highway projects authorized by legislative acts (SLH) through June 30, 2002.

Government-Wide Financial Statements - The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Statement of Net Assets - The statement of net assets includes all capital assets and long-term liabilities that are excluded from the Governmental Funds financial statements. The net assets are reported in three categories: invested in capital assets, net of related debt; restricted; and unrestricted.

Statement of Activities - The statement of activities reports expenses and revenues in a format that focuses on the cost of the Highways Division's program. Revenues are classified as either program revenues or general revenues. Program revenues include charges paid by users, as well as capital or operating grants. Revenues that are not classified as program revenues, including all taxes, are presented as general revenues.

Cash - Cash reported in the balance sheet/statement of net assets includes cash in the State Treasury, including deposits received and held for others in the amount of \$7,916,224 at June 30, 2002. The deposits were received on the Highways Division's contracts with third parties. The Director of Finance is responsible for the safekeeping of all moneys paid into the State Treasury (cash pool).

At June 30, 2002, information relating to the insurance and collateral of cash deposits was not available since such information is determined on a statewide basis and not for individual departments or divisions. Cash deposits of the State are covered by federal deposit insurance or by collateral held either by the State Treasury or by the State's fiscal agent in the State's name.

Effective fiscal 2000, the Highways Division participates in the State Treasury Investment Pool System, pursuant to Act 199, Session Laws of Hawaii 1998. The investment pool system centralizes all phases of the investment process under the direction of the Director of Finance, thereby pooling the State's cash resources to maximize investment returns. State departments and agencies are eligible to invest all funds of qualifying appropriation accounts, eliminating their responsibility for the investment of appropriated funds. The State Treasury allocates investment earnings (interest) monthly, based on the average weighted cash balance of each account. At June 30, 2002, all of the Highways Division's restricted and unrestricted cash were deposited in the State Treasury Investment Pool System.

The HRS authorize the Director of Finance to invest in obligations of or guaranteed by the U.S. Government, obligations of the State, federally-insured savings and checking accounts, time certificates of deposit, and repurchase agreements with federally insured financial institutions. Cash and deposits with financial institutions are collateralized in accordance with State statutes.

Receivables - Receivables are reported at their gross value when earned and are reduced by the estimated portion that is expected to be uncollectible. The allowance for uncollectible accounts is based on collection history and current information regarding the credit worthiness of the tenants and others doing business with the Highways Division. When continued collection activity results in receipt of amounts previously written off, revenue is recognized for the amount collected.

Prepaid Expenses - Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid expenses in both government-wide and Governmental Funds financial statements.

Restricted Assets - Restricted assets consist of moneys and other resources, the use of which is legally restricted. Certain resources set aside for the repayment of highways system revenue bonds are classified as restricted assets on the government-wide statement of net assets as they are maintained separately. Restricted assets account for the principal and interest amounts accumulated to make debt service payments and also include security deposits from third parties.

Capital Assets - Capital assets, which include land and improvements, buildings and improvements, vehicles and equipment, and infrastructure (i.e., roads, bridges, tunnels) are reported in the government-wide statement of net assets. Such assets are recorded at cost or at estimated fair market value at the date of donation. Capital outlays are recorded as expenditures of the State Highway Fund or Capital Projects Fund in the Governmental Funds and as assets in the government-wide statement of net assets to the extent the capitalization threshold is met. Capital assets are depreciated by the straight-line method over their estimated useful lives as follows:

Class of Assets	Estimated Useful Lives	Capitalization Threshold
Land improvements	20 years	\$100,000
Buildings	45 years	100,000
Building improvements	20 years	100,000
Vehicles and equipment	5-10 years	5,000
Infrastructure	13-46 years	100,000

Disposals of assets are recorded by removing the costs and related accumulated depreciation from the accounts with a resulting gain or loss.

Repairs and maintenance, and minor replacements, renewals and betterments are charged against operations. Major replacements, renewals and betterments are capitalized.

Accrued Vacation and Compensatory Pay - The Highways Division accrues all vacation and compensatory pay at current salary rates, including additional amounts for certain salary-related expenses associated with the payment of compensated absences, in accordance with GASB Statement No. 16, *Accounting for Compensated Absences*. Vacation is earned at the rate of 168 hours per calendar year. Accumulation of such vacation is limited to 720 hours at calendar year-end and is convertible to pay upon termination of employment.

Long-Term Obligations - In the government-wide statement of net assets, long-term debt and other long-term obligations are reported as liabilities. Bond premiums and issuance costs are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the Governmental Funds financial statements, bond premiums and issuance costs are recognized during the current period. The face amount of debt and any related premium are reported as other financing sources. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

Encumbrances - The Highways Division's accounting procedures provide for the recording of commitments as encumbrances at the time contracts are awarded and executed. Purchase orders issued for materials, supplies, and services chargeable to annual appropriations for operating costs, which are outstanding at the end of the year, are also encumbered. Encumbrances are recorded as a reservation of fund balance in the Governmental Funds balance sheet. The related expenditure is reported in the period in which the liability is incurred. Encumbrances are not recognized in the government-wide statement of net assets.

Employees' Retirement System - The Highways Division's contributions to the Employees' Retirement System of the State of Hawaii (ERS) are based on the current contribution rate determined by the State Department of Budget and Finance. The Highways Division's policy is to fund its required contribution each pay period.

Risk Management - The Highways Division is exposed to various risks of loss from torts; theft of, damage to, or destruction of assets; errors or omissions; natural disasters; and injuries to employees. The Highways Division is self-insured for workers' compensation as discussed in Note 17. Liabilities related to these losses are reported when it is probable that the losses have occurred and the amount of those losses can be reasonably estimated.

Use of Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

3. BUDGETS AND BUDGETARY ACCOUNTING

State Highway Fund - In the Governmental Funds statement of revenues and expenditures--budget and actual--State Highway Fund (non-GAAP budgetary basis), amounts reflected as original and amended budgeted revenues are the official estimates as compiled by the State Department of Budget and Finance at the time of budget consideration and adoption by the State Legislature. Revenues received from federal grants-in-aid are not included in the statement of revenues and expenditures--budget and actual--State Highway Fund (non-GAAP budgetary basis) since such grants are normally reimbursements of costs incurred on approved projects.

