2002 ANNUAL REPORT

SPECIAL PURPOSE REVENUE BONDS
AUTHORIZED UNDER

ACT 262
SESSION LAWS OF HAWAII 1998

AND

ACT 257
SESSION LAWS OF HAWAII 1999

PUBLIC UTILITIES COMMISSION
DEPARTMENT OF BUDGET AND FINANCE
STATE OF HAWAII

JUNE 2003
Section 2 of Act 262 1998 and Section 2 of Act 257 1999 authorize the issuance of special purpose revenue bonds (“SPRBs”) by the State of Hawaii Department of Budget and Finance (“B&F”) to assist utilities serving the general public with the financing of multi-purpose capital improvement programs for the local furnishing of electric energy and gas.

Pursuant to Section 2 of Act 262 1998 and Section 2 of Act 257 1999, the approval of the Public Utilities Commission (“Commission”) is required for projects funded with the bond proceeds.

Pursuant to Section 3 of Act 262 1998 and Section 3 of Act 257 1999, the Commission is required to report annually on the progress in reducing the financing costs of electric and gas utilities through the use of SPRBs. The reports must also include: (1) the cost of the bonds at the time of issue in comparison to the cost of financing through conventional loans; (2) the estimated benefits derived from the use of SPRBs; and (3) a listing of capital improvement projects to be funded by SPRBs.

Accordingly, this report presents a summary of bond financing under the aforesaid acts. It covers acts with authorization periods in effect or with funds in trustee accounts during the 2002 calendar year.

**PROGRESS IN REDUCING FINANCING COSTS WITH SPRBs**

The following table displays the authorization period for bond financing, the qualifying electric and gas utilities, and the total principal amounts in SPRBs authorized and issued under each act, as of December 31, 2002.

The total issued amounts are also presented in the last column as percentages of the authorized amounts.
SPRBs Authorized and Issued as of 12/31/02
($ thousands)

<table>
<thead>
<tr>
<th>Act</th>
<th>Utility*</th>
<th>Total Authorized</th>
<th>Total Issued</th>
<th>Total %**</th>
</tr>
</thead>
<tbody>
<tr>
<td>Act 262 1998***</td>
<td>HECO</td>
<td>$ 75,000</td>
<td>$ 75,000</td>
<td>100%</td>
</tr>
<tr>
<td>(7/20/98 - 12/31/03)</td>
<td>HELCO</td>
<td>25,000</td>
<td>-0-</td>
<td>-0-</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>$ 100,000</td>
<td>$ 75,000</td>
<td>75%</td>
</tr>
<tr>
<td>Act 257 1999</td>
<td>TGC</td>
<td>$ 19,600</td>
<td>$ 19,600</td>
<td>100%</td>
</tr>
<tr>
<td>(7/1/99 - 12/31/02)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

* HECO (Hawaiian Electric Company, Inc.), HELCO (Hawaii Electric Light Company, Inc.) and TGC (The Gas Company, division of Citizens Communications Company).

** The total issued amount as a percentage of the total authorized amount.


The status of bond financing under the Acts is reported in the attached Exhibit A. Among other things, Exhibit A lists each bond series under the Acts and the principal amounts issued in one or more series for each utility.

As shown in Exhibit A, 2002 SPRB issues consisted of Series 2002A, issued on behalf of HECO under Act 262 1998.

Act 262 1998 authorized the issuance of $25 million in SPRBs on behalf of HELCO for multi-project capital improvement program, including the acquisition of land, facilities used to produce electricity (including two new fossil fuel generating units on the island of Hawaii), transmission and distribution facilities, and other electric systems and facilities, or any combination thereof. Pursuant to Act 262 1998, the authorization to issue SPRBs lapses on December 31, 2003. In 2002, the Commission did not receive filings relating to any bonds issued on behalf of HELCO under Act 262 1998.

**COMPARISON OF COSTS AND SAVINGS**

Exhibit A also presents the interest rates of SPRBs in comparison with the interest rates of equivalent taxable debt (first mortgage bonds or unsecured notes), the estimated savings in interest expense on annual and 30-year or 20.5-year bases, and the status of the construction funds held in trustee accounts.

As shown in greater detail in Exhibit A, the estimated savings in interest expense under each act is as follows:
Estimated Savings in Interest Expense as of 12/31/02
($ Thousands)

<table>
<thead>
<tr>
<th>Act</th>
<th>Annual</th>
<th>30-Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Act 262 1998</td>
<td>$ 1,077.5</td>
<td>$ 32,325.0</td>
</tr>
<tr>
<td>Act 257 1999</td>
<td>$ 915.3</td>
<td>$ 18,764.1</td>
</tr>
</tbody>
</table>

(Variances in figures between annual and 30-year interest savings are due to rounding. For Act 257 1999, interest expense savings is on 20.5-year basis as the bonds mature in 20.5 years, on December 1, 2020.)

The overall savings under each act may reflect a number of variables associated with bond financing, such as taxes, issuance costs, trustee fees, deferred taxes, and the refunding (redemption) of bonds before maturity.

**BENEFITS OF USING SPRBs**

SPRB loans offer electric and gas utility companies a lower interest rate alternative to other forms of debt on borrowings needed to provide essential public energy facilities. Because the interest earned by SPRB purchasers is exempt from federal and state income taxes, the bonds can bear a lower interest rate than taxable debt with equivalent characteristics (maturity dates, call provisions etc.). In addition, revenue bonds generally have lower underwriting fees. As a result of the interest savings, the utility’s capital finance costs are lower than they otherwise would be. These savings ultimately benefit electric and gas utility customers in the form of lower electric and gas rates set by the Commission.

**LISTING OF CAPITAL IMPROVEMENT PROJECTS**

Lists of capital improvement projects to be funded by bond proceeds under each of the Acts were exhibited in previous SPRB annual reports as shown below:

<table>
<thead>
<tr>
<th>Act</th>
<th>SPRB Annual Report</th>
</tr>
</thead>
<tbody>
<tr>
<td>Act 262 1998</td>
<td>1999</td>
</tr>
<tr>
<td>Act 257 1999</td>
<td>1999</td>
</tr>
</tbody>
</table>

In 1999, the Commission approved HECO projects to be funded, in part, from the proceeds of the sale of up to $75 million of SPRBs authorized by Act 262 1998. These projects are listed in Exhibit B of this report. The total cost of these projects exceeds the authorized bond amounts authorized by Act 262 1998 to allow for changes in the timing or scope of individual projects. In 2002, the Commission approved HECO’s supplemental projects and participation in the sale of up to $40 million of SPRBs authorized by Act 262 1998. These supplemental projects are listed in Exhibit C and are in addition to the projects listed...
in Exhibit B. The cost of these supplemental projects, totaling approximately $150 million, are to be funded, in part, with the proceeds of the sale of SPRBs issued under Act 262 1998.

To track the use of bond proceeds, the Commission requires the electric utilities to file quarterly and annual reports on the projects funded and the amounts used. These records are maintained at the Commission.