In the case of expenditures, the original and amended budgeted amounts reflected on the Governmental Funds statement of revenues and expenditures--budget and actual--State Highway Fund (non-GAAP budgetary basis) are derived from: the Supplemental Appropriations Act of 2000 (Act 281, SLH 2000)

- authorizations for expenditures for operating purposes for the Highways Division (\$163,699,000) and the MVS0 (\$6,933,976).

Appropriations are made and expenditures are controlled at the program level reflected in the Governmental Funds statement of revenues and expenditures--budget and actual--State Highway Fund (non-GAAP budgetary basis). State Highway Fund appropriations lapse at year-end.

With reference to the Governmental Funds statement of revenues and expenditures--budget and actual--State Highway Fund (non-GAAP budgetary basis), budget and actual amounts for expenditures include encumbrances and exclude expenditures charged to prior years' appropriations and unbudgeted federally funded expenditures.

The reconciliation of the budgetary actual excess of revenues over expenditures as shown on the Governmental Funds statement of revenues and expenditures--budget and actual--State Highway Fund (non-GAAP budgetary basis) to the Governmental Funds statement of revenues, expenditures, and changes in fund balances—State Highway Fund is as follows:

Excess of revenues over expenditures, non-GAAP budgetary basis	\$ 40,846,995
Federal grants-in-aid	25,820,089
Operating transfers out to State of Hawaii for debt service	24,494,091
Other adjustments to modified accrual basis of accounting	<u>(6,535,439)</u>
Excess of revenues over expenditures, GAAP basis	<u>\$ 84,625,736</u>

Capital Projects Fund - Excess Capital Projects Fund appropriations lapse after completion of the project, which is generally two or three years subsequent to appropriation. Funds appropriated as part of a qualified federal award program do not lapse.

4. TAX AND FEE REVENUES

State Fuel Tax - The primary source of revenues for the State Highway Fund is the state tax on liquid (motor vehicle) fuel. For the year ended June 30, 2002, the tax imposed on each gallon of fuel was as follows:

Gasoline	16 cents
Diesel Fuel:	
Non-highway use	1 cent
Highway use	16 cents
Liquefied Petroleum Gas:	
Non-highway use	1 cent
Highway use	11 cents

Vehicle Weight Tax and Penalties - The vehicle weight tax was 0.75-1.25 cent per pound of net vehicle weight (depending upon the weight of the vehicle) to a maximum of \$150 per vehicle.

Rental Motor Vehicle Surcharge Tax - The rental motor vehicle surcharge tax was \$3 a day or any portion of a day that a rental motor vehicle is rented or leased.

Vehicle Registration Fee - The vehicle registration fee was \$20 per vehicle.

Tour Vehicle Surcharge Tax - The tour vehicle surcharge tax was \$65 a month for tour vehicles categorized by the Public Utilities Commission as an over seventeen-passenger carrier vehicle and \$15 a month for tour vehicles categorized as an eight to seventeen-passenger carrier vehicle.

Other Taxes and Fees - The motor carrier safety inspection fee was \$1.50 per vehicle every six months.

5. FEDERAL GRANTS-IN-AID

The Highways Division has projects in progress in which part of the funding is being provided by the Federal Highway Administration ("FHWA") through grants-in-aid. Such projects are generally accounted for in the Capital Projects and State Highway Funds. At June 30, 2002, the receivable from the U.S. Government is comprised of billed costs, pending reimbursement, as well as unbilled costs, which are eligible for reimbursement. At June 30, 2002, expenditures of approximately \$3,400,000 were not recorded as receivables and as federal grants-in-aid revenue, pending qualification for reimbursement by the Highways Division. In addition, the MVSO has projects in progress in which part of the funding is being provided through federal grants-in-aid. The grants contain various compliance requirements, which must be met by the MVSO, including a matching of the grant amounts with state and local highway safety expenditures as defined in a formula. MVSO's matching requirement is met through the expenditures of the Division of Driver Education, The Judiciary, State of Hawaii. Costs reimbursement by the FHWA and National Highway Traffic Safety Administration ("NHTSA") are subject to final audit by federal agencies. In addition, FHWA and NHTSA reserve the right to examine the Highways Division for economy, efficiency, and program results. The Highways Division's management believes that any federal aid received as of June 30, 2002 that might be required to be repaid to the FHWA or NHTSA based on federal audits would not be material to the financial position of the various funds of the Highways Division at June 30, 2002, or the results of operations of such funds for the year then ended.

6. NON-IMPOSED FRINGE BENEFITS

Payroll fringe benefit costs of employees of the Highways Divisions are assumed by the State and are not charged to the Highways Division operating funds. These costs totaling \$181,520 have been reported as revenues and expenditures.

7. CAPITAL ASSETS

Changes in capital assets during the year ended June 30, 2002 were as follows:

	Balance July 1, 2001	Additions	Deductions	Transfers	Balance June 30, 2002
Capital assets not being depreciated:					
Land	\$ 417,382,435				\$ 417,382,435
Construction in progress	61,350,283	\$ 34,592,782		\$ (8,296,307)	87,646,758
Infrastructure	<u>661,387,261</u>	<u>10,055,639</u>		<u>1,016,171</u>	<u>672,459,071</u>
Total	1,140,119,979	44,648,421		(7,280,136)	1,177,488,264
Capital assets being depreciated:					
Land improvements	235,509				235,509
Buildings and improvements	5,884,448	3,043,182		131,753	9,059,383
Vehicles and equipment	36,906,326	2,874,139	\$ (1,811,013)	906,190	38,875,642
Infrastructure	<u>7,129,508,369</u>	<u>70,905,826</u>		<u>6,242,193</u>	<u>7,206,656,388</u>
Total	7,172,534,652	76,823,147	(1,811,013)	7,280,136	7,254,826,922
Less accumulated depreciation	<u>(2,310,170,362)</u>	<u>(230,705,793)</u>	<u>1,434,851</u>		<u>(2,539,441,304)</u>
Capital assets being depreciated - net	<u>4,862,364,290</u>	<u>(153,882,646)</u>	<u>(376,162)</u>	<u>7,280,136</u>	<u>4,715,385,618</u>
Total capital assets	<u>\$ 6,002,484,269</u>	<u>\$(109,234,225)</u>	<u>\$ (376,162)</u>	<u>\$ -</u>	<u>\$ 5,892,873,882</u>

8. GENERAL LONG-TERM LIABILITIES

Changes in general long-term liabilities during the year ended June 30, 2002 were as follows:

	Balance June 30, 2001	Increase	Decrease	Balance June 30, 2002	Current	Noncurrent
Accrued workers' compensation	\$ 4,036,000	\$ 1,492,350	\$ (897,303)	\$ 4,631,047	\$ 897,303	\$ 3,733,744
Accrued vacation	8,307,646	3,224,156	(2,586,855)	8,944,947	2,564,316	6,380,631
Revenue bonds	<u>221,765,000</u>	<u>72,787,593</u>	<u>(7,229,274)</u>	<u>287,323,319</u>	<u>8,000,000</u>	<u>279,323,319</u>
	<u>\$ 234,108,646</u>	<u>\$ 77,504,099</u>	<u>\$ (10,713,432)</u>	<u>\$ 300,899,313</u>	<u>\$ 11,461,619</u>	<u>\$ 289,437,694</u>

9. REVENUE BONDS

In 1993, the Director issued the *Certificate of the Director of Transportation Providing for the Issuance of State of Hawaii Highway Revenue Bonds* ("Certificate"). Subsequent issues of revenue bonds were covered by supplemental certificates to the original 1993 Certificate.

These revenue bonds are payable solely from, and collateralized solely by, the revenues held in the State Highway Fund consisting primarily of highway fuel taxes, vehicle registration fees, vehicle weight taxes, rental motor vehicle and tour vehicle surcharge taxes, and interest earnings on moneys previously credited to the State Highway Fund. The proceeds of the revenue Bonds are used to finance certain highway capital improvement projects and other related projects for the State Highways System.

On September 1, 1993, the Highways Division issued \$75,000,000 in State of Hawaii Highway Revenue Bonds, Series 1993 ("1993 Bonds"). The 1993 Bonds bear interest at rates ranging from 2.6% to 5.0% and mature in increasing annual installments through 2013. On September 1, 1996, the Highways Division issued \$55,000,000 in State of Hawaii Highway Revenue Bonds, Series 1996 ("1996 Bonds"). The 1996 Bonds bear interest at rates ranging from 3.8% to 6.0% and mature in increasing annual installments through 2016. The 1993 Bonds maturing on and after July 1, 2004, and the 1996 Bonds maturing on and after July 1, 2006 are subject to redemption at the option of the State at prices ranging from 102% to 100% plus accrued interest.

On July 1, 1998, the Highways Division issued \$94,920,000 in State of Hawaii Highway Revenue Bonds, Series 1998 ("1998 Bonds"). The Bonds bear interest at rates ranging from 4.0% to 5.5% and mature in annual installments through 2018. The Bonds maturing on and after July 1, 2009 through July 1, 2016 are subject to redemption at the option of the State on and after July 1, 2008 at prices ranging from 101% to 100% plus accrued interest.

On October 1, 2000, the Highways Division issued \$50,000,000 in State of Hawaii Highway Revenue Bonds, Series 2000 ("2000 Bonds"). The Bonds bear interest at rates ranging from 4.4% to 5.5% and mature in annual installments through 2020. The Bonds maturing on and after July 1, 2011 through July 1, 2020 are subject to redemption at the option of the State after July 1, 2010 at a price of 100% plus accrued interest.

On October 3, 2001, the Highways Division issued \$70,000,000 in State of Hawaii Highway Revenue Bonds, Series 2001 ("2001 Bonds"). The Bonds bear interest at rates ranging from 3.8% to 5.4% and mature in annual installments through 2022. The bonds maturing on and after July 11, 2011 are subject to redemption at the option of the State at a redemption of 100% plus accrued interest. These bonds were issued at a premium of \$2,787,593 which will be amortized over the life of the bond using the effective interest method.

The following is a summary of highways system revenue bonds issued and outstanding at June 30, 2002:

Series	Interest Rate	Final Maturity Date (July 1)	Original Amount of Issue	Outstanding Amount
1993	2.6% - 5.0%	2013	\$ 75,000,000	\$ 45,350,000
1996	3.8% - 6.0%	2016	55,000,000	34,635,000
1998	4.0% - 5.5%	2018	94,920,000	85,700,000
2000	4.4% - 5.5%	2020	50,000,000	48,940,000
2001	3.8% - 5.4%	2022	<u>70,000,000</u>	<u>70,000,000</u>
			\$ 344,920,000	284,625,000
			Add unamortized premium	2,698,319
			Less current portion	<u>(8,000,000)</u>
			Noncurrent portion	<u>\$ 279,323,319</u>

The approximate maturities for revenue bonds, including interest of \$157,801,000 (debt service fund of \$7,270,000 and general long-term debt of \$150,531,000) in each of the next five years and thereafter are as follows:

	Principal	Interest	Total
Year ending June 30:			
2003	\$ 8,000,000	\$ 14,339,998	\$ 22,339,998
2004	10,635,000	13,891,905	24,526,905
2005	11,135,000	13,388,925	24,523,925
2006	11,640,000	12,862,572	24,502,572
2007	12,190,000	12,304,765	24,494,765
2008-2012	70,370,000	51,705,080	122,075,080
2013-2017	90,015,000	31,405,398	121,420,398
2018-2022	65,240,000	7,767,791	73,007,791
2023	<u>5,400,000</u>	<u>135,000</u>	<u>5,535,000</u>
Total	<u>\$ 284,625,000</u>	<u>\$ 157,801,434</u>	<u>\$ 442,426,434</u>

In 2002, \$21,452,974 was transferred from the State Highway Fund to the Debt Service Fund for repayment of Revenue Bonds principal of \$8,000,000 and interest of \$13,452,974.

10. OTHER FINANCING SOURCES AND USES / TRANSFERS

Operating transfers, accounted for in the Governmental Funds statement of revenues, expenditures, and changes in fund balances as other financing sources and uses, and on the government-wide statement of net assets as transfers are summarized as follows:

Description	Transfers In (Out)				Adjustments	Statement of Activities
	State Highway Fund	Debt Service Fund	Capital Projects Fund	Total		
Funding of highway capital projects	\$ (8,586,641)		\$ 8,586,641			
Proceeds from issuance of revenue bonds			70,000,000	\$ 70,000,000	\$ (70,000,000)	
Premiums from issuance of revenue bonds	2,787,593			2,787,593	(2,787,593)	
Reimbursement to State for debt service on general obligation bonds	(24,494,091)			(24,494,091)		\$ (24,494,091)
Funding of revenue bond debt service	(21,452,974)	\$ 21,452,974				
Transfers of funds to Airports Division	<u>(17,103,058)</u>	<u> </u>	<u> </u>	<u>(17,103,058)</u>	<u> </u>	<u>(17,103,058)</u>
	<u>\$ (68,849,171)</u>	<u>\$ 21,452,974</u>	<u>\$ 78,586,641</u>	<u>\$ 31,190,444</u>	<u>\$ (72,787,593)</u>	<u>\$ (41,597,149)</u>

Funding of Highway Capital Projects

Funding of highway capital projects by the State Highway Fund is recognized when received by the Capital Projects Fund.

Reimbursement to State for Debt Service

Allocated portions of the State's general obligation bonds have been designated by the Director of Finance, State of Hawaii, to be reimbursed from the State Highway Fund. The proceeds from these bonds are related to the above funds transferred from the State to the Highways Division for highway capital projects. These bonds are the obligations of the State and are not included in these financial statements. The amount of the Highways Division's reimbursement to the State for debt service is primarily determined by the Director of Finance, State of Hawaii.

The annual amounts required to amortize the designated portions of general obligation bonds as of June 30, 2002 are as follows:

	Principal	Interest	Total
Year ending June 30:			
2003	\$ 12,446,521	\$ 5,981,243	\$ 18,427,764
2004	9,182,553	5,417,311	14,599,864
2005	9,355,578	4,722,049	14,077,627
2006	13,251,584	4,025,540	17,277,124
2007	14,295,350	3,360,195	17,655,545
2008-2012	51,924,536	7,325,830	59,250,366
2013-2017	8,131,316	365,323	8,496,639
2018-2021	<u>83,378</u>	<u>10,548</u>	<u>93,926</u>
Total	<u>\$118,670,816</u>	<u>\$ 31,208,039</u>	<u>\$149,878,855</u>

Debt service reimbursements are accounted for as expenditures of the "Administration of Highways Division" program on the Governmental Funds statement of revenues and expenditures--budget and actual--State Highway Fund (non-GAAP budgetary basis) and are accounted for as "Operating transfers out" of the State Highway Fund on the Governmental Funds statement of revenues, expenditures, and changes in fund balances. Reimbursement payments consisted of \$17,781,182 for principal and \$6,712,909 for interest for the year ended June 30, 2002.

Transfer of Funds to Airports

In fiscal year 1991, the Airports Division transferred \$250,000,000 to the Highways Division of the Department of Transportation, pursuant to Act 309, SLH 1989, as amended. The funds were transferred to be used by the Highways Division for certain highway projects within 10 miles by road of an airport. During fiscal year 2002, the Highways Division transferred the remaining balance of approximately \$17,100,000 back to the Airports Division.

11. RECONCILIATIONS OF GOVERNMENTAL FUNDS AND GOVERNMENT-WIDE FINANCIAL STATEMENTS

The following schedule reconciles the Governmental Funds fund balances to the government-wide net assets:

Total Governmental Funds fund balances	\$ 362,320,197
Amounts reported as net assets for government-wide reporting are different because:	
Capital assets used in governmental activities are not financial resources and therefore are not reported in the Governmental Funds financial statements.	5,892,873,882
Bond issuance costs are recorded as expenditures in Governmental Funds financial statements when the costs are first incurred. However, in the government-wide financial statements, such amounts are recorded as a deferred charge and amortized over the life of the related bonds.	694,599
Long-term liabilities are not due and payable in the current period and therefore are not reported in the Governmental Funds financial statements:	
Accrued vacation	(8,944,947)
Accrued workers' compensation	(4,631,047)
Revenue bonds payable	(276,625,000)
Premium on revenue bonds	(2,698,319)
Revenues and the related receivables from government contracts are recorded on the modified accrual basis for Governmental Funds financial statements and on the accrual basis for government-wide financial statements.	<u>6,573,641</u>
Total government-wide net assets	<u><u>\$ 5,969,563,006</u></u>

The following schedule reconciles the Governmental Funds change in fund balances to the government-wide change in net assets:

Governmental Funds change in fund balances	\$ 44,768,373
Amounts reported for governmental activities in the statement of net assets are different because:	
Governmental Funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This amount includes the adjustment for capital outlay of \$121,471,568 offset by depreciation expense of \$230,705,793 in the current period.	(109,234,225)
Repayment of bond principal is reported as an expenditure in the Governmental Funds, but the repayment reduces long-term liabilities in the statement of net assets.	8,000,000
Bond proceeds provide current financial resources to governmental funds, but issuing debt and related original issue premium increases long-term liabilities in the statement of net assets. This amount includes the amortization of revenue bond premium of \$89,274 in the current period.	(72,698,319)
Bond issue costs are reported as expenditures in the governmental funds as they require the use of current financial resources. However, in the statement of activities, these expenses are allocated over the remaining life of the related bond and reported as an offset to interest expense. This amount includes bond issue costs of \$717,580 offset by amortization expense of \$22,981 in the current period.	694,599
Government Funds report the full amount of the proceeds from a capital asset sale. However, in the statement of activities, the sale of capital assets are reported only to the extent of the difference between the selling price and the carrying value of the asset sold. The Highways Division did not receive any cash for disposed assets with carrying value of \$376,162.	(376,162)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in Governmental Funds.	6,573,641
Expenses in the statement of activities that do not use current financial resources are not reported as expenditures in Governmental Funds.	<u>(1,232,348)</u>
Government-wide change in net assets	<u>\$ (123,504,441)</u>

12. RESTATEMENTS OF FUND BALANCES / NET ASSETS

The following schedule reconciles the June 30, 2001 fund balances / net assets, as previously reported, to the fund balance / net assets, as restated, to include the adoption of new pronouncements:

	State Highway Fund	Capital Projects Fund	Total
Fund balances as of June 30, 2001	\$ 168,209,824	\$ 148,660,700	\$ 316,870,524
Prior period adjustments, Governmental Funds - changes in accounting principle:			
Interfund cash transfers currently recorded as interfund loans	12,739,791	(12,739,791)	
Expenditures for land parcels held for sale currently recorded as an asset	<u>681,300</u>	<u> </u>	<u>681,300</u>
Fund balances, as restated	181,630,915	135,920,909	317,551,824
Prior period adjustments, government-wide financial statements - changes in accounting principle:			
Capitalization of capital assets, net			6,002,484,269
Recording of unmatured revenue bonds payable			(214,625,000)
Liability recognition:			
Accrued vacation			(8,307,646)
Workers' compensation			<u>(4,036,000)</u>
Beginning net assets, as restated			<u>\$ 6,093,067,447</u>

13. PENSION INFORMATION

Employees' Retirement System ("ERS")

All full-time employees of the Highways Division are eligible to participate in the ERS, a cost-sharing multiple-employer public employee retirement system established to administer a pension benefit program for all state and county employees. The ERS was established by Chapter 88 of the HRS and is governed by a Board of Trustees. All contributions, benefits and eligibility requirements are established by Chapter 88 of the HRS and can be amended by legislative action.

The ERS is composed of a contributory retirement plan and a noncontributory retirement plan. Eligible employees who were in service and a member of the existing contributory plan on June 30, 1984, were given an option to remain in the existing plan or join the noncontributory plan, effective January 1, 1985. All new eligible employees hired after June 30, 1984, automatically become members of the noncontributory plan. Both plans provide death and disability benefits and cost of living increases. Benefits are established by state statute. In the contributory plan, employees may elect normal retirement at age 55 with 5 years of credited service or elect early retirement at any age with 25 years of credited service. Such employees are entitled to retirement benefits, payable monthly for life, of 2% of their average final salary, as defined, for each year of credited service. Benefits fully vest on reaching five years of service; retirement benefits are actuarially reduced for early retirement. Covered contributory plan employees are required by state statute to contribute 7.8% of their salary to the plan;

the Highways Division is required by state statute to contribute the remaining amounts necessary to pay contributory plan benefits when due. In the noncontributory plan, employees may elect normal retirement at age 62 with 10 years of credited service or at age 55 with 30 years of credited service, or elect early retirement at age 55 with 20 years of credited service. Such employees are entitled to retirement benefits, payable monthly for life, of 1.25% of their average final salary, as defined, for each year of credited service. Benefits fully vest on reaching 10 years of service; retirement benefits are actuarially reduced for early retirement. The Highways Division is required by state statute to contribute all amounts necessary to pay noncontributory plan benefits when due.

The Highways Division's contribution to the ERS for fiscal years 2002, 2001, and 2000 was approximately \$11,000, \$22,000, and \$2,233,000, respectively, and represented the required contributions for each year. Actual contributions paid by the Highways Division equal contributions required by the ERS.

The ERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to the ERS, 201 Merchant Street, Suite 1400, Honolulu, Hawaii, 96813 or by calling (808) 586-1660.

Post-Retirement Health Care and Life Insurance Benefits

In addition to providing pension benefits, the State provides certain health care (medical, prescription drug, vision, and dental) and life insurance benefits for retired employees. Contributions are based upon negotiated collective bargaining agreements and are limited by state statute to the actual cost of benefit coverage. The Highways Division pays for 100% of these benefits for employees who have at least 10 years of service. The Highways Division's share of the cost of these benefits is pro-rated for employees with less than 10 years of service. The Highways Division also reimburses Medicare expenses of retirees and qualified spouses (through the State) who are at least 62 years of age and have at least 10 years of service. Contributions are based upon negotiated collective bargaining agreements and are limited by state statute to the actual cost of benefit coverage. The amounts allocated to the Highways Division for fiscal year 2002 aggregated approximately \$209,000.

14. TRANSACTIONS WITH OTHER GOVERNMENT AGENCIES

The State assesses a surcharge of 5% for central service expenses on all receipts of the State Highway Fund, after deducting any amounts pledged, charged or encumbered, for the payment of bonds and interest during the year. The assessments amounted to approximately \$7,187,000 in fiscal year 2002.

The Highways Division is assessed a percentage of the cost of the general administration expenses of the Department. The assessments amounted to approximately \$4,857,000. During fiscal year 2002, the Highways Division received assessment refunds from the Department amounting to approximately \$1,202,000, resulting in a net general administration expense of approximately \$3,655,000.

15. OPERATING LEASES

Rental expenditures

The Highways Division leases office and baseyard space under various long-term operating lease agreements expiring at various dates through fiscal year 2019 and beyond. Scheduled minimum rental payments for succeeding fiscal years ending June 30 are as follows:

Year ending June 30:	
2003	\$ 828,708
2004	828,708
2005	828,708
2006	828,708
2007	828,708
2008-2012	4,143,540
2013-2017	4,143,540
2018-2019	<u>1,104,944</u>
Total	<u>\$13,535,564</u>

The total rental expenditures during fiscal year 2002 for operating leases were \$828,708.

Rental revenues

The Highways Division also leases various Highways owned properties under noncancellable long-term lease agreements that expire through fiscal year 2043 and beyond. Scheduled minimum revenues for succeeding fiscal years ending June 30 are as follows:

Year ending June 30:	
2003	\$ 317,672
2004	317,672
2005	317,672
2006	317,672
2007	317,672
2008-2012	1,588,360
2013-2017	1,588,360
2018-2022	1,477,410
2023-2027	1,429,860
2028-2032	600,860
2033-2037	442,182
2037-2042	362,100
2043	<u>3,025</u>
Total	<u>\$9,080,517</u>

16. COMMITMENTS

Condemnation Proceedings

The Highways Division occasionally finds it necessary to condemn property for construction of highways. These proceedings require the Highways Division to compensate the existing property owner for the fair market value of the real property. Prior to the determination of the fair market value, the Highways Division is required to deposit funds in State courts for these proceedings. Such funds deposited may not be sufficient to cover the full amount required for compensation purposes. Management, however, believes any additional compensation in excess of amounts deposited with State courts will not be material to the financial statements of the Highways Division.

Deferred Compensation Plan

The State established a deferred compensation plan ("plan") in accordance with Section 457 of the Internal Revenue Code, which enables State employees to defer a portion of their compensation. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

All amounts of compensation deferred under the plan, as well as property and rights purchased with those amounts and income attributable to these amounts, are held in trust by third-party agents for the exclusive benefit of participants and their beneficiaries. The assets and liabilities of the plan are not reflected in the State or Highways Division financial statements.

Sick Pay

Sick leave accumulates at the rate of one and three-quarters working days for each month of service without limit. It may be taken only in the event of illness and is not convertible to pay upon termination of employment. Accordingly, no liability for sick pay is recorded. However, a state employee who retires or leaves government service in good standing with 60 days or more of unused sick leave is entitled to additional service credits in the ERS. Accumulated sick leave at June 30, 2002 aggregated approximately \$19,719,000.

17. RISK MANAGEMENT

Property and Liability Insurance

The State maintains certain insurance coverages to satisfy bond indenture agreements as well as for other purposes, but is substantially self-insured for all other perils. The State records a liability for risk financing and insurance related losses, including incurred but not reported, if it is determined that a loss has been incurred and the amount can be reasonably estimated. The State retains various risks and insures certain excess layers with commercial insurance companies.

Workers' Compensation

The State is self-insured for workers' compensation. Accordingly, the Highways Division is liable for workers' compensation claims filed by its employees. Liabilities for workers' compensation claims are established if information indicates that it is probable that liabilities have been incurred and the amount of those claims can be reasonably estimated. The basis for estimating the liabilities for unpaid claims include the effects of specific incremental claim adjustment expenses, salvage and subrogation, and

other allocated or unallocated claim adjustment expenses. These liabilities include an amount for claims that have been incurred but not reported. The workers' compensation reserve amounted to \$4,631,000 at June 30, 2002.

18. CONTINGENT LIABILITIES AND OTHER

Litigation

The State is the defendant in lawsuits seeking damages allegedly related to State highways and highway construction contracts. While the ultimate liabilities, if any, in the disposition of these matters are presently difficult to estimate, it is management's belief that the outcomes are not likely to have a material adverse effect on the Highways Division's financial position. In addition, the State has not determined whether the ultimate liabilities, if any, will be imposed on the State Highway Fund. Accordingly, no provisions for any liabilities that might result have been made in the accompanying financial statements.

19. DEFICIT BALANCE

At June 30, 2002, the Capital Projects Fund had an unreserved deficit balance of \$2,720,006. The Highways Division intends to take corrective action to eliminate this deficit balance.

20. SUBSEQUENT EVENT

The Highways Division intends to issue \$45.7 million of revenue bonds, which will be used to refund certain previously issued bonds still outstanding. The issuance is expected to take place in April 2003.

* * * * *

PROPOSED FORM OF BOND COUNSEL OPINION

[Closing Date]

State of Hawaii
Honolulu, Hawaii

Re: \$_____ State of Hawaii
Highway Revenue Bonds, Refunding Series 2003

We have served as bond counsel with respect to the issuance by the State of Hawaii (the "State") of \$_____ aggregate principal amount of its bonds designated the State of Hawaii Highway Revenue Bonds, Refunding Series 2003 (the "2003 Bonds"), dated as of _____, 2003. The 2003 Bonds are issued under the Constitution and statutes of the State, including particularly Part III of Chapter 39, Hawaii Revised Statutes, as amended (the "Act"), and under and pursuant to the Certificate of the Director of Transportation of the State, dated as of August 1, 1993 (the "Master Certificate"), as heretofore amended and supplemented and as further amended and supplemented by the Sixth Supplemental Certificate of said Director, dated as of _____, 2003 (the "Sixth Supplemental Certificate" and, together with the Master Certificate, the "Certificate"). All capitalized terms used and not otherwise not defined herein shall have the meanings set forth in the Certificate.

In our capacity as bond counsel, we have reviewed the Certificate, the Tax Certificate of the State of even date herewith (the "Tax Certificate") and such other certificates, records, opinions and documents delivered in connection with the issuance of the 2003 Bonds as we deemed necessary for purposes of the opinions expressed herein (collectively, the "Bond Documents"). We have assumed the genuineness of all Bond Documents presented to us as originals, conformity to the originals of all Bond Documents presented to us as copies, and the due execution and delivery of all Bond Documents by, and validity and enforceability thereof against, each party thereto other than the State. We have also assumed, without independent investigation, the accuracy of all representations and certifications and the correctness of all legal opinions set forth in the Bond Documents.

With respect to our opinion as to federal tax matters (as set forth in Paragraph 3 below), we have assumed (without independent investigation, as aforesaid) the accuracy of the representations and certifications of the State in the Certificate and Tax Certificate as to certain facts, circumstances, estimates and expectations which are material to the exclusion of interest on the 2003 Bonds from gross income under the Internal Revenue Code of 1986, as amended (the "Code"). We have further assumed compliance with all covenants and agreements of the State under the Certificate and the Tax Certificate to comply with all requirements of the Code which must be satisfied subsequent to the issuance of the 2003 Bonds in order for the interest on the 2003 Bonds to be and to remain excluded from gross income for federal income tax purposes under the Code.

We call attention to the fact that the rights and obligations under the Bonds and the Bond Documents, and the enforceability of such rights and obligations, may be subject to bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles and to applicable limitations on legal remedies against counties in the State of Hawaii.

Based upon and subject to the foregoing, and in reliance thereon, we are of the opinion that:

1. The 2003 Bonds constitute valid and binding special obligations of the State, payable solely from and secured solely by the Pledged Funds under the Certificate.
2. The Sixth Supplemental Certificate has been duly executed and delivered by the Director of Transportation and constitutes the valid and binding obligation of the State. The Certificate creates a

valid pledge of the Pledged Funds, subject to the provisions of the Certificate permitting the application of such Pledged Funds for the purposes and on the terms and conditions specified in the Certificate.

3. Interest on the 2003 Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Code, as presently enacted and construed. Interest on the 2003 Bonds is not an item of tax preference under the Code for purposes of the alternative minimum tax imposed on individuals and corporations, but we note that such interest is included in adjusted current earnings of certain corporations for purposes of computing their alternative minimum tax liability under the Code.
4. Under the laws of the State, as presently enacted and construed, the 2003 Bonds and the income therefrom are exempt from all taxation by the State or any county or other political subdivision thereof, except inheritance, transfer and estate taxes, and certain franchise taxes imposed on banks and other financial institutions.

Except as stated in paragraphs 3 and 4 above, we express no opinion as to any federal or state tax consequences relating to the ownership or disposition of the 2003 Bonds or to the accrual or receipt of interest thereon.

In our capacity as bond counsel, we have not been retained to express, and do not express, any opinion as to the accuracy, adequacy or completeness of any official statement or other offering documents used in connection with the offer and sale of the 2003 Bonds.

Our engagement with respect to the 2003 Bonds has concluded with the issuance thereof. We have assumed no obligation to revise or supplement this opinion letter to reflect any changes in law or other facts or circumstances which may come to our attention after the date hereof.

Very truly yours,

McCORRISTON MILLER MUKAI MacKINNON LLP

CONTINUING DISCLOSURE CERTIFICATE

This Continuing Disclosure Certificate (this "Disclosure Certificate") is executed and delivered by the State of Hawaii (the "State"), acting by and through the State Director of Transportation, in connection with the issuance of \$44,940,000 State of Hawaii Highway Revenue Bonds, Refunding Series 2003 (the "2003 Bonds"). The 2003 Bonds are being issued pursuant to the authority of the Constitution and laws of the State, including, in particular, certain acts of the Legislature of the State and that certain Certificate of the Director of Transportation Providing for the Issuance of the State of Hawaii, Highway Revenue Bonds dated as of August 1, 1993, as supplemented and amended by the Sixth Supplemental Certificate of the Director of Transportation providing for the Issuance of the State of Hawaii, Highway Revenue Bonds, Series 2003, dated as of March 25, 2003 (collectively the "Bond Certificate").

Pursuant to Section 7.04 of the Sixth Supplemental Certificate, the State, acting by and through its Director of Transportation, agrees as follows:

Section 1. Purpose of Disclosure Certificate. This Disclosure Certificate is being executed and delivered by the State for the benefit of the Bondholders and Beneficial Owners of the 2003 Bonds and in order to assist the Participating Underwriter in complying with Securities and Exchange Commission Rule 15c2-12(b)(5).

Section 2. Definitions. In addition to the definitions set forth in the Bond Certificate, which apply to any capitalized term used in this Disclosure Certificate unless otherwise defined in this Section, the following capitalized terms shall have the following meanings:

"Annual Information" means the type of financial information and operating data set forth under the subheadings "REVENUE SOURCES - Historical Revenues", "DEBT SERVICE COVERAGE- Bond Debt Service" (where there is a change other than from scheduled principal maturities) and "INFORMATION RELATING TO REVENUE SOURCES" in Appendix B in the final Official Statement, dated _____, 2003, for the 2003 Bonds.

"Audited Financial Statements" means the audited financial statements of the State Highway Fund and any other fund of the State into which Revenues are deposited, prepared in accordance with generally acceptable accounting principles as promulgated from time to time by the Government Accounting Standards Board and the Financial Accounting Standards Board of the Financial Accounting Foundation.

"Beneficial Owner" shall mean any person which (a) has the power, directly or indirectly, to vote or consent with respect to, or to dispose of ownership of, any 2003 Bonds (including persons holding 2003 Bonds through a Clearing Agency, nominees, depositories or other intermediaries), or (b) is treated as the owner of any 2003 Bonds for federal income tax purposes.

"Dissemination Agent" shall mean the Director of Finance or any successor Dissemination Agent designated in writing by the Director of Finance and which has filed with the Director of Finance a written acceptance of such designation.

"Filing Date" means the first day of the tenth month following the end of each Fiscal Year (or the next succeeding business day if that day is not a business day).

"Fiscal Year" means each fiscal year of the Department of Transportation commencing on July 1 of each calendar year and ending on June 30 of the immediately succeeding calendar year.

"Listed Events" shall mean any of the events listed in subsection 4(a) of this Disclosure Certificate.

“National Repository” shall mean any Nationally Recognized Municipal Securities Information Repository as recognized from time to time by the SEC for purposes referred to in the Rule. This National Repositories currently approved by the Securities and Exchange Commission are set forth at www.sec.gov/info/municipal/nrmsir.htm.

“Participating Underwriter” shall mean the original underwriter of the 2003 Bonds required to comply with the Rule in connection with offering of the 2003 Bonds.

“Repositories” shall mean each National Repository and each State Repository.

“Rule” shall mean Rule 15c2-12(b)(5) adopted by the Securities and Exchange Commission under the Securities and Exchange Commission under the Securities Exchange Act of 1934, as the same may be amended from time to time.

“State” shall mean the State of Hawaii.

“State Repository” shall mean any public or private repository or entity designated by the State as a state repository for the purpose of the Rule and recognized as such by the Securities and Exchange Commission. As of the date of this Disclosure Certificate, there is no State Repository.

Section 3. Filing of Annual Information and Audited Financial Statements.

- (a) The State is the only “obligated person” (as defined in the Rule) for the 2003 Bonds.
- (b) The State shall provide, or shall cause the Dissemination Agent to provide, to each Repository:
 - (i) Annual information for the preceding fiscal year, and unaudited financial statements of the Pledged Funds if Audited Financial Statements are not provided at the same time, not later than the Filing Date for each fiscal year; and
 - (ii) Audited Financial Statements for the preceding fiscal year, not later than the later of (A) the Filing Date for each fiscal year or (B) 30 days after receipt thereof by the Department of Transportation.

Audited Financial Statements are expected to be available together with the Annual Information. The State is required to deliver, or cause to be delivered, such information in such manner and by such time so that the Repositories receive the information on or before the date specified.

The Annual Information may be submitted as a single document or as separate documents comprising a package and may cross-reference other information including official statements of debt issues of the State or related public entities, which have been submitted to each of the Repositories or the Securities and Exchange Commission. If the document included by reference is a final official statement, it must be available from the Municipal Securities Rulemaking Board. The State shall clearly identify each such other document so included by reference. The Audited Financial Statements may be submitted separately from the Annual Information.

If the Department’s fiscal year changes, it shall give notice of such change in the same manner as for a Listed Event under subsection 4(b).

(c) If the State is unable to provide to the Repositories the information described in subsection (b) by the Filing Date, the Director of Finance shall send a notice to each Repository and the Municipal Securities Rulemaking Board in substantially the form attached as Exhibit A.

(d) If the Director of Finance has appointed a Dissemination Agent, then not later than 15 Business Days prior to Filing Date, the Director of Transportation shall provide the Annual Information and Audited Financial

Statements (or unaudited financial statements if the Audited Financial Statements are not available) to the Dissemination Agent.

(e) The Dissemination Agent shall:

- (i) determine each year prior to the Filing Date the name and address of each National Repository and the State Repository, if any; and
- (ii) if the Dissemination Agent is other than the Director of Finance, file a report with the Director of Finance certifying that the information described in subsection (b) has been provided pursuant to this Disclosure Certificate, stating the date it was provided and listing all the Repositories to which it was provided.

Section 4. Reporting of Significant Events.

(a) Pursuant to the provisions of this Section 4, the State shall give, or cause to be given, notice of the occurrence of any of the following events with respect to the 2003 Bonds, if material:

1. principal and interest payment delinquencies;
2. non-payment related defaults;
3. modifications to rights of Bondholders,
4. bond calls other than scheduled mandatory sinking fund redemptions;
5. defeasances;
6. rating changes;
7. adverse tax opinions or events affecting the tax-exempt status of the 2003 Bonds;
8. unscheduled draws on the debt service reserves reflecting financial difficulties;
9. unscheduled draws on the credit enhancements reflecting financial difficulties;
10. substitution of the credit or liquidity providers or their failure to perform; or
11. release, substitution or sale of property securing repayment of the 2003 Bonds.

(b) Whenever the Director of Transportation or other responsible officials of the State become aware of the occurrence of a Listed Event, the State shall as soon as possible determine if such event would be material under applicable federal securities laws and, if so, the State shall prepare and provide or cause to be provided notice of such occurrence to each Repository.

Notwithstanding the foregoing, notice of Listed Events described in subsections (a)(4) and (5) above need not be given under this subsection (b) any earlier than the notice (if any) of the underlying event is given to Bondholders of affected 2003 Bonds pursuant to the Bond Certificate.

Section 5. Termination of Reporting Obligation. The State's obligations under this Disclosure Certificate shall terminate (a) upon the legal defeasance, prior redemption or repayment in full of all of the 2003 Bonds or (b) when the Rule no longer applies to these 2003 Bonds. If such termination occurs prior to the final maturity of the 2003 Bonds, the State shall give notice of such termination in the same manner as for a Listed Event under subsection 4(b).

Section 6. Dissemination Agent. The Director of Finance may, from time to time, appoint or engage a Dissemination Agent to assist the State in carrying out its obligations under this Disclosure Certificate, and may discharge

any such Agent, with or without appointing a successor Dissemination Agent. The Dissemination Agent shall not be responsible in any manner for the content of any notice or report prepared by the State pursuant to this Disclosure Certificate.

Section 7. Amendment; Waiver; Amendment to Accounting Principles to be Followed.

(a) Notwithstanding any other provision of this Disclosure Certificate, the State may amend this Disclosure Certificate, and any provision of this Disclosure Certificate may be waived, provided that the following conditions are satisfied:

(i) If the amendment or waiver relates to the definition of “Annual Information” or the provisions of subsection 3(a) or (b), or Section 5, it may only be made in connection with a change in circumstances that arises from a change in legal requirements, change in law, or change in the identity, nature or status of the Obligated Person with respect to the 2003 Bonds, or the type of business conducted by the Obligated Person;

(ii) The undertaking, as amended or taking into account such waiver, would, in the opinion of nationally recognized bond counsel selected by the State, have complied with the requirements of the Rule at the time of the original issuance of the 2003 Bonds, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances; and

(iii) The amendment or waiver either (i) is approved by the Holders of the 2003 Bonds in the same manner as provided in the Bond Certificate for amendments to the Bond Certificate with the consent of Holders of the 2003 Bonds, or (ii) does not, in the opinion of nationally recognized bond counsel selected by the State, materially impair the interests of the Holders or Beneficial Owners of the 2003 Bonds.

(b) In the event of any amendment or waiver of a provision of this Disclosure Certificate, the State shall describe such amendment in the next Annual Information, and shall include, as applicable, a narrative explanation of the reason for the amendment or waiver and its impact on the type (or in the case of a change of accounting principles, on the presentation) of the information being presented by the State.

(c) If the amendment changes the accounting principles to be followed in preparing financial statements from that specified in the definition of Audited Financial Statements, then (i) the State shall give notice of such amendment in the same manner as for a Listed Event under subsection 4(b), and (ii) the Annual Information for the year in which the change is made should present a comparison (in narrative form and also, if feasible, in quantitative form) between the financial statements as prepared on the basis of the amended definition of accounting principles and those prepared on the basis of the former definition of accounting principles.

Section 8. Additional Information - Supplements. (a) Nothing in this Disclosure Certificate shall be deemed to prevent the State from disseminating any other information, using the means of dissemination set forth in this Disclosure Certificate or any other means of communication, or including any other information in any Annual Information or notice of occurrence of a Listed Event, in addition to that which is required by this Disclosure Certificate.

If the State chooses to include any information in any Annual Information or notice of occurrence of a Listed Event in addition to that which is specifically required by this Disclosure Certificate, the State shall have no obligation under this Disclosure Certificate to update such information or include it in any future Annual Information or notice of occurrence of a Listed Event.

(b) Nothing in this Disclosure Certificate shall be deemed to prevent the State from supplementing this Disclosure Certificate to provide that it shall also govern continuing disclosure for one or more issues of Additional Bonds (as defined in the Bond Certificate).

Section 9. Failure to Perform.

(a) The agreements of the State set forth in Sections 3 and 4 of this Disclosure Certificate are intended to be for the benefit solely of the Bondholders and Beneficial Owners from time to time of the 2003 Bonds.

The sole remedy for any breach of this Disclosure Certificate by the State shall be limited, as hereinafter described, to a right of Bondholders and Beneficial Owners to cause proceedings at law or in equity to be instituted and maintained to obtain mandamus or specific performance by the State of its obligations hereunder. Any individual Bondholder or Beneficial Owner may institute and maintain, or cause to be instituted and maintained, such proceedings to require the State to provide or cause to be provided a pertinent filing if such a filing is due and has not been made. Any such proceedings challenging the adequacy of the information provided in accordance with this Disclosure Certificate may be instituted and maintained only by the Bondholders and the Beneficial Owners of not less than 25% in principal amount of the 2003 Bonds then outstanding or their agent.

(b) Any failure of the State to comply with any provisions of this Disclosure Certificate shall not be a default or an event of default with respect to the 2003 Bonds under the Bond Certificate.

Section 10. Beneficiaries. This Disclosure Certificate shall inure solely to the benefit of the State, the Dissemination Agent, the Participating Underwriter and Bondholders and Beneficial Owners from time to time of the 2003 Bonds and shall create no rights in any other person or entity.

Section 11. Recordkeeping. The Director of Finance shall maintain records of all Annual Information and notice of material Listed Events including the content of such disclosure, the names of the entities with whom such disclosures were filed and the date of filing such disclosure.

Section 12. Governing Law. This Disclosure Certificate shall be governed by the laws of the State.

Dated _____, 2003.

STATE OF HAWAII

By:
Title